AFFIDAVIT OF M. SORNARAJAH

I, Muthucumaraswamy Sornarajah, of the Republic of Singapore HEREBY AFFIRM that:

1. I am currently a Professor at the Faculty of Law of the National University of Singapore, a Fellow at the Centre for Energy, Petroleum and Mineral Law and Policy at the University of Dundee, Scotland, and a Solicitor of the High Court of England and Wales.

2. I have dedicated much of my legal and teaching career to the subject of international investment law, and have written and lectured extensively on the subject. A list of my publications on the topic is included in my Curriculum Vitae, which is attached as Exhibit “A” to this affidavit.

3. I have also served as a consultant to the United Nations Conference on Trade and Development on Multilateral Investment Treaties and to the United Nations Development Programme. I am Director of the

4  During my career, I have served as: the Head of the Law School of the University of Tasmania, Australia; a Stirling Fellow at the Yale Law School; a Visiting Fellow at the Research Centre for International Law, University of Cambridge; a Research Fellow at the Max-Planck-Institut für ausländisches öffentliches Recht und Völkerrecht in Heidelberg, Germany; and as a visiting professor at the Washington College of Law, American University at Washington.


6  *The International Law on Foreign Investment*, presents a survey of public international law applicable to the protection of foreign investment. The book examines a variety of techniques adopted by states for attracting foreign investment and for ensuring that foreign investment serves their economic objectives. The work compares foreign investment legislation and regulations, and assesses their legality in light of international norms. It considers the changing perceptions of foreign investment and the new forms of foreign investment that have emerged from these changes. The book identifies the risks to foreign investment and surveys the effectiveness of different methods of risk avoidance. In considering these issues I have taken account not only of the law, but also of the relevant literature in economics, political science and other associated disciplines. A second edition of this book will be published this year by Cambridge University Press.

7  *The Settlement of Foreign Investment Disputes* draws on the experience gained from a broad spectrum of successful negotiation, arbitration, and litigation techniques and provides a comprehensive, critical survey of the principal methods of settling foreign investment disputes. The book treats the subject systematically, dealing first with the internal balances within modern foreign investment contracts, the complexities that arise due to state participation or interference in these contracts, and the stances that are
taken when disputes arise. It goes on to examine, in turn, the main issues involved in negotiation, arbitration, and judicial settlement as the methods of settling foreign investment disputes, discussing the controversial themes in each of these methods in detail. Recognizing that the focus of attention is shifting to the misconduct of multinational corporations, the last chapter contains a discussion of the role of domestic courts.

8 I was counsel for the Claimant in *Yaung Chi Oo Ltd v The Republic of Myanmar*. I was arbitrator along with Judge Stephen Schwebel and Ambassador Cardenas in *Phaiton Energy Corporation v Listrik Negara Indonesia and the Republic of Indonesia*. I have been sole arbitrator and consultant in various arbitrations.

9 I have also written extensively in the fields of commercial arbitration and public international law.

10 For these reasons, I have knowledge of the matters to which I hereinafter depose.

**Overview**

11 I have been asked to provide an overview of the development of international investment treaties which describes their historical foundations and their importance in the context of international and domestic law.

12 The following affidavit is organized into four parts. Part I traces the historical developments leading to the establishment of international investment treaties, the earliest examples of which were negotiated in the mid twentieth century. Part II describes the investment provisions of the *North American Free Trade Agreement* ("NAFTA") and provides a brief description of the nature of the claims that have been brought by foreign investors under the dispute settlement provisions of Chapter Eleven of that Treaty (hereinafter referred to as "investor-State arbitration"). Part III discusses the significance of these developments for the sovereignty of nations and integrity of their domestic constitutional and judicial systems. Part IV describes the contemporary debate about the future of international investment treaties, and examines the broad consequences of this extraordinary development in international law.
The essential conclusions of my assessment are:

i) Investor-State arbitral regimes, such as the one established by Chapter Eleven of NAFTA, combine elements of public international law and private international commercial arbitration without regard to the very different purposes those international regimes were established to serve. The arbitral procedures established by this regime allow a foreign investor, usually a large multinational corporation, to claim damages against a nation state for breach of the terms of a treaty to which the investor is not a party and pursuant to which it owes no obligations.

ii) Prior to the advent of such investor-State arbitral regimes in the latter part of the 20th century, a foreign investor would have had to establish the existence of an agreement with that nation state in order to submit a dispute to arbitration. Otherwise the only recourse for such an investor would have been to the domestic courts or tribunals of the nation whose actions were being impugned. If there is a denial of remedies by the local courts, then an international claim may arise. The claim has, thereafter, to be espoused by the home state of the investor and pursued as an international claim through international tribunals. The investor himself had no status in law to pursue any remedies against the state. The “local remedies rule” required that remedies provided by the national laws of the host state be exhausted before a claim can arise in the international arena.¹

iii) By obviating the requirement for privity of contract, investor-State arbitral regimes allow foreign investors to claim damages arising from the actions, policies or laws of sovereign states which are undertaken entirely outside the sphere of commercial relationships. Conversely, international tribunals are empowered to resolve disputes that should initially have been brought in accordance with the domestic laws and procedures of the nation state whose actions or laws are being challenged and later, pursued by the home state of the foreign investor as an international regime.

claim. This system gave the initial opportunity to local courts to remedy any injustice that may have been done to the foreign investor and also to frame the nature of the dispute for later resolution by international tribunals.

iv) Investor-State arbitration under Chapter Eleven has been invoked to challenge a diverse array of government actions including: environmental and public health laws; public procurement practices; municipal land-use approvals; the delivery of services by a Crown corporation; the allocation of softwood export quotas; and the decisions of courts and a civil jury.

v) The government measures that are most often the subject matter of investor-State disputes are neither explicitly about investment, nor international in their design or application. Rather the typical targets of investor-State claims are measures established to serve broad public policy objectives.

vi) Thus, investor-State arbitration employs dispute resolution procedures drawn from the sphere of private international commercial arbitration, but enlists them for a purpose they were never intended and are ill-equipped to serve - namely, to resolve disputes about government policy, programs and law that have broad public implications and which often affect many in society. Yet once empowered, investor-State arbitral tribunals operate entirely outside the framework of domestic law and constitutional safeguards.

vii) By establishing such extra-judicial dispute procedures, matters which had historically been the exclusive sovereign preserve of parliaments and the courts are now subject to adjudication by these tribunals.

viii) The investor-State procedures under Chapter Eleven of NAFTA end with an award that is binding under international law and which domestic courts will recognize and enforce. Yet the scope for judicial oversight of the arbitral process or review of arbitral awards is uncertain because both depend upon the law of the place in which the arbitration occurs. Where arbitration takes place
outside Canada for example, there may be no opportunity whatsoever for judicial review by
Canadian courts of an award made against Canada and concerning Canadian laws, policies or
programs.

ix) Investor-State arbitration under Chapter Eleven effectively internationalizes disputes that
have historically been the domain of municipal law. Several commentators have aptly characterized
these developments as having established a new international constitutional order to which the
domestic constitutions of nation states are subservient.

x) Initially driven by a wave and enthusiasm for the policies of trade and investment
liberalization, the adverse impacts of these dramatic developments upon the sovereignty of nations,
the integrity of their domestic constitutional arrangements and their capacity to achieve other
societal goals, such an environmental and human rights protection, are only now coming to light.

PART I: THE ORIGINS OF INTERNATIONAL INVESTMENT AGREEMENTS

14. The practice of arbitration has it origins in early history. The arbitration of commercial disputes has
existed since the dawn of commerce. Similarly, the use of arbitration to resolve international disputes
between nation states (“state-to-state arbitration”) also has a well established history.\(^2\)

15. The advent of treaties providing for the resolution of private commercial disputes arising from
contractual relationships (“international commercial arbitration”) is of much more modern origin, and dates
from the 20\(^{th}\) century. In recent years, a number of international conventions have codified the rules for
international commercial arbitration and provided for the recognition and enforcement of international

\(^2\) Redfern and Hunter, *Law and Practice of International Commercial Arbitration*, 3\(^{rd}\) ed (London: Sweet and
Maxwell, 1999), at p. 1; Mustill, “Arbitration: History and Background”, (1989) 6 Journal of International Arbitration,
43.
arbitral awards. Prior to these developments, commercial arbitration, whether international or domestic, was entirely a matter for the municipal law of nation states.

16. Of even more recent origin is the use of international treaty instruments which allow private foreign investors to invoke international arbitral processes to assert claims against, and concerning the actions taken by, nation states ("investor-State arbitration"). This development was in many ways unheralded and represented a very significant departure from the norms of both international and domestic law.

17. Investor-State arbitration, such as provided for under the investment provisions set out in Chapter Eleven of NAFTA, has been constructed from elements taken from two different spheres of international arbitration: the first developed to resolve disputes between states; the second to resolve international disputes arising from private commercial relationships. Therefore, it is important to understand the origins and purposes of these distinct spheres of international arbitration in order to assess the character and implications of investor-State arbitration. An account of the historical setting for the arbitration of foreign investment disputes can be found in Chapter 6 of my book, *The Settlement of Foreign Investment Disputes*, a copy of which is attached hereto as Exhibit “B”.

**State-to-State Arbitration**

18. International arbitration, which historically was defined as arbitration between states, represents the oldest form of pacific settlement between nations through third party intervention. Arbitration of inter-state disputes has been particularly useful for resolving those disputes which the parties are either unwilling or

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3 For discussion of the concept of “international” arbitration see paragraphs 18 to 21.

4 The first such treaty was between Germany and Pakistan in 1958. R Dolzer and M Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff, 1995) But, the early treaties did not have strong dispute settlement provisions. The treaties with strong provisions came to be made later. The exact effect of these formulations was not known until 1991. The first case that used a treaty provision to find jurisdiction was *AAPL v. Sri Lanka* decided in 1991 (reported in (1991) 6 ICSID Review 526). The notion of arbitration without privity is of rather recent vintage. It has now come to be accepted as a result of a series of awards in which jurisdiction was based in treaty provisions.

5 For example, the First Hague Peace Conference in 1899 stated, “international arbitration has as its objects the settlement of disputes between states.”
unable to resolve through negotiation. It has, for example, played an important role in resolving international boundary disputes, such as those concerning maritime fishing areas.  

19. Historically, and until well into the 20th century, the concept of “international arbitration” was confined to the practice of resolving disputes between states. A dispute between a state and an alien was not regarded as an international dispute capable of being settled through international processes, but rather one to be resolved by the courts or tribunals of the state against which the claim was being asserted. International law was seen as law between sovereign states and prevailing doctrine denied the possibility of an individual or a corporate entity having sufficient status in international law to have recourse to an international remedy through international tribunals.  

20. In all cases, contracts between states and foreign private parties were subject to, and dependent upon, the municipal law of some state. There is a plethora of dicta and opinion in the first half of the twentieth century, which makes this position clear.  

21. In fact, it was not until after the Second World War that attempts were made to render disputes arising between states and foreign entities amenable to arbitration under international law or some supranational system akin to international law. These efforts culminated in the establishment of international

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6 JG Merrills, International Dispute Settlement (Cambridge University Press, 1998)  


8 Sornarajah: The Settlement of Foreign Investment Disputes, noting the Serbian Loans Case (1926) PCU Series A, NO. 20, p. 17: “The controversy submitted to this court is exclusively concerned with relations between the borrowing State and private persons, that is to say, relations which are, in themselves, within the domain of municipal law”. See also J. Basdevant (1936) 58 Hague Recueil at 677: “Un differend entre un etet et un stranger ne releve pas du droit International”.  

9 The Lena Goldfields Arbitration stands alone as an early case in which there was arbitration between a private company and a state. In the late 1950s, there were a series of Middle Eastern arbitrations relating to the oil industry where we find the emergence of international investment arbitration. They are based on the idea that the local laws of the Middle Eastern states were not sophisticated enough to handle petroleum arbitrations. This reasoning was used to create a transnational system of arbitration to deal with petroleum contracts and later diversified to include foreign
investment arbitral regimes, which drew heavily on developments that were also occurring in the area of international commercial arbitration, which I turn to next.

**International Commercial Arbitration**

22. As noted, arbitration of commercial disputes dates from the earliest times. When disputes arose between traders belonging to different states, such arbitrations acquired an international dimension. However, until well into the twentieth century, arbitration of commercial disputes was considered to be “national” in the sense that disputes would usually be settled in accordance with the rules of the jurisdiction in which an arbitration was held.

23. As the popularity of arbitration of commercial disputes grew, so did pressure to establish international norms for the conduct of such arbitrations and, more importantly, for the recognition and enforcement of arbitral awards. As a result, during the mid-20th century, a number of international conventions were established to codify the rules for international commercial arbitration and to provide for the recognition and enforcement of arbitral awards arising from such proceedings.\(^\text{10}\)

24. The establishment of a comprehensive regime relating to international commercial arbitration was largely realized in 1958 with the adoption of the *New York Convention*, which provided an effective method of obtaining recognition and enforcement of foreign arbitral awards.\(^\text{11}\) The other significant development of this period was the establishment of specialized institutions to administer international investment generally.

\(^\text{10}\) For an overview of the development of international conventions concerning international arbitration from the Geneva Protocol in 1923 to the New York and Washington Conventions is the later half of the century, see Redfern and Hunter, note 2, at pp. 43-74.

\(^\text{11}\) The establishment of the *New York Convention* paved the way for the development and refinement of the rules and procedures for conducting international commercial arbitration. Thus, to facilitate the harmonization of arbitral rules of different countries, in 1976, the *United Commission on International Trade Law* (UNCITRAL) adopted Arbitration Rules, and nearly a decade later, the *Model Law* on International Commercial Arbitration. The *Model Law* has subsequently been adopted by many nations, including Canada, where it provides the template for dealing with the subject of international arbitration. See, for example, the *Commercial Arbitration Act*, R.S.C 1985, c. 17 (2nd, Supp.); Peter Binder, *International Commercial Arbitrations in UNCITRAL Model Law Jurisdictions* (Sweet and Maxwell, 2000).
arbitration, the most prominent of which is the *International Centre for the Settlement of Investment Disputes* (ICSID).\(^{12}\)

25. The terms “international” and “commercial” are used to delineate the parameters of these arbitral regimes. The term “international” is most often used in this context to distinguish commercial arbitration which in some way transcends national boundaries, from arbitration which is purely national or domestic in character.\(^{13}\)

26. The term “commercial” on the other hand, has been defined quite differently by various nations, which often distinguish between contracts that are amenable to settlement by arbitration, and those which are not.\(^{14}\)

27. The importance of these distinctions is acknowledged by international protocols and conventions concerning commercial arbitration, which commonly empower parties to reserve the right to define which contracts will be considered commercial under national law.\(^{15}\) Thus, disputes arising from matrimonial,

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12 The ICSID was established by the Washington Convention of 1965 which requires, *inter alia*, that each contracting state shall recognize an award rendered pursuant to it as binding and provide for its enforcement as if it were a final judgment of a court in that state. While neither Canada nor Mexico is a party to the Convention, it is mentioned here because it represents one of three procedural mechanisms to which foreign investors may seek recourse under NAFTA Article 1120, though not against Canada or Mexico. Non-parties may choose to hold ad hoc arbitrations under the Additional Facility Rules of ICSID and ask ICSID to administer the arbitration. Some NAFTA tribunals have used this option: see *ADF Group Inc. v. United States*, see note 51 infra.

13 Redfern and Hunter, note 2, pp. 13 and 14. This international dimension may arise either from the nature of the dispute (such as disputes arising from international trade), or from the national origins of the parties. Various national systems of law may have adopted one, the other, or a hybrid of these criteria to determine whether a dispute is international in character.

14 Thus, in civil law jurisdictions, two merchants could arbitrate a dispute regarding a commercial contract, but the same parties could not arbitrate a contractual dispute concerning property tenure, employment or family law: Redfern and Hunter, note 2, p. 18.

15 For example, Article I.3 of the New York Convention allows contracting states to limit the application of the Convention to disputes arising out of legal relationships “which are commercial under the national law of the state making such declaration.” A similar commercial reservation was permitted under the Geneva Protocol of 1923: Redfern and Hunter, note 2, pp. 457-458.
property tenure, employment law are often considered to be beyond the sphere of commercial relationships.\textsuperscript{16}

28. The procedural norms of international commercial arbitration reflect the fundamental assumption that these disputes are essentially private in character and of no consequence to third parties. For instance, arbitral proceedings are generally held in camera, and the confidentiality of the arbitral process is seen as one of its most important advantages.\textsuperscript{17} Unlike proceedings in a court of law, international commercial arbitration is consistently regarded as a private proceeding. Indeed, the importance of secrecy to the arbitral process is expressly acknowledged by international commercial arbitration rules which provide, for example, that “Deliberations of the Tribunal shall take place in private and remain secret,” or that “Hearings shall be held in camera unless the parties agree otherwise”.\textsuperscript{18}

29. In accordance with these norms and assumptions about the private character of international commercial arbitral disputes, party autonomy is the guiding principle with respect to the procedures to be followed by arbitral tribunals. Thus, parties to such arbitrations are typically free to choose their own tribunal,\textsuperscript{19} to determine the place of arbitration,\textsuperscript{20} and generally to set out the rules that will guide the conduct of the arbitration.\textsuperscript{21}

\textsuperscript{16} Redfern and Hunter, note 2, pp. 18-19.

\textsuperscript{17} See Redfern and Hunter, note 2, p. 27, who quote a former Secretary-General of the International Chamber of Commerce as stating:

“It became apparent to me very soon after taking up my responsibilities at the ICC that the users of international commercial arbitration, i.e. the companies, governments and individuals who are parties in such cases, place the highest value upon confidentiality as a fundamental characteristic of international commercial arbitration. When enquiring as to the features of international commercial arbitration which attracted parties to it as opposed to litigation, confidentiality of the proceedings and the fact that these proceedings and the resulting award would not enter into the public domain was almost invariably mentioned.”

\textsuperscript{18} These rules are set out in Article 24(1) of the Additional Facility Rules of ICSID, and Article 25 of UNCITRAL, respectively.

\textsuperscript{19} ICSID AFR - articles 3(2) and 6(3); UNCITRAL - articles 5, 6.1 and 7.1.

\textsuperscript{20} ICSID AFR - articles 20, 21; UNCITRAL - article 16.

\textsuperscript{21} ICSID AFR - article 3(2); UNCITRAL - articles 1.1 and 15.1.
30. Similarly, the issues of notice to, and potential intervention by, third parties is entirely ignored by the conventions and arbitral rules that frame such proceedings. The assumption that international commercial disputes are purely private in nature also underlies the limited scope for judicial review of such awards, a subject to which I will return in Part III.

31. In sum, by the latter part of the twentieth century, an international regime had been established in order to facilitate the resolution of international commercial disputes. That regime is complimented by domestic laws providing for the recognition and enforcement of foreign arbitral awards. However, the ambit of this regime is limited to commercial relationships that are essentially private and which have an international character. Moreover, the types of relationships that will be considered “commercial” for these purposes may be reserved to the prerogatives of nation states so they may delineate the sphere of public policy and law which these regimes may not transgress.

**Investor-State Arbitration**

32. This brings us to the development of international investor-State arbitral regimes. The primary vehicle for establishing international disciplines concerning the interests of foreign investors is the Bilateral Investment Treaty (“BIT”), the first examples of which were negotiated in the late 1950s. The treaties have been progressively modified, the newer versions of them being more sophisticated. Their original aim was to

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23 The scope for judicial review of international commercial arbitral awards is generally only permitted in accordance with the municipal laws of the jurisdiction chosen as the place of arbitration. These, in turn, are usually reflective of international norms established for such domestic legislation which narrowly confines the scope for judicial review to basic questions of procedural irregularities and jurisdictional competence. In addition to these basic jurisdictional issues, it is common for both international conventions and domestic legislation providing for the enforcement of arbitral awards to provide for the setting aside of such awards as being contrary to the public policy of that jurisdiction. However, courts have consistently adopted a conservative interpretation of the scope for review established by the public policy standard. See, for example, the approach adopted by Canadian courts as commented on in Haigh, Kunetzki and Antony, “International Commercial Arbitration and the Canadian Experience”, (1995) 34 Alta.L. Rev. (No. 1) 137, at fn. 86 and 87.

24 See Dawson, *Whose Rights? The NAFTA Chapter 11 Debate* (Centre for Trade Policy and Law, 2002); Christopher Wilkie, “The Origins of NAFTA Investment Provisions”, in Dawson (ed) *Whose Rights?*, supra at p. 17, which identifies a BIT between Germany and Pakistan negotiated in 1959 as the first of its kind. The first BITS to which Canada was a party and which, in accordance with Canadian practice, are described as Foreign Investment Protection Agreements (FIPAs) were negotiated in the early 1990s. The date of the first FIPA, in that case with Poland, is
protect investments made by foreign investors of developed states in developing states which were seen as unstable and risky. The elimination of legal and political risks through the statement of firm rules was the main objectives of these treaties. In the context of these objectives, Chapter 11 of NAFTA is an anomaly as it seeks to impose rules on two developed states, Canada and the United States, in their investment relations.

33. Common features of these BITs include a broad definition of investment and provisions which oblige State-parties to these treaties to accord certain treatment to foreign investors and their investments. A centerpiece of these treaties is the prohibition against taking of property or anything tantamount to a taking except on payment of compensation and the satisfaction of some other conditions. These obligations take the form of general prohibitions against government action, legislative and otherwise, that would, for example, impose foreign ownership restrictions for key industries or sectors. They may also impact regulatory legislation of states which may be in the public interest.

34. The most remarkable feature of these treaties were provisions giving third-party investors standing to invoke international arbitral mechanisms to assert damage claims against sovereign states, notwithstanding the absence of having any contractual or other direct relationship with that national government. Prior to this development, a foreign investor would have had to establish the existence of an agreement with the nation state to submit such a dispute to arbitration. In the absence of such agreement, the foreign investor’s only recourse would have been to the domestic courts and later, in the event of non-satisfaction, to the diplomatic intercession of his home state.

35. Thus, unlike the usual concept of arbitration, these treaties establish a right to arbitration even though no privity of contract exists between the disputing investor and the nation state against which the claim is brought. This development represented a fundamental departure from the firmly entrenched

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25 In many BITs the State-party makes a unilateral or standing offer to arbitrate any dispute that might arise in the future. When a dispute arises and the private investor submits the dispute for arbitration under the BIT, typically an “agreement to arbitrate” is considered to have been made.

principle that arbitration is entirely dependent on the consent of the parties as evidenced in a written agreement (most often included as a clause in a commercial contract).

36. By obviating the requirement for privity of contract, foreign investors were also empowered to claim damages arising from the actions, policies or laws of sovereign states that are undertaken entirely outside the sphere of commercial relationships. Conversely, international tribunals are empowered to resolve disputes that could otherwise have only been brought in accordance with the domestic laws and procedures of the nation state whose actions or laws are being impugned.

37. The adoption of international commercial arbitration regimes to resolve disputes arising under international investment treaties puts the international and domestic framework of law, developed to provide for the recognition and enforcement of commercial arbitral awards, at the service of disputes which have nothing at all to do with private commercial arrangements. Thus, investor-State arbitration depends upon a framework of law established for purposes very different than those it is now serving.

PART II: CHAPTER ELEVEN OF NAFTA

38. As noted, the investment provisions of NAFTA are set out in Chapter Eleven. Under Chapter Eleven, foreign investors are empowered to unilaterally invoke binding international arbitration against a State-party which the investor alleges has breached its obligations under Part “A” of Chapter Eleven or certain other NAFTA provisions.

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27 The investment provisions of NAFTA represented a significant extension of Canadian treaty practice with respect to foreign investment protection. At the time, five FIPAs had been negotiated by Canada, but none included the right to invoke investor-State procedures as expansive and unqualified as those set out in NAFTA: Wilkie, note 24, at pp.16-17.

28 In more than one investor-State claim brought pursuant to NAFTA, the disputing investor is seeking to expand the scope of investor-State litigation to obligations that are not explicitly incorporated to Chapter Eleven dispute procedures: see United Parcel Service of America Inc. v. Canada, at note 46, infra and Methanex Corporation v. United States of America, at note 45, infra.
39. For the most part, Chapter Eleven delineates a catalogue of government “measures” which may neither be adopted, maintained nor enforced by either national or sub-national governments. “Measures” are defined to include “any law, regulation, procedure, requirement or practice”. 29 “Investment” is also defined expansively to include many forms of tangible and intangible property interests, including debt and equity interests, business concessions and licenses.

40. Some of the obligations of the State-parties to NAFTA are framed as positive obligations, such as:

- the obligation to accord “National Treatment” to foreign investors and their investments by according them no less favourable treatment than is accorded, in like circumstances, to a State-party’s own investors and to their investments. 30 This requirement would, for example, prohibit restrictions on foreign investment, including those that are specific to particular industries or sectors;

- the obligation to accord “Most Favoured Nation Treatment” to foreign investors and to their investments by according them no less favourable treatment than is accorded, in like circumstances, to investors from any other nation, or to their investments; 31

- the obligation to accord to foreign investments treatment in accordance with “international law including fair and equitable treatment and full protection and security”. 32

41. Other obligations establish broad prohibitions on a diverse array of government “measures”. For instance:

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29 NAFTA Article 201.
30 Article 1102.
31 Article 1103.
32 Article 1105.
parties are prohibited from imposing “Performance Requirements” - i.e. administrative or regulatory requirements, such as obligations to source goods and services locally - as a condition on the right to establish or carry on investment activities;\(^\text{33}\)

- parties are prohibited from imposing any constraints on the right of foreign investors to choose senior managers and board members of any nationality;\(^\text{34}\)

- parties are prohibited from imposing constraints on the right of foreign investors to repatriate profits “freely and without delay”;\(^\text{35}\) and

- parties are prohibited from taking any action which directly or indirectly “expropriates” an investment or represents a measure “tantamount to expropriation”.\(^\text{36}\)

42. Therefore, in addition to proscribing government actions that might favour domestic investors or citizens, NAFTA investment disciplines prohibit a diverse array of government policies, laws and actions that may be entirely non-discriminatory in their design and application. As a result, NAFTA parties are barred from imposing certain requirements on the investors/investments of another NAFTA party even if the same requirements are imposed on all investors and investments, be they domestic or foreign.

43. An article published in the *ICSID Review* described NAFTA as being explicit in terms and vast in scope. The author characterized NAFTA’s investor-State suit provisions as follows:

> It grants innumerable present and future investors the right to arbitrate a wide range of grievances arising from the actions of a large number of public authorities whether or not any specific agreement has been concluded with the particular complainant, and so impels

\(^\text{33}\) Article 1106.

\(^\text{34}\) Article 1107.

\(^\text{35}\) Article 1109.

\(^\text{36}\) Article 1110.
us to reconsider fundamental assumptions about the international legal process as it affects investors abroad.\textsuperscript{37}

44. Commenting on NAFTA and the European Energy Charter Treaty, which was negotiated subsequently, the author goes on to state:

By allowing direct recourse by private complainants with respect to [such] a wide range of issues, these treaties create a dramatic extension of arbitral jurisdiction in the international realm.\textsuperscript{38}

\textbf{Investor-State Litigation Under NAFTA}

45. The expansive scope of NAFTA investment rules is evidenced in the record of claims that have been brought pursuant to these provisions. Since 1997, when the first formal claim was made by a foreign investor against Canada,\textsuperscript{39} at least twenty-nine investor-State claims appear to have been brought under Chapter Eleven’s provisions. Of the claims about which information has been made public,\textsuperscript{40} eight have been brought against Canada, nine against the U.S.,\textsuperscript{41} and twelve against Mexico.


\textsuperscript{38} Paulsson, note 37.

\textsuperscript{39} The first case in which a foreign investor sued Canada was Ethyl Corporation \textit{v.} Canada. In that case, U.S. based Ethyl Corporation brought a claim against Canada for $250 million in damages allegedly caused by the federal regulation of a neuro-toxic fuel additive the company distributed in Canada. That claim was settled when Canada rescinded the regulation, paid the company over $19 million in costs, and issued a formal written statement which amounted to a public apology for having regulated in the first place: All relevant materials concerning this case can be found on the website of Canada’s Department of Foreign Affairs and International Trade (“DFAIT”) at www.dfait-maeci.gc.ca/tna-nac/ethyl-en.asp (last accessed on 10 December 2002).

\textsuperscript{40} Information about other Chapter 11 claims can also be found on the DFAIT website: www.dfait-maeci.gc.ca/tna-nac/gov-en.asp. As of 10 December 2002, the website listed 8 arbitration claims brought against Canada, 6 against the U.S., and 7 against Mexico. On the same date, a site maintained by a professor of law at the University of Windsor identified 9 claims against Canada, 9 against the U.S. and 11 against Mexico: www.naftaclaims.com/. While the NAFTA Commission is required to keep a public record of all Chapter Eleven Notices of Claim (Article 1126), these claims are not recorded on its website: www.nafta-sec-ahena.org/english/index.htm.

\textsuperscript{41} All of the reported claims brought by Canadian investors but one have been initiated against the U.S. The sole exception is a claim brought against Mexico by International Thunderbird Gaming Corporation, by all accounts a Canadian company, on August 23, 2002.
46. Foreign investors who invoke the investor-State provisions of Chapter Eleven against a State-party typically claim damages in the hundreds of millions of dollars. Moreover, the government measures that are being assailed in these proceedings span a broad spectrum of policy, programmatic, legislative, regulatory and judicial action.\footnote{As indicated above, “measures” are defined by NAFTA Article 201 to include any law, regulation, procedure, requirement or practice.} Claims have been asserted concerning:


(ii) municipal land use decisions;\footnote{Mondev International Ltd., supra, note 43; \textit{Metalclad Corp. v. United Mexican States} (Notice of Arbitration, 2 January 1997), online at The U.S. Department of State: www.state.gov/documents/organization/3997.pdf (date accessed: 11 December 2002).}


(iv) the manner in which certain parcel and courier product services are provided by Canada Post;\footnote{United Parcel Service of America Inc. v. Canada (Notice of Arbitration, 19 April 2000), online at DAFIT: www.dfait-maeci.gc.ca/tna-nac/documents/ups-noa.pdf (date accessed: 11 Dec.2002).}


the imposition of import tariffs on Canadian softwood lumber products;\textsuperscript{49}

the allocation of export quotas under an international trade agreement concerning softwood lumber products;\textsuperscript{50} and

the procurement practices and requirements of federal and sub-national governments.\textsuperscript{51}

These claims illustrate the diversity of policy, legislative, programmatic and judicial functions that are now the subject of investor-State claims brought under Chapter Eleven. The government measures that are the subject matter of these disputes are neither explicitly about investment, nor international in their design or application. Rather the typical targets of investor-State claims are measures established to serve such broad and domestic public policy objectives as environmental protection or the delivery of public postal services.

Thus, matters which have historically been the exclusive sovereign preserve of parliaments and the courts are now subject to adjudication by international tribunals originally designed to resolve private international commercial disputes.

As noted, investor-State procedures have been invoked to challenge judicial determinations made by the courts of a NAFTA Party.\textsuperscript{52} In \textit{The Loewen Group, Inc. v. United States of America}, a Chapter Eleven tribunal rejected the respondent’s objections to its jurisdiction to consider a claim relating to the jury decision rendered in private contract litigation. The tribunal concluded that the decision of the jury


\textsuperscript{52} Other investor-State claims were initiated after domestic judicial remedies had been explored or were ongoing: see \textit{Metalclad, supra}, note 44; \textit{Sun Belt Water Inc. supra}, note 48; \textit{S.D. Myers Inc. v. Canada} (Notice of Arbitration, 30 October 1998), online at DFIAT: www.dfait-maeci.gc.ca/tna-nac/documents/myers2.pdf (Statement of Claim of 30 October 1998), online at DFIAT: www.dfait-maeci.gc.ca/tna-nac/documents/myers3.pdf (date accessed: 12 December 2002).
constituted a governmental “measure” under NAFTA, and placed no limits on what types of court actions or judicial decisions could be so categorized.\textsuperscript{53} In \textit{Mondev International Ltd. v. United States of America}, a Chapter Eleven tribunal assumed jurisdiction to review a decision of a U.S. appellate court.\textsuperscript{54} In \textit{Azinian v United Mexican States}, the disputing investor challenged the determinations of Mexican courts annulling a concession contract it had negotiated with a particular municipal government.\textsuperscript{55}

50. To date, seven investor-State claims have been determined on their merits. Of these, four have found in favour of the disputing investor. In one case, \textit{Metalclad Corp. v. United Mexican States}, a local municipality denied a foreign investor a building permit to establish a hazardous waste disposal site on land already contaminated with hazardous waste. The denial of the building permit was held to be an “expropriation” within the meaning of Chapter Eleven. By holding that there was a taking that had to be compensated, the tribunal effectively impeded the duty of the State to act to the benefit of its people’s health.\textsuperscript{56}

\textsuperscript{53} \textit{The Loewen Group, Inc. supra}, note 43 - see Award on Jurisdiction, 5 January 2001, paras. 39-60, online at The American Society of International Law: www.international-economic-law.org/Loewen/ (date accessed: 12 December 2002).

\textsuperscript{54} \textit{Mondev International Ltd. supra}, note 43 - see Final Award of 11 October 2002, para. 92, online at The U.S. State Department: www.state.gov/documents/organization/14442.pdf (date accessed: 12 December 2002).

\textsuperscript{55} \textit{Azinian, supra}, note 43.

\textsuperscript{56} \textit{Metalclad Corporation, supra}, note 44 - see Final Award of 30 August 2000, online at DFAIT: www.dfait-maei.gc.ca/tna-nac/documents/Award-e.pdf (date accessed: 12 December 2002).
51. Mexico subsequently sought judicial review of this award in British Columbia. The Supreme Court of British Columbia recognized that the tribunal’s definition of “expropriation” was exceptionally broad, but held that it could not interfere with the decision:57

The Tribunal gave an extremely broad definition of expropriation for the purposes of Article 1110. In addition to the more conventional notion of expropriation involving a taking of property, the Tribunal held that expropriation under the NAFTA includes covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property. *This definition is sufficiently broad to include a legitimate rezoning of property by a municipality or other zoning authority. However, the definition of expropriation is a question of law with which this Court is not entitled to interfere* under the International [Commercial Arbitration Act]. [emphasis added]

52. Two other claims decided in favour of disputing investors were brought against Canada. One, *Pope and Talbot v. Canada*, involved the manner in which export quotas had been allocated to the disputing investor for its softwood lumber products.58 The other, *S.D. Myers v. Canada*, involved a federal ban on the export of certain hazardous waste and Canada’s obligations under an international environmental treaty.59

53. Summaries of many of these Chapter Eleven cases can be found in two publications. The first is *Private Rights, Public Problems*, a book written by Howard Mann and published by the International Institute for Sustainable Development and World Wildlife Fund. The other is a document published in 2001 by Public Citizen, a non-profit public interest advocacy group based in Washington, D.C, titled *NAFTA Chapter 11 Investor-to-State Cases: Bankrupting Democracy*. These texts are attached to this affidavit as Exhibits “C” and “D” respectively.

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58 *Pope and Talbot*, supra, note 50.

59 *S.D. Myers*, supra, note 52.
54. In its 35 year history, ICSID has handled 40 cases which have invoked the provisions of a BIT (of which, as noted, there are now more than 2000). By comparison, nearly thirty investor-State claims have been brought under Chapter Eleven of NAFTA alone within a shorter period. Moreover, given the quantum of damages sought in Chapter 11 cases, and in light of the far reaching public policy implications that would follow should foreign investors prevail, the importance of these claims cannot be measured solely by their number.

See note 61, infra.

Kenneth J. Vandevelde, Investment Liberalization and Economic Development: The Role of Bilateral Investment Treaties, 36 Colum. J. Transnat’l L. 501. In its 35 year history, ICSID handled 79 cases, forty of which arose pursuant to the provisions of specific foreign investment agreements. Half of these cases have been initiated in the past 5 years, an increase which has been attributed to the notoriety surrounding the cases brought pursuant to NAFTA investment rules: see L. Peterson, Changing Investment Litigation, Bit by BIT, in Bridges, May 2001, Year 5 No. 4. Also on the proliferation of foreign investment disputes see Antonio R. Parra; Provisions on the Settlement of Investment Disputes in Modern Investment Laws, Bilateral Investment Treaties and Multilateral Instruments on Investment, (1997), 12 Foreign Investment Law Journal, 287 at pp. 361-362.
PART III: THE IMPACT OF INVESTOR-STATE PROCEDURES ON THE SOVEREIGNTY, RULE OF LAW, AND CONSTITUTIONAL NORMS OF MEMBER STATES

55. The advent of international investment treaties that empower private investors (who are invariably multinational corporations) to invoke binding international arbitration to enforce the provisions of those treaties represents a dramatic departure from the conventions of international law in two respects. First, these treaties accord non-state entities the right to enforce an international trade agreement to which they are not parties and pursuant to which they have no obligations. Second, investor-State litigation extends the sphere of international commercial arbitration to disputes that have no foundation in contract, and which often arise from issues that are essentially public, rather than private in character.

56. As the cases which have arisen under Chapter Eleven illustrate, investment tribunals are encroaching into areas which international commercial arbitral tribunals were not designed to deal with. Thus tribunals that are set up at the instance of a private party consistently deal with disputes that go well beyond the contractual or commercial disputes which were originally contemplated by the instruments establishing a regime for international commercial arbitration.

57. This is made even more problematic by the fact that these tribunals are predominantly guided by economic and commercial considerations, and are structurally incapable of reflecting the larger social, cultural, political and moral objectives of the international community necessary for the fair resolution of disputes which may have significant public interest components. Such tribunals have often shown an undue deference to the rights of the private investor and far too little consideration for the interests of the state in pursuing other legitimate, and often non-commercial public policy objectives such as environmental protection.  

58. These unprecedented developments in international law have resulted in a considerable surrender of sovereignty by the State-parties to such agreements. The nature and extent of the impact of international investment regimes on sovereignty and the constitutional norms of State-parties is determined both by the substantive nature of obligations engendered by these regimes, as well as by the dispute procedures available to ensure that these obligations are adhered to. In other words, the corrosive impact of NAFTA investment rules on sovereignty has both a substantive and procedural dimension.

**The Constitutional Characteristics of NAFTA Investment Rules**

59. The substantive obligations undertaken by nation States under international treaties and other agreements are inherently constraining of their sovereign authority. Indeed, several commentators have aptly characterized these developments as having established a new international constitutional order to which the domestic constitutions of nation states are subservient.\(^\text{63}\) Thus, international trade and investment agreements can be seen as having the characteristics of constitutional instruments because they represent a form of pre-commitment strategy that binds future governments, they are difficult to amend, and they are binding politically and, in some cases, judicially as well.\(^\text{64}\)

60. Decisions like *Metalclad* and *Mondev* involved the responsibility of sub-national entities at provincial and even city council levels. They demonstrate how deep the investment treaty can bite into the structure of government making the federal state liable for what happens at the bottom of the decentralized state structure. The investment treaties like NAFTA therefore contemplate intense supervision of the activities of local decision making bodies if responsibility is to be avoided. Quite apart from the creation of such machinery, the legality of such supervision within the existing constitutional structures is to be doubted.

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Internal constitutional systems do not contemplate liability of the central government for the exercise of powers delegated to lower bodies. But, the investment treaties do. The constitutional capacity of the federal governments to recall powers that are based on original compacts is to be doubted. The dissonance between investment treaties and federal systems is evident.

**NAFTA’s Takings Rule**

61. One of the clearest illustrations of how the requirements of such international agreements acquire the character of quasi-constitutional instruments can be found in the provision of Chapter Eleven dealing with the issue of expropriation.

62. The protection of private property rights engendered by NAFTA Article 1110 is absolute in the sense that this provision prohibits government measures which “may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment”, except in certain specified circumstances. Even in

65 Article 1110: Expropriation and Compensation, provides in part:

1. No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ("expropriation"), except:

   (a) for a public purpose;

   (b) on a non-discriminatory basis;

   (c) in accordance with due process of law and Article 1105(1); and

   (d) on payment of compensation in accordance with paragraphs 2 through 6.

2. Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place ("date of expropriation"), and shall not reflect any change in value occurring because the intended expropriation had become known earlier. 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.
these circumstances, compensation must be paid that is equivalent to the fair market value of the expropriated investment.

63. However, in many common and civil jurisdictions, property rights are not regarded as unconditional, but are subject to certain and over-riding social objectives or concerns. Canada, for one, explicitly rejected the inclusion of private property protection in the Constitution Act, 1982. Rather, under its constitutional arrangements, governments may expropriate private property so long as they act lawfully. Moreover, the circumstances and extent to which compensation will be paid in such cases is a matter for the legislatures and Parliament to determine.66

64. In effect, NAFTA codifies the protection of the private property interests of foreign investors in a manner that is virtually as binding on the federal government as would have been the case had foreign property rights had been entrenched in its Constitution. While nothing in NAFTA prevents governments from expropriating property, the obligation to pay compensation in accordance with Article 1110 is binding and enforceable, notwithstanding any stipulation to the contrary that might be made by Canadian legislatures or courts.

65. As noted by David Schneiderman in his work concerning the impact of NAFTA investment rules, the expropriation provisions of NAFTA may been seen as effectively incorporating the U.S. Constitution’s Fifth Amendment protection of property rights, and the Fourteenth Amendment requirement of due process.67 The former provides that private property shall not be taken for public use without just compensation. The latter, establishes a constitutional guarantee of due process. As engendered by Article

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67 Schneiderman, note 66 at p. 515-521.
1110, both requirements are now binding on Canada and its failure to comply with these obligations may give rise to enforceable damage awards against it.

66. To be sure, the constraints on sovereign authority are indirect - no provision of NAFTA compels Canada to amend its domestic law, although in many instances it has done so. Nevertheless, the coercive impact of this regime is demonstrable and can readily be observed in the changes made by nations to their domestic policies, programs and law that often follow from the invocation of trade dispute and investor-State procedures. The consequences of non-compliance with international trade disciplines, which may result in financial penalties enforceable as judgments of Canadian courts, and trade sanctions measured in the tens if not hundreds of millions of dollars, are too simply too severe for any nation to ignore.

67. Internal constitutional balances are upset by the provisions of treaties like NAFTA. A recourse to property protection arises in the foreign investor but not to a Canadian investor. This remedy can be pursued through an international tribunal whereas whatever remedy that is available to a Canadian investor has to be pursued through local courts. Equality provisions of the constitution are necessarily violated as a result.

68. Since decisions of courts can amount to interferences with property (see the Azinian, Mondev and Loewen case), there could be recourse to international arbitration against them, thereby bypassing the appellate courts within the host state. This violates notions of hierarchy of courts established by the constitution and enables the executive to defeat judicial control over domestic matters merely by entering into a treaty with arbitration provisions. Fundamental notions of separation of powers are affected as a result.

68 Twenty-nine federal statutes were amended to implement Canada’s obligations under NAFTA, these amendments are set out in Part II of the NAFTA implementing legislation - The North American Free Trade Agreement Implementation Act, Statutes of Canada, 1993, c. 44, Part II, ss. 22-241.
69. Constitutional systems of the Commonwealth, following the British heritage, ensure that no particular class or section of the community is privileged by instituting checks and balances within the system. NAFTA privileges the class of rich foreign investors, often large multinationals, by ensuring that immediate recourse to test the validity of state conduct against purely external standards are made available unilaterally. It gives impetus to economic liberalism as a political philosophy which privileges a distinct group—foreign investors.

Investor-State Procedures Substantially Increase the Corrosive Effect of International Investment Disciplines on Sovereignty

70. One important consequence of empowering foreign investors to enforce provisions of NAFTA has been to remove Chapter Eleven’s powerful enforcement provisions from the diplomatic, strategic and economic constraints that usually temper a State’s willingness to seek recourse to international dispute regimes. State-parties have an incentive to seek a balanced interpretation of trade and investment rules because they must also observe them.69 Private investors on the other hand, have no obligations under NAFTA and are therefore free of the moderating influence that reciprocity often brings to bear. Evidence that this dynamic is indeed at play can be found in the fact that no State-to-State dispute proceeding has yet been initiated under Chapter Eleven.

71. Therefore, by according countless private investors and corporations the right to invoke international arbitration to enforce the investment provisions of NAFTA, Canada and the other State-parties to NAFTA have substantially increased their exposure to legal claims that require them to defend domestic policies and laws before international tribunals.

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72. The notoriety, cost and potential liability associated with trade challenges and investor-State claims have been described as producing a “chill” over the development of domestic policy and law by governments. Moreover the inclination to engage in this form of self-censorship is accentuated when the ambit of the constraints imposed by a particular international commitment are unknown or uncertain. Negotiators of NAFTA and officers implementing its provisions have stated that the nature of the litigation that has resulted from Chapter eleven were unforeseen.

73. For policy and regulators, the task of attempting to fashion domestic measures that will not run afoul of Chapter Eleven requirements is significantly complicated by three factors. The first is the unprecedented and largely untested character of the disciplines set out in Chapter Eleven, which often engender broad concepts and terms which are not defined. The second has been the considerable inconsistency that has characterized the approach adopted by investor-State Tribunals to the interpretation of these disciplines. The third, results from the absence of any doctrine of judicial precedent or stare decisis to bind the determinations of such Tribunals. In these circumstances, it will often be impossible to ascertain with any reasonable degree of certainty precisely where the boundaries of NAFTA constraints will be drawn.

70 Mann, supra, note 69 at p. 33-34, and also see Schneiderman, supra, note 66 at pp. 534-535.

71 Thus, Mark Clodfelter, Assistant Legal Adviser, US Department of State, whose office prosecutes and defends the NAFTA claims in which the US is involved, stated: “The United States, and for that matter Canada and Mexico, took a very big step into the unknown when they signed onto Chapter 11”: Mark Clodfelter, “US State Department Participation in International Economic Dispute Resolution” 42 South Texas Law Review 1273 at p.1283 (2001).

72 For example, the prohibition against measures which expropriate foreign investments not only applies to direct and indirect measures, but also to measures that are “tantamount to expropriation.” None of these terms, including “expropriation”, are defined by NAFTA.


74 Many of the tribunals have been constituted with persons with no experience in investment arbitration or in public international law. Many of the arbitrators come from regions outside the Americas and have little or no Canadian or American experience in understanding the nature of the political factors that shape the disputes.
Moreover the scope of government actions that may be impugned by investor-State claims has been defined very expansively by tribunals seized of such disputes. For example, in *Ethyl Corporation v. Canada*, the disputing investor claimed that parliamentary debate regarding the environmental impacts of a gasoline additive manufactured by the company harmed its good will and international reputation. This harm, according to the company, represented an expropriation of its good will for which damages could be claimed under Chapter Eleven. Not long after losing a preliminary motion in which its objection to the Chapter 11 Tribunal’s jurisdiction to consider the claim was dismissed, Canada settled the case in favour of the disputing investor, paying damages and rescinding the legislation promulgated after that parliamentary debate.

In *United Parcel Service v. Canada*, the tribunal criticized Canada for submissions it had before the British Columbia Supreme Court regarding the appropriate standard of review of another award, *Metalclad v. Mexico*. The Tribunal stated that it was “troubled by Canada’s submission” that “chapter 11 Tribunals should not attract extensive judicial deference.” Moreover, this concern was explicitly taken in account by the Tribunal in rejecting Canada’s submission that the *United Parcel Service* case should be arbitrated in Canada.

Investor-State litigation has thus created a forum in which foreign investors have been able to attach legal liability and consequences to the most fundamental functions of a democratic government, namely:

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76 Mann, note 69 at pp. 72-73.

77 As indicated in paragraph 51, Mexico sought judicial review of an award made in favour of the disputing investor, Metalclad, in the B.C. courts. As a State-party to NAFTA, Canada intervened in the proceedings. Among other issues, the Canada made submissions concerning the proper scope for review of such an award under the provincial statutes concerning the recognition and enforcement of commercial arbitral awards: *The Commercial Arbitration Act, R.S.B.C. 1996, c. 55; International Commercial Arbitration Act, R.S.B.C. 1996, c. 233.*

parliamentary debate and the right of the federal government to have its views on the proper interpretation of domestic law represented to a court of superior jurisdiction.

The Intrusion of Investor-State Procedures into the Domain of National Courts and Tribunals

77. In addition to these impacts upon sovereignty and the constitutional norms of member states, NAFTA investor-State procedures also intrude into the domain of national courts and tribunals. This occurs in at least three ways. First, these procedures allow foreign investors to assert claims before international tribunals that would otherwise and historically have been within the exclusive jurisdiction of national courts. Second, investor-State claims empower international tribunals to effectively constitute themselves as courts of appellate jurisdiction for the purposes of reviewing the determinations of national courts, including courts of appellate jurisdiction. Finally, Chapter Eleven procedures empower international tribunals to award damages against sovereign states arising from the legislative and other actions of government, but without assuring that such proceedings or awards will be subject to any judicial oversight by the courts of the nation against which the award is made.

Intrusion on the Jurisdiction of National Courts

78. As set out above, claims brought by foreign investors under Chapter Eleven allege harm to their investments caused by some act or omission by a national, state, provincial or local government. Historically, such claims could have only been brought before the courts of the State against which the claim was made.

79. Indeed, NAFTA explicitly acknowledges that investor-State claims may fall within the competence of national courts. In this regard, Article 1121 requires, as pre-condition for asserting an investor-State claim, that the disputing investor waive its right to pursue a remedy concerning the impugned measure before
any administrative tribunal or court except for proceedings for injunctive, declaratory or other extraordinary relief.

80. Evidence of the overlap in jurisdiction between domestic courts and investor-State tribunals can also be found in the fact that several Chapter Eleven claims were brought only after domestic judicial remedies were sought. For example in Metalclad Corporation, the investor-State claim was initiated only after Metalclad sought judicial review of Mexico’s decision not to issue the building permit.

Investment Tribunals as Courts of Appellate Jurisdiction

81. There are several examples of Chapter Eleven tribunals assuming the role of an appellate court of the jurisdiction against which a claim has been asserted. In several of these cases, the tribunal has been called upon to determine whether the procedures and determinations of national courts in proceedings involving the interests of foreign investors are themselves in breach of NAFTA constraints.

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79 See Azinian, supra, note 43; Mondev International Ltd., supra, note 43; Metalclad Corporation, supra, note 44; The Loewen Group, Inc, supra, note 43.

80 Metalclad Corporation, supra, note 44.
82. For instance, in *The Loewen Group*, the tribunal rejected the State’s argument that the definition of “measure” in Chapter Eleven did not extent to judicial acts or the decision of a jury in a civil trial. The tribunal held that interpreting “measures” to include judicial acts not only accorded with the general principle of State responsibility under international law, but was also necessary in order to give effect to the objectives of NAFTA.\(^81\)

....an interpretation of ‘measures’ which extends to judicial acts conforms to the objectives of NAFTA as set out in Article 102(1), more particularly objectives (b), (c) and (e), namely to

(b) promote conditions of fair competition in the free trade area;

(c) increase substantially investment opportunities in the territories of the parties;

. . .

(e) create effective procedures for the implementation and application of this Agreement, for its joint administration and for the resolution of disputes.

83. Confronted with a similar argument, another Chapter Eleven Tribunal concluded that Chapter Eleven dispute procedures did not entitle claimants to seek review of national court decisions as though a Chapter Eleven tribunal was seized of plenary appellate jurisdiction.\(^82\) Nevertheless, the Tribunal went on to quote with favour the comments of a former President of the International Court of Justice who, noted that:\(^83\)

. . . [I]n the present century State responsibility for judicial acts came to be recognized. Although independent of Government, the judiciary is not independent of the State: the judgment given by a judicial authority emanates from an organ of the State in just the same way as a law promulgated by the legislature or a decision taken by the executive.

84. Concurring with this view, the Tribunal in *Loewen* also rejected the submissions of the respondent United States that NAFTA should be understood in accordance with the principle

\(^{81}\) *The Loewen Group, Inc.*, supra, note 43, at para. 46-49.

\(^{82}\) *Azinian*, supra, note 43, at para. 99.

that treaties are to be interpreted in deference to the sovereignty of states.\textsuperscript{84} It also concluded that, even if understood to include certain judicial acts, the term “measures” as defined by NAFTA would include judgments arising from purely private disputes. In dealing with this latter point, the Tribunal explicitly distinguished the decision of the Supreme Court of Canada drawing a distinction between the legislative, executive and administrative branches of government with respect to the application of the \textit{Canadian Charter of Rights and Freedoms}.\textsuperscript{85}

85. In addition to this quasi-appellate role, some Chapter Eleven tribunals have effectively constituted themselves as if they were a court of constitutional competence. For instance, in \textit{Metalclad Corporation}, the Tribunal determined that it was \textit{ultra vires} the authority of a municipal government to deny Metalclad a building permit on environmental grounds. In coming to this conclusion, the Tribunal ignored the decision of the Mexican Federal Court which had rejected an application by the disputing investor seeking review of the decision of the municipality on the grounds that review should first be sought by the State Administrative Tribunal. In disregarding the decision of a domestic Mexican Court, the Tribunal effectively assumed the role of a court of appeal.

86. By rendering judicial acts amenable to review under investor-State procedures, Chapter Eleven establishes a regime which may operate as a virtual appellate court operating outside the sovereign jurisdiction of the NAFTA Parties, and which is empowered to review the decisions even of their highest courts. At the same time, as I discuss below, the decisions of these tribunals are subject to little, if any,

\textsuperscript{84} Azinian, supra, note 43, para. 51.

\textsuperscript{85} Azinian, supra, note 43, para 55, referring to \textit{Retail, Wholesale and Department Store Union, Local 580 v Dolphin Delivery Ltd.}, [1986] 2 SCR 572.
judicial scrutiny. Indeed, in certain cases, there may no opportunity for judicial review whatsoever by the courts of the nation against which a claim is brought.

Limiting the Scope for Judicial Supervision

87. The third way in which Chapter Eleven’s enforcement procedures intrude into the sphere of authority of domestic courts arises from the absence of effective judicial oversight of international commercial arbitral proceedings. Under NAFTA, judicial oversight of investor-State suits is vested exclusively in the jurisdiction named as the place of arbitration, which may be in any nation that has ratified the 1958 New York Convention. The scope for judicial review is determined by the law of that jurisdiction. Typically, statutes defining the ambit of judicial oversight accord great deference to the arbitral awards of such international tribunals.

88. The only other opportunity for judicial oversight of an arbitral award arises when enforcement proceedings are brought in a particular jurisdiction. When this happens, a court may refuse enforcement on

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86 According to the official ratification website, 121 state parties have ratified the Convention: http://untreaty.un.org/English/sample/EnglishInternetBible/partI/chapterXXII/treatyl.asp

87 Redfern and Hunter, note 2, at pp. 431-433.

the limited grounds available for doing so.\textsuperscript{89} Even where enforcement is refused in one jurisdiction, the award remains enforceable in every other jurisdiction that is signatory to the \textit{New York Convention}, allowing an investor to shop for a convenient and sympathetic forum.

89. Similarly, a tribunal will decide the place of arbitration if the parties cannot agree. As I have already noted, in the \textit{United Parcel Service} case, the Tribunal decided that the arbitration should not take place in Canada in part because, in its view, Canada did not evince a sufficiently deferential attitude to Chapter Eleven tribunals in its submissions in the \textit{Metalclad Corporation} judicial review. Holding the arbitration in the United States means that Canadian courts will have no jurisdiction to review the proceedings or the Tribunal’s decision unless enforcement proceedings are brought in Canada. As noted above, even a court in the jurisdiction chosen as the place of arbitration would have limited authority to review such arbitral awards.

90. Thus, in addition to displacing the original jurisdiction of national courts to determine disputes between foreign investors and governments, Chapter Eleven also significantly circumscribes the superintending and reforming power of the superior courts in Canada.

\textbf{PART IV: THE DUBIOUS FOUNDATIONS AND UNCERTAIN FUTURE OF INVESTOR STATE PROCEDURES}

\textsuperscript{89} An award may be set aside on the basis that it is contrary to public policy of the country chosen to be the place of arbitration. Enforcement may be refused on this ground as well, but in this case the public policy at issue is that of the state in which enforcement is sought. For a discussion of the limited scope accorded this public policy review by the courts: see Redfern and Hunter, note 2, at pp. 471-474.
91. The establishment of international disciplines which may be unilaterally enforced by non-parties is anomalous as a feature of multi-lateral trade agreements. Similarly, incorporating such enforcement rights as an element of NAFTA represented a distinct departure from the norms of international trade agreements to which Canada was a Party.

92. Thus, the inclusion in NAFTA of disciplines amenable to private enforcement represented a markedly different approach than adopted by Canada in establishing the Canada-U.S. Free Trade Agreement (FTA) in 1989, which in other respects provided a template for NAFTA.\(^90\) The FTA contained investment disciplines virtually identical to those set out in NAFTA, but it did not give non-parties the right to enforce those disciplines through arbitration or by any other means. In fact, NAFTA was the first international trade agreement to include the right of unilateral third party enforcement.\(^91\)

93. Similarly, no right of private enforcement is provided for by the Agreement on Trade-Related Investment Measures or by any other agreement of the World Trade Organization (“WTO”).\(^92\) No individual or corporate entity has the right to invoke the dispute procedures of the WTO, but rather must rely upon the national government of its resident jurisdiction to do so on its behalf. The same is true with respect to the enforcement of NAFTA disciplines, save for those concerning foreign investment and set out in, or incorporated into, Chapter Eleven.\(^93\) Moreover, even when, in the rare case, international trade dispute procedures are invoked to address the complaint of a particular corporation, that corporate entity has no right to participate in the State-to-State dispute proceedings. Reserving access to the dispute

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\(^{91}\) See Donald M. McCrae’s introduction in Dawson, Whose Rights? The NAFTA Chapter 11 Debate, supra, note 24.

\(^{92}\) Final Act Embodying The Results of the Uruguay Round of Multilateral Trade Negotiations, signed at Marrakesh on April 15, 1994

\(^{93}\) Chapter 19 establishes dispute procedures with respect to Antidumping and Countervailing Duty Matters, and Chapter 20 establishes dispute settlement procedures with respect to all matters arising under the Agreement, with the exception of those arising Chapter 19. The dispute procedures delineated by Chapters 19 and 20 can only be invoked by the NAFTA Parties.
machinery of international trade agreements is consistent with, and follows from, the historic norm that the protection of foreign nationals abroad is a function of the state.

94. The dramatic developments in international law represented by NAFTA Investment Rules occurred with a noticeable lack of debate in the parliamentary fora of nations now a party to such international agreements. That debate was only to come, at least in certain jurisdictions, several years later in response to efforts to establish a Multilateral Agreement on Investment (MAI) for which NAFTA was the model. A similar paucity of critical analysis exists in academic or other arenas, with commentary most often being limited to a technical exegesis of these international regimes, which leaves the theoretical or policy foundations for such dramatic developments in international law largely unexplored and untested.

95. For example, the establishment of powerful international enforcement mechanisms, such as those engendered by NAFTA investor-State procedures, has often been promoted as serving the interests of developing nations. It is argued that these procedures bring the rule of law into previously unequal relationships and foster foreign direct investment in poorer nations. In fact, there is little, if any, evidence to support the claim that developing countries are the beneficiaries of these developments. Indeed, notwithstanding the rise of international foreign investment regimes, the bulk of foreign direct investment still flows to the wealthiest of nations and, if anything, the gap between rich and poor nations has grown. Moreover, the lack of accountability that attends investor-State procedures fundamentally undermines, rather than fosters, the institutions of democratic governance that are fundamental to the rule of law.

96. Nevertheless, carried along by the forces of globalization and liberalization, the 1990s was a period in which there was a significant proliferation of bilateral investment treaties. However, developing countries

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have increasingly resisted these developments and have recently been joined in their opposition by non-governmental organizations based in developing countries, and by certain governments in those richer nations as well. Evidence of this resistance can be found in the failed efforts by the promoters of these regimes to establish multi-lateral investment regimes based on the BIT or NAFTA model.

97. For example, negotiations in the Uruguay Round of international trade negotiations that ultimately led to the establishment of the World Trade Organization (WTO) failed to yield a comprehensive set of investment rules along the lines of those engendered by NAFTA, notwithstanding the persistent efforts of the United States to achieve that objective. The Agreement on Trade-Related Investment Measures (TRIMS) that was included as an element of the Marrakesh Agreement Establishing the World Trade Organization represented little more than a codification of the status quo of the 1947 General Agreement on Tariffs and Trade (GATT).

98. The failure of the Uruguay Round negotiations to lead to the establishment of more substantial and far-reaching investment disciplines was commonly attributed to resistance by developing countries. To finesse their perceived recalcitrance, a strategy was developed among certain developed countries to establish such binding disciplines in stages, beginning with those like-minded wealthier nations and then broadening the ambit of their agreement to include all members of the WTO. Accordingly, in 1995, the twenty-nine member countries of the Organization for Economic Co-operation and Development undertook the task of completing an enforceable agreement for the protection and promotion of foreign investment in the form of the MAI.

99. On April 28, 1998, negotiations of the MAI were suspended and subsequently abandoned because of resistance to the agreement in the United States Congress, the withdrawal of France from the

97 Trebilcock and Howse, supra note 94 at pp. 351-52.

98 Trebilcock and Howse, supra note 94, pp. 357-358.

99 Trebilcock and Howse, supra note 94, p. 358.
negotiations, waning support from the business community, and the coordinated action of citizen organizations in Canada, France, New Zealand, and elsewhere.\textsuperscript{100}

100. The potential impact of the MAI on the sovereignty, independence and regulatory roles of government, and on cultural policy, the environment; and labour rights, were the most prominent issues in the public debate that arose in Canada, the United States and other OECD countries concerning this proposed investment treaty. As noted, it is significant that the MAI initiative represented the first occasion on which new rules concerning foreign investor protection enjoyed any measure of wide-spread public discussion or debate.

101. The issue of foreign investment has once again arisen in the context of a new round of trade negotiations that was initiated at the most recent meeting of the WTO Ministerial Council in Doha, Qatar. However, the decision about whether to initiate such negotiations, and the modalities for such negotiations, will not be resolved until the next Ministerial Council which is scheduled for Cancun Mexico in 2003.

102. In sum, the advent of international treaties according foreign investors the right to unilaterally invoke binding arbitration to assert claims against nation states represented a dramatic departure from the norms of both international and domestic law. It is only very recently that the broader implications of these developments have come to light and attracted any significant degree of informed discussion and debate. With that debate, has come growing skepticism about and opposition to the establishment of international investor-State arbitral regimes such as the one established by Chapter Eleven.

\textsuperscript{100} Trebilcock and Howse, supra note 94, pp. 362-365 and also see UNCTAD, Lessons From the MAI, United Nations, 1999. UNCTAD/ITE/IIT/MISC. 22.
103. I make this affidavit in support of an application and for no other or improper purpose.

AFFIRMED before me at the City of ________, in the ____________ )
        of ________________ on ___________ )
        April _____, 2003 )    DR. MUTHUCUMARASWAMY SORNARAJAH

A Commissioner for taking affidavits, etc.