

**IN THE ARBITRATION  
UNDER CHAPTER ELEVEN OF THE NAFTA  
AND THE ICSID ARBITRATION (ADDITIONAL FACILITY)  
RULES**

BETWEEN:

MOBIL INVESTMENTS CANADA INC. &  
MURPHY OIL CORPORATION

Claimants

AND

GOVERNMENT OF CANADA

Respondent

ICSID Case No. ARB(AF)/07/4

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**CLAIMANTS' RESPONSE TO THE SECOND NAFTA  
ARTICLE 1128 SUBMISSIONS OF MEXICO AND THE  
UNITED STATES OF AMERICA**

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ARBITRAL TRIBUNAL:

Professor Hans van Houtte, President  
Professor Merit Janow  
Professor Philippe Sands

February 7, 2011

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## I.

### INTRODUCTION

1. Claimants hereby submit our response to the second Article 1128 submissions of Mexico and the United States.<sup>1</sup>

2. The United States's submission supports Claimants' view that a proper interpretation under international law of the term "consistency" in Section 2(f)(ii) of the Interpretative Note to Annex I refers both to the NAFTA *and* domestic law. Mexico's submission is only partly correct, as it refers only to domestic law and ignores entirely the express terms of the NAFTA, cited by the United States, that require reference also to the terms of the NAFTA and the Vienna Convention on the Law of Treaties ("VCLT"). Both the United States and Mexico view the question of whether a subordinate measure can be "consistent" with a listed measure while imposing additional and/or more onerous requirements than the prior legal regime as a fact-driven inquiry that must be decided on a case-by-case basis. As Claimants have made clear throughout this arbitration, the Guidelines substantially increase the pre-existing local content requirements both qualitatively and quantitatively and, on the facts of this case, cannot be considered "consistent" with the prior legal regime consisting of the Accord Acts, the Hibernia and Terra Nova Benefits Plans, and the Board's decisions approving those Plans.

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<sup>1</sup> See Second Submission of the United States of America ("USA 2"), and Submission of the United Mexican States Responding to Questions Raised by the Tribunal ("Mexico 2"), both dated January 21, 2011. For reasons set forth in paragraphs 21 through 22 below, this submission also contains a brief commentary on Canada's Reply to Claimants' Post-Hearing Brief ("Canada's Reply PHB").

## II.

### CLAIMANTS' COMMENTS ON MEXICO'S AND THE UNITED STATES'S RESPONSES TO THE TRIBUNAL'S QUESTIONS

- A. As a matter of law, is the determination of whether a subordinate measure is “consistent with the measure” to be assessed by reference to (i) the national law governing the measure under the authority of which the subordinate measure has been adopted, or (ii) the law of the NAFTA, or (iii) both? If it is or includes the law of the NAFTA, what is the standard by which such assessment is made, and the available sources thereof?**

3. It is clear that the United States agrees with Claimants on the correct approach to interpreting Section 2(f)(ii) of the Interpretative Note to Annex I. *First*, NAFTA Article 1131 requires the Tribunal, as a matter of first principles, to apply international law to determine the scope of a Party's Annex I reservation.<sup>2</sup> *Second*, in a case where a disputing Party does not request a binding interpretation from the NAFTA Free Trade Commission (“FTC”) on the scope of its Annex I reservation pursuant to Article 1132, Article 1131 dictates that the reservation be analyzed in accordance with the principles

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<sup>2</sup> USA 2, ¶ 4; *see also* CA-3, NAFTA, art. 1131(1); CA-1, NAFTA, art. 102(2); Tr. 1132:11-16; Claimants' Reply to Canada's Post-Hearing Submission (“Claimants' Reply PHB”), ¶ 12.

of treaty interpretation provided for in the VCLT.<sup>3</sup> These uncontroversial propositions do not appear to be in dispute.<sup>4</sup>

4. Applying the VCLT principles leads the United States and Claimants to the same conclusion: “both the law of the NAFTA and national law are relevant” to the determination of whether a subordinate measure is “consistent with” a measure listed in a Party’s Annex I reservation.<sup>5</sup> Claimants agree that domestic law is a relevant consideration: it presents an essential first hurdle which a subordinate measure must clear before the question of consistency as a matter of the NAFTA even arises. If a measure is not a “subordinate measure” as a matter of domestic law, then it can never fall within the scope of a Party’s Annex I reservation. As noted above, Mexico’s conclusion that “consistency” is determined by domestic law is correct only in part.<sup>6</sup> Further, while “authority” may be viewed predominantly as a question of domestic law, “consistency” must have an international law content for the reasons stated by the United States, with which Claimants agree.<sup>7</sup>

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<sup>3</sup> USA 2, ¶ 4. *See also* Tr. 1124:8-21, 1126:18-1127:1; Claimants’ Reply PHB, ¶ 3.

<sup>4</sup> Canada’s Post-Hearing Submission (“Canada’s PHB”), ¶¶ 2-3, 23-24.

<sup>5</sup> USA 2, ¶ 3; *see also id.* ¶ 9; Tr. 1132:6-16, 1141:7-22, 1153:7-22; Claimants’ Reply PHB, ¶¶ 3-5, 17-18, 23-24.

<sup>6</sup> Mexico 2, ¶ 3. Canada selectively quotes the United States to support its position that the other two NAFTA Parties confirm the importance of domestic law in deciding whether a measure is “subordinate” under Section 2(f)(ii). In so doing, Canada ignores the significance that the United States accords to the law of the NAFTA by relegating its statements on this point to a brief footnote. *See* Canada’s Reply PHB, ¶¶ 36-37 & n. 57.

<sup>7</sup> *See* USA 2, ¶ 7. *See also infra* ¶¶ 5-10; Tr. 1131:6-1132:20, 1141:13-22; Claimants’ Reply PHB, ¶¶ 4-5, 17-18, 23-24.

5. If a measure does constitute a “subordinate measure” as a matter of domestic law, then the question of its “consistency” with the listed measure must be determined as a matter of the law of the NAFTA. This result applies because “a ‘subordinate measure’ falls within the definition of a ‘measure’ that has been exempted from conforming to certain NAFTA obligations.”<sup>8</sup> The United States agrees with Claimants that the relevant considerations include:

the context of the reservation the Parties negotiated, including the NAFTA obligation from which the listed measure is reserved *and the degree of the reserved measure’s and subordinate measure’s non-conformity with that obligation*, in light of the other elements of the reservation that would be relevant.<sup>9</sup>

6. As stated by the United States, the Tribunal should compare (i) the reserved measure’s non-conformity with the relevant NAFTA obligation prior to the adoption of the subordinate measure and (ii) the subordinate measure’s non-conformity with the relevant NAFTA obligation.<sup>10</sup> This conclusion accords with Claimants’ position that the term “consistent with” requires that there should be no decrease in conformity between the NAFTA and the measure listed in

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<sup>8</sup> USA 2, ¶ 7. *See also* Memorial, ¶¶ 163-166; Reply, ¶¶ 99-104; Claimants’ Submission on the US and Mexico’s NAFTA Article 1128 Submissions (“Claimants’ First 1128 Response”), ¶¶ 40-43; Tr. 91:13-92:7, 98:17-99:4, 1123:20-1124:4, 1124:22-1125:6, 1128:20-1129:12, 1131:15-1132:5; Claimants’ Reply PHB, ¶¶ 4, 17.

<sup>9</sup> USA 2, ¶ 9 (emphasis added).

<sup>10</sup> *Id.*; *see also id.* ¶ 10.

Annex I as a result of the adoption of the subordinate measure.<sup>11</sup>

7. The factors considered by the United States as part of its VCLT analysis also underline the correctness of Claimants' arguments. First, Claimants and the United States proffer identical definitions of the ordinary meaning of the term "consistent": "in accord," "compatible," or "without contradiction."<sup>12</sup> Notably, this definition of "consistent" is almost identical to the definition of "conformity": "agreement" and "congruity, harmony, accordance."<sup>13</sup>

8. The United States further notes the special meaning of the term "measure" under the NAFTA: i.e., "any law, regulation, procedure, requirement or practice."<sup>14</sup> This broad definition provides further reason why "consistency" under Section 2(f)(ii) should be assessed under the same matrix as "conformity" under Article 1108(1)(c). The latter provision refers to "an amendment to any non-conforming *measure*." If a "measure" under the NAFTA can consist of an informal

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<sup>11</sup> See Claimants' First 1128 Response, ¶¶ 41-43; Tr. 93:8-96:19, 98:17-99:4, 1130:9-1132:5, 1141:13-1142:5, 1154:6-1161:9; Claimants' Reply PHB, ¶¶ 17-18, 23-24, 27-32.

<sup>12</sup> See USA 2, ¶ 5; Claimants' First 1128 Response, ¶ 38 & n. 51.

<sup>13</sup> See The American Heritage Dictionary Second College Edition, p. 309 (1991) ("[s]imilarity in form or character: agreement"); Webster's Ninth New Collegiate Dictionary, p. 276 (1991) ("correspondence in form, manner, or character: agreement"); Merriam-Webster's Collegiate Dictionary, p. 262 (2003) ("correspondence in form, manner, or character: agreement"); Oxford English Dictionary Online ("[c]orrespondence in form or manner; agreement in character; likeness, resemblance; congruity, harmony, accordance"), available at [dictionary.oed.com](http://dictionary.oed.com) (last checked February 1, 2011).

<sup>14</sup> USA 2, ¶ 5; see also CA-2, NAFTA, art. 201.

“practice,” then “amendment” must necessarily encompass more than formal amendments, because informal practices are not formally amended. The relevant inquiry must be whether a measure has the effect of an amendment, no matter its formal designation under domestic law. It is clear that the Guidelines have the practical effect of amending the prior legal regime and fail the ratchet rule.<sup>15</sup> They therefore fall outside the scope of Canada’s Annex I reservation.

9. The United States and Claimants also have identified the same relevant contextual elements as informing the interpretation of the term “consistency.” As the United States notes, “the Parties’ desire to promote transparency” is “one of the key objectives of the NAFTA.”<sup>16</sup> Claimants already have explained why interpreting “consistency” as referring only to domestic law would undermine the transparency of the Parties’ Annex I Schedules.<sup>17</sup> The United States also refers to NAFTA Article 1132, which provides that a Party may request that the FTC issue a binding interpretation on the issue of whether a challenged measure in a NAFTA Chapter 11 arbitration falls within the scope of a reservation or exception under Annex I.<sup>18</sup> The FTC is composed of the ministers of trade of the NAFTA Parties.<sup>19</sup> It is ideally suited to assessing whether a new subordinate measure is consistent with the

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<sup>15</sup> Memorial, ¶¶ 179-192; Reply, ¶¶ 107-110; Claimants’ First 1128 Response, ¶¶ 38-40, 42-43; Tr. 62:6-65:14, 1142:22-1143:11; Claimants’ Opening Presentation, Slide 31; Claimants’ Closing Presentation, Slide 33; Claimants’ Post-Hearing Brief (Redacted) (“Claimants’ PHB”), ¶¶ 6-7, 23; Claimants’ Reply PHB, ¶¶ 25-26, 33.

<sup>16</sup> USA 2, ¶ 8.

<sup>17</sup> Tr. 1158:11-22; Claimants’ Reply PHB, ¶ 18.

<sup>18</sup> USA 2, ¶ 4.

<sup>19</sup> See NAFTA art. 2001 (FTC to be made up of cabinet-level representatives of the NAFTA Parties).



international bargain negotiated by the NAFTA Parties and reflected in the Annex. It has no capacity to engage in the intricate analysis of a single Party's domestic law that Canada suggests is the sole relevant exercise. The reference by the United States to Article 1132 thus accords with the Claimants' observation that, contrary to Canada's position, none of the NAFTA Parties is expert in each other's domestic administrative law, so that resolving questions of "consistency" under Section 2(f)(ii) depends on the NAFTA's terms and not on the intricacies of domestic administrative law doctrines.<sup>20</sup>

10. Mexico's submission throws into sharp relief the perils inherent in an approach by which "consistency" derives its meaning solely from domestic norms. Mexico observes that:

Legal systems (national laws) are not finished or at rest, to the contrary they are in a continuous process of creation (i.e. a legal system is a succession of momentary legal systems; a constant process of building regulations); consequently, in order to preserve the uniformity of a legal system, the system must be provided with the necessary rules to determine whether a certain measure is valid, as well as the means to correct it.<sup>21</sup>

Mexico's observation is correct as a general matter; it is also why grandfathering regimes, such as Article 1108(1) and Annex I of the NAFTA, are put into place. Because legal systems have a tendency to evolve, the NAFTA Parties wished to ensure in 1994 that their legal systems did not evolve in the wrong direction: in a manner that decreased the conformity of the listed measures with the Treaty.

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<sup>20</sup> Claimants' Reply PHB, ¶ 18.

<sup>21</sup> Mexico 2, ¶ 2.

11. Canada’s argument that *all* subordinate measures adopted under *all* provincial measures are exempted from the NAFTA by virtue of its Annex I reservation for provisional measures, if correct, further demonstrates why an international law approach to “consistency” is so essential.<sup>22</sup> The Parties, including their constituent states and provinces, otherwise would be free to undermine the entire structure of the NAFTA through the enactment of subordinate regulations that were authorized and consistent with their own general administrative law. Assessment of consistency by reference to the NAFTA itself provides a far more stable and predictable framework, consistent with the goals of the Treaty.

12. The conclusion of the United States that “consistency” is a question of both domestic and NAFTA law provides a definitive answer to Canada’s most recent allegation that Claimants “attempt to misuse the NAFTA to appeal the decisions of the Canadian courts.”<sup>23</sup> The Canadian domestic courts did not purport to determine “authority” and “consistency” as a matter of the law of the NAFTA.<sup>24</sup> Canada’s repeated pleas that the Tribunal “defer” and “not overturn” the decisions of the domestic courts are thus a *non sequitur*.<sup>25</sup>

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<sup>22</sup> Canada’s Reply PHB, ¶ 26.

<sup>23</sup> Canada’s Reply PHB, ¶ 1.

<sup>24</sup> See USA 2, ¶ 9; see also *id.* ¶ 10. For the avoidance of doubt, Claimants continue to dispute that the Canadian domestic courts determined the issues of “authority” and “consistency” for the purposes of domestic law; they relied instead on a “reasonableness” standard. Claimants’ First 1128 Response, ¶¶ 44-47; Tr. 97:15-98:9, 1137:9-1139:5; Claimants’ PHB, ¶¶ 17-20; Claimants’ Reply PHB, ¶¶ 15-16, 22.

<sup>25</sup> See, e.g., Canada’s Reply PHB, ¶¶ 3, 42, 53, 58.

13. The United States’s submission demonstrates that a subordinate measure may be “consistent” with a listed measure as a matter of national law and yet “inconsistent” for the purposes of Section 2(f)(ii). It is indisputable that an action taken by a government may be valid under its domestic law but invalid under a treaty or other international law obligation. Canada’s attempt to argue otherwise and to rest entirely on domestic law leaves no room for the Tribunal to conduct the analysis required of it under international law.<sup>26</sup>

14. Three particular arguments posited by Canada in its latest brief are inconsistent with the correct recognition by the United States of the proper place of international law in the analysis. *First*, Canada argues that “an international tribunal which ignores domestic law risks that its decision will conflict with those of domestic courts.”<sup>27</sup> Because, in this case, the domestic courts did not consider consistency under the

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<sup>26</sup> As Claimants have observed, Canada improperly leaps from a concession that domestic court decisions are facts to be considered to a conclusion that domestic law applies as a rule of decision absent a denial of justice. Claimants’ Reply PHB, ¶¶ 21-22. However, even the authorities that Canada cites in its latest brief, make clear that domestic court decisions constitute “additional evidence of the situation” and “one of the many factors which have to be considered.” See Canada’s Reply PHB, ¶ 50 & n. 90 (citing **CA-91**, *Case Concerning Elettronica Sicula S.p.A. (ELSI)* (*United States v. Italy*), ICJ Reports 1989, p. 15, Judgment of July 20, 1989, ¶ 99; **CA-85**, *Amco Asia Corp. v. Republic of Indonesia*, ICSID Case No. ARB/81/1, Award of November 20, 1984, ¶ 177). Moreover, the fact that the ICJ in *ELSI* and the ICSID Tribunal in *Amco* concluded that the domestic decisions were consistent with their own decisions does not mean they considered themselves bound to defer to the municipal decisions on international law issues. They simply decided that they did not have to reach the issue.

<sup>27</sup> Canada’s Reply PHB, ¶ 35.

NAFTA, the Tribunal risks no conflict with the domestic courts in deciding this issue.<sup>28</sup>

15. *Second*, Canada argues that “the domestic law of the three NAFTA parties have highly developed rules to determine if a domestic measure is authorized by and consistent with another domestic measure.”<sup>29</sup> The fact that domestic law may consist of “more detailed rules” on a particular issue does not mean that only domestic law is applied and that international law is disregarded.

16. *Third*, Canada claims that “ignoring domestic laws created to decide the subordination of one domestic measure to another infringes the sovereignty of the NAFTA countries

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<sup>28</sup> Canada refers fourteen times to Claimants’ supposed requests to the Tribunal to “overturn” findings of the Canadian courts. See Canada’s Reply PHB, ¶¶ 58, 64, 69, 72, 78, 80, 82, 83, 84, 85, 88, 92, 108, 116. Canada fails to comprehend that Claimants are asking the Tribunal to determine issues of international, and not domestic, law. Canada’s reference in its latest brief to the recent ICSID Award in *RSM v. Grenada* is similarly misguided. See Canada’s Reply PHB, ¶¶ 3, 51-52; **RA-169**, *RSM Production Corporation v. Grenada* (ICSID Case No. ARB/10/6) Award, 11 March 2009. Claimants are not asking this Tribunal to “reopen” any municipal court decisions. Further, as Claimants pointed out at the hearing and in our written briefs, the issue of “consistency,” even as a matter of Canadian law, was not “distinctly ... put in issue” or “distinctly determined” by the Canadian courts, even if the word “consistent” did feature in *obiter* comments rendered by the courts, and used to misleading effect by Canada in this arbitration. See *supra* n. 24. The rule enunciated by the *RSM* tribunal would only be relevant if Claimants were asking the Tribunal to re-examine the question of the “reasonableness” of the Guidelines as a matter of Canadian administrative law. Needless to say, that question is not at issue in this arbitration.

<sup>29</sup> Canada’s Reply PHB, ¶ 35.

which created those laws.”<sup>30</sup> Canada ignores the fact that entry into a treaty regime is itself an exercise of a nation’s sovereignty. By signing and ratifying the NAFTA, Canada voluntarily agreed that domestic regulators can continue to enact subordinate measures but, as applied to investors of the Treaty partners, they must be consistent with the NAFTA. Holding Canada to this freely undertaken treaty commitment does not infringe its sovereignty.

17. As a final matter, the United States’s submission confirms the error of Canada’s attempt to read the Description element out of its reservation for the Federal Accord Act. As the United States observes, Section 2 of the Interpretative Note to Annex I “requires [NAFTA] Parties to elaborate certain ‘elements’ of the reservation.”<sup>31</sup> These elements include “the description of any liberalization commitments for, and remaining non-conforming aspects of, the reserved measure.”<sup>32</sup> The requirement to set forth all of these elements must mean that each element is significant, and not solely for liberalization purposes. The descriptions of the non-conforming aspects of the measures were what the political bodies of each NAFTA Party had to consider in determining whether to sign or to accede to the treaty. The descriptions thus represented the essence of the deal that the Parties understood to have been struck, not the afterthought that Canada now suggests. Indeed, under Canada’s original position in this arbitration, “if a NAFTA party has described the non-conforming aspect of its measure under the

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<sup>30</sup> *Id.*

<sup>31</sup> USA 2, ¶ 8 (emphasis added); *see also id.* ¶ 10 (Tribunal should consider “the particular elements of the non-conforming measure entry” in Annex I, among other things); CA-6, NAFTA, Annex I, Interpretative Note, § 2.

<sup>32</sup> USA 2, ¶ 8 (emphasis added); *see also* CA-6, NAFTA, Annex I, Interpretative Note, § 2 (g).

‘Description’ heading in Annex I, only subordinate measures which address that aspect of the measure will be reserved.”<sup>33</sup> The United States also refers to Section 3 of the Interpretative Note and highlights, as Claimants did, that “all elements of the reservation shall be considered” and that the “reservation shall be interpreted in light of the relevant provisions of the Chapters against which the reservation is taken.”<sup>34</sup> Claimants have repeatedly stressed that Canada did provide a description of the “non-conforming aspects” of the Accord Act, which described the benefits plan requirement but not the Board’s ability to enact guidelines and interpretation notes, and which should not now be ignored.<sup>35</sup>

**B. As a matter of (i) national law, and / or (ii) the law of the NAFTA, can a subordinate measure be “consistent with the measure” if it imposes additional and / or more onerous burdens on a legal or natural person who is subject to the subordinate measure?**

18. The United States and Mexico share the view that consistency is a fact-specific inquiry requiring a case-by-case analysis. The analytical framework developed by the United States, which results from its analysis of Section 2(f)(ii) under the VCLT, provides a list of relevant considerations, including:

- (i) the domestic legal context of the measure; (ii) the particular elements of the non-conforming measure

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<sup>33</sup> Rejoinder, ¶ 109.

<sup>34</sup> USA 2, ¶ 8; *see also* CA-6, NAFTA, Annex I, Interpretative Note, § 3.

<sup>35</sup> Claimants’ First 1128 Response, ¶¶ 35-36; Tr. 92:14-93:5, 1117:19-1124:4; Claimants’ PHB, ¶ 15; Claimants’ Reply PHB, ¶¶ 5-11.

entry and the subordinate measure, including, *inter alia*, the extent of the non-conformity of each with the obligation against which the measure is reserved; and (iii) the specific facts and circumstances of the case.<sup>36</sup>

19. Applying this analysis to the facts of the case, it is clear that (i) it is, at best, questionable whether the Guidelines are “consistent” with the prior legal regime as a matter of domestic law;<sup>37</sup> (ii) the Guidelines were not adopted under the authority of any of the non-conforming aspects of the Accord Acts as listed in the Description element of Canada’s reservation;<sup>38</sup> (iii) the Guidelines impose more onerous burdens on Claimants than the pre-2004 local content regime; and (iv) the Guidelines render the pre-existing local content regime more non-conforming with Article 1106.<sup>39</sup> Therefore, the Guidelines are not covered by Canada’s Annex I reservation.

20. Mexico’s conclusion that “a case by case analysis is required” to determine whether an additional and/or more onerous burden renders a subordinate measure “inconsistent” deserves further comment.<sup>40</sup> It appears from Mexico’s response to this question that there is space for a finding that a subordinate measure is “inconsistent” with the listed measure, even where the former measure has been upheld as a matter of

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<sup>36</sup> USA 2, ¶ 10; *see also supra* ¶ 5.

<sup>37</sup> *See supra* nn. 24 & 28. *See also* CA-53, *Hibernia and Petro-Canada v. C-NOPB*, Supreme Court of Newfoundland and Labrador Court of Appeal, 2008 NLCA 46, ¶ 150 (Sept. 4, 2008) (*per* Justice Rowe, dissenting) (“[T]he Guidelines impose additional R&D requirements inconsistent with [Decision] 97.02 .... The same is true regarding [Decision] 86.01[.]”).

<sup>38</sup> *See supra* n. 35.

<sup>39</sup> *See supra* n. 15.

<sup>40</sup> *See* Mexico 2, ¶ 6.

domestic law, depending on the Tribunal’s “case by case” analysis of any additional burdens imposed by the subordinate measure. The degree to which the Guidelines impose additional and more onerous burdens than the prior legal regime necessitates a finding of inconsistency in this case.<sup>41</sup>

### III.

#### CLAIMANTS’ OBSERVATIONS ON CANADA’S REPLY TO CLAIMANTS’ POST-HEARING BRIEF

21. As agreed in the parties’ joint letter, consistent with the Tribunal’s direction that post-hearing briefs be “succinct,”<sup>42</sup> the post-hearing briefs were intended to be a substitute for oral rebuttal of closing arguments, as well as to provide answers to the specific questions posed by the Tribunal.<sup>43</sup> Claimants honored that agreement by presenting our rebuttal to Canada’s closing argument in succinct, bullet point format, and by devoting half our initial post-hearing brief to responding directly to the Tribunal’s questions. To the contrary, Canada’s Reply to Claimants’ Post-Hearing Brief is effectively a restatement of its entire case. Its 77 full-size pages are largely repetitive of points Canada already has made and that Claimants already have answered. Moreover, Canada did not respond to some questions of the Tribunal,

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<sup>41</sup> See *supra* n. 15. For the avoidance of doubt, Claimants disagree with Mexico’s contention that a subordinate measure can sometimes be consistent with a listed measure even if it imposes additional and/or more onerous burdens. See Mexico 2, ¶¶ 4-5. This analysis is fatally undermined because Mexico, like Canada, has failed to conduct a proper analysis of Section 2(f)(ii) under the VCLT, as directed by NAFTA Article 1131. See *supra* ¶¶ 3-6, 18.

<sup>42</sup> See Tribunal letter of Nov. 9, 2010, ¶ 4.

<sup>43</sup> Joint letter from the Parties, Nov. 5, 2010, p. 2.



such as those involving domestic authorities relating to damages, until its second post-hearing brief.

22. The Tribunal will recall that, in response to Canada's objections, it required Claimants to submit a redacted version of our Post-Hearing Brief, which omitted content that was directly responsive to a question posed by the Tribunal and which the parties had agreed would be addressed in that brief. While Claimants believe that similar relief would be appropriate in this situation, we appreciate that the Tribunal is ready to bring the case to completion. Accordingly, and because Canada's reply largely covers trodden ground, we are prepared to rest on our prior submissions. However, the integrity of the record requires a brief response to certain egregious misstatements in Canada's latest submission and also to arguments and authorities submitted in that brief that should have been included in Canada's initial post-hearing brief.

- At many junctures in its reply brief, Canada simply restates arguments, failing to reply to, or even acknowledge, Claimants' prior responses and rebuttals to its points. For example, Claimants already have responded to Canada's argument that Article 1106 does not prohibit a requirement that *indirectly* implicates the use of a local service, by demonstrating that the Guidelines *directly* require the *use or accordance of a preference* to local services.<sup>44</sup> Indeed, Canada's argument completely loses sight of the fact that the *sole purpose* of the Guidelines was to increase the amount of money being poured into the province for local services; there was nothing indirect or incidental about

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<sup>44</sup> See Canada's Reply PHB, ¶¶ 13-16. See also Claimants' First 1128 Response, ¶¶ 56-58; Tr. 77:2-81:19, 1108:4-1110:11; Claimants' PHB, ¶¶ 9, 12.

this at all.<sup>45</sup> Canada also disclaims the argument that a subordinate measure must be adopted “under the authority of and consistent with” a non-conforming aspect of a listed measure in a Party’s Annex I reservation, yet fails to dispute Claimants’ observation that this interpretation was *first posited by Canada*.<sup>46</sup> As a third example, Canada continues to argue that Hibernia’s financial statements somehow provide support for its argument that Claimants have not incurred any loss. Canada does not even purport to address Claimants’ explanation why its argument on this point is wrong.<sup>47</sup> Claimants have also explained, on numerous occasions, that Mr. Rosen’s damages model incorporates a deduction for future spending that Claimants would have undertaken in the ordinary course of business.<sup>48</sup> Yet Canada chooses to ignore this fact completely, focusing instead on whether individual

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<sup>45</sup> See, e.g., Tr. 792:12-19 (President Van Houtte: “[W]as it more a question of money, or was it more a question of research and development? A: It was a question of money. We were being motivated by the legislation, which talked of requirement for research and development expenditures, and what we were searching for was what would be an appropriate expenditure.”).

<sup>46</sup> See Canada’s Reply PHB, ¶¶ 29-31; Rejoinder ¶ 109; *supra*, p. 12 and n.33. Canada simply says that Claimants’ reliance on the statements made in its Rejoinder is “not correct,” without further explanation.

<sup>47</sup> See Canada’s Reply PHB, ¶ 129; Claimants’ PHB, ¶ 32.

<sup>48</sup> See Memorial, ¶ 218; Reply, ¶¶ 266, 299; Tr. 135:18-136:5, 1174:20-1175:13; Claimants’ PHB, ¶ 31. The fact that Claimants calculated more than \$140 million in “ordinary R&D spending,” not included in our damages calculation, rebuts Canada’s argument that Claimants are seeking a “windfall.” See Canada’s Reply PHB, ¶ 122; Claimants’ Opening Presentation, Slide 29.

expenditures are “in the ordinary course” or not.<sup>49</sup> Although space precludes a more complete recital of the instances in which Canada chooses simply to disregard Claimants’ prior submissions in an attempt to have the last word on the matter, we urge the Tribunal to review those submissions for responses to many of the arguments raised in Canada’s latest brief.

- On numerous occasions, Canada inappropriately cites to Claimants’ Post-Hearing Brief to support its mischaracterizations of our arguments. For example, Canada cites to paragraph 6 of Claimants’ brief as stating “because the [benefits] plans do not contain a quantum of spending, [Claimants] can choose not to spend if they wish.”<sup>50</sup> Claimants said nothing of the sort. Rather, Claimants stated that the Board’s consistent approvals of the Projects’ POAs demonstrated that they were “spending on R&D and E&T at levels consistent with those [Benefits] plans.”<sup>51</sup> In another mischaracterization, Canada represents that Claimants “argue that the Guidelines force them to *use* local services to carry out R&D in the Province,” citing to paragraph 9 of Claimants’ brief.<sup>52</sup> Claimants in fact stated in that paragraph (and elsewhere) that they cannot make expenditures under the Guidelines without using *or according a preference to* local services.<sup>53</sup>

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<sup>49</sup> Canada’s Reply PHB, ¶¶ 122-126

<sup>50</sup> Canada’s Reply PHB, ¶ 57 & n. 95.

<sup>51</sup> Claimants’ PHB, ¶ 6.

<sup>52</sup> Canada’s Reply PHB, ¶ 15 & n. 24 (emphasis added),

<sup>53</sup> Claimants’ PHB, ¶ 9. *See also id.*; Reply, ¶¶ 77-84; Claimants’ First 1128 Response, ¶ 10; Tr. 77:8-80:22, 1108:4-1110:1, which demonstrate the fallacy of Canada’s arguments that Claimants could spend tens of millions of dollars to comply with the Guidelines without using local goods or services.

This is a key difference. Canada also cites to paragraph 15 of Claimants’ post-hearing brief for support that Claimants “dismiss the application” of Section 3 of the Interpretative Note to Annex I.<sup>54</sup> This is incorrect; rather, we *apply* Section 3, arguing that only the chapeau of that provision is relevant in a case such as the present, where there is no discrepancy between the elements of a reservation.<sup>55</sup> Given the scope of this submission, we cannot point out each and every inappropriate reference to Claimants’ brief, but we urge the Tribunal to pay close attention to the support proffered for each of Canada’s allegations — and, of course, to take note of Canada’s continued failure to cite any support at all for many of its propositions, which we have noted before.<sup>56</sup>

- Canada also introduces a series of factual errors regarding Claimants’ past R&D and E&T spending and their expenditure obligations under the Guidelines. *First*, Canada argues that, as a percentage of revenue, the Guidelines require the Claimants to spend less on R&D and E&T than they were spending before the Guidelines came into effect.<sup>57</sup> This “percentage of revenue” analysis, first employed in Canada’s Rejoinder, is hugely misleading. For example, Canada includes the year 1997 for Hibernia, a year which saw only two months of oil production.<sup>58</sup> The analysis cannot even be carried out with regard to Terra Nova

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<sup>54</sup> Canada’s Reply PHB, ¶ 24 & n. 45.

<sup>55</sup> See Claimants’ PHB, ¶ 15.

<sup>56</sup> See, e.g., Reply, ¶ 146 *et seq.*; Claimants’ PHB, ¶¶ 2, 13, 27; Tr. 71:1 *et seq.*

<sup>57</sup> Canada’s Reply PHB, ¶ 91.

<sup>58</sup> Rejoinder, ¶ 210.

because it did not earn any revenue until 2002.<sup>59</sup> *Second*, Canada argues that Claimants will spend less under the Guidelines than they spent before. This is incorrect and a perversion of the record. In the years preceding the Guidelines, Hibernia’s annual SR&ED-approved expenditures exceeded \$10 million only once, and \$5 million only twice.<sup>60</sup> By contrast, the Guidelines require HMDC to make R&D and E&T expenditures in excess of \$10 million each year through 2011, and in excess of \$5 million each year through 2020.<sup>61</sup> *Third*, Canada’s statement that the Board “consistently fulfilled its obligation to approve expenditures on R&D and E&T” is clearly erroneous.<sup>62</sup> In the very early years of the Hibernia project, the Board issued letters confirming its satisfaction with annual benefits reports. However, these letters ceased in 1989.<sup>63</sup> The Hibernia project did not even report the quantity of R&D and E&T expenditures separately until 1997.<sup>64</sup> With regard to Terra Nova, Canada points to two documents, neither of which even purport to constitute approval of the project’s R&D expenditures.<sup>65</sup>

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<sup>59</sup> *Id.* ¶ 211.

<sup>60</sup> **CE-144**, Hibernia SR&ED Acceptance Chart.

<sup>61</sup> Third Expert Report of Howard N. Rosen, Schedule 2.

<sup>62</sup> *See* Canada’s Reply PHB, ¶ 65.

<sup>63</sup> *See* Memorial, ¶ 90 & n. 159.

<sup>64</sup> *See* Reply, ¶ 157.

<sup>65</sup> One document is a letter from the Board to Terra Nova reminding the operator to consider Newfoundland and Canadian institutions when research needs arise in relation to an area of R&D specifically enumerated in Terra Nova’s Benefits Plan. *See* Reply, ¶¶ 163-164. *See also* **RE-18**, Letter from H. Stanley, CNLOPB, to

- Canada states that Claimants submitted no evidence “of practice by any of [the NAFTA Parties or] the other 189 members of the United Nations” in response to the Tribunal’s question regarding the existence of evidence of state practice and *opinio juris* to support the obligation to protect an investor’s legitimate expectations.<sup>66</sup> This is an inappropriate attack. Canada is well aware that, in response to its own request, the Tribunal limited the authorities Claimants could submit in response to this question “exclusively to materials relating to authorities and cases already cited in the pre-hearing submissions.”<sup>67</sup>
- Canada disputes the relevance of the domestic authorities submitted by Claimants in response to the Tribunal’s question regarding damages,<sup>68</sup> on the grounds that “domestic law has different principles for the award of damages depending on the type of breach and obligation involved.”<sup>69</sup> This is unremarkable; it goes without saying that the nature of the obligations at issue in the domestic cases is not identical to the treaty obligations at issue here. However, Canada cannot deny that, in appropriate cases, domestic courts award

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G. Bruce, Petro-Canada (Feb. 3, 1999). The other is an internal Board memo recommending that Terra Nova had satisfied the reporting requirements under Condition 7 of the Board’s Approval of Terra Nova’s Benefits Plan. *See* Reply, ¶ 159; **RE-20**, Memorandum from H. Stanley, CNLOPB, to Board Members (Feb. 11, 2000).

<sup>66</sup> Canada’s Reply PHB, ¶ 98.

<sup>67</sup> *See* Tribunal Letter of November 9, 2010, ¶ 3.

<sup>68</sup> *See* Legal Questions to the Parties from the Tribunal, to be Addressed in Closing Arguments (Oct. 21, 2010), ¶ 5(c).

<sup>69</sup> Canada’s Reply PHB, n. 234.

damages in circumstances where a number of unresolved variables mean that the exact quantum of the plaintiff's loss cannot be calculated: for example, in lost profits cases. The basic principles applied by the domestic courts in those cases can be of some utility to a tribunal dealing with similar variables in an award of damages for a treaty violation. Presumably, that is why the Tribunal asked for input on domestic authority.

- Canada's treatment of the domestic authorities on damages is both misleading and unfair. *First*, Canada attempts to rely on two US cases and one Canadian case to argue that the domestic law of both countries requires a plaintiff to prove the *amount* of its damages with reasonable certainty. In doing so, Canada ignores the clear statements in the US cases on which it relies: "*the amount of loss need not be proven with 'certainty.'*"<sup>70</sup> Further, the Canadian case cites to the very case law on which Claimants rely, which establishes that: "[a]n assessment of future lost profits must, of necessity, be an *estimate.*"<sup>71</sup> *Second*, Canada cites to one US case and one Canadian case as support for the proposition that domestic courts will not base compensation on predictions of the future price of oil.<sup>72</sup> Canada ignores the emphasis in both cases on the

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<sup>70</sup> **RA-165**, *Kidder, Peabody & Co. Incorporated v. IAG International Acceptance Group N.V.* (Dec. 21, 1998) 1998 WL 888988, \*5 (S.D.N.Y.) (emphasis added); *see also* **RA-170** *Kenford Co., Inc. v. Erie County*, Court of Appeals of New York, 67 N.Y.2d 257, 262 (May 6, 1986).

<sup>71</sup> *See* Canada's Reply PHB, n. 313; **RA-166**, *Magnussen Furniture Inc. v. Mylex Ltd.*, 2008 CarswellOnt 1352, ¶ 77 (March 14, 2008) (emphasis added); *see also* Claimants' PHB, ¶ 63 & n. 153.

<sup>72</sup> *See* Canada's Reply PHB, n. 281

alternative remedies available to prevent future loss on the plaintiff's part; remedies which are unavailable under the NAFTA.<sup>73</sup> Claimants have noted that the availability of such remedies renders an award of future damages less imperative under domestic law.<sup>74</sup> *Third*, Canada cites to a Canadian case as support for the proposition that "[d]omestic courts also refuse to grant damages which have not been incurred."<sup>75</sup> This ignores that fact that Claimants' damages have been incurred.<sup>76</sup> In any event, the Canadian court emphasized that the plaintiff would have recourse to the courts in the future to claim damages as they arose.<sup>77</sup> *Finally*, the Mexican decision on which Canada relies simply stands for the proposition, undisputed by Claimants, that a plaintiff must prove that it has suffered a loss in order to claim damages.<sup>78</sup>

- Canada's treatment of *Waste Management* is also, at best, misleading. Canada blends its discussion of the Decision on Jurisdiction and the Award on the Merits

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<sup>73</sup> See **RA-163**, *America Southwest Corp. v. Allen*, Supreme Court of Mississippi, 336 So.2d 1297, 1300-1301 (August 24, 1976); **RA-164** *Erehwon Exploration Limited v. Northstar Energy Corp.*, Alberta Court of Queen's Bench, 15 Alta. L.R. (3d) 200, ¶¶ 50-55.

<sup>74</sup> Claimants' PHB, ¶¶ 67-68.

<sup>75</sup> See Canada's Reply PHB, n. 257.

<sup>76</sup> See Reply, ¶¶ 236-239, 246-248.

<sup>77</sup> **RA-167**, *Markesteyn v. R.*, Federal Court of Canada Trial Division, 2000 CarswellNat 1960, ¶ 19 (Aug. 11, 2000); see also *supra* n. 74.

<sup>78</sup> **RA-168**, Civil Appeal 154/2003, *Promociones Russek, S.A. de C.V.*, Ninth Era, Seventh Collegiate Court of Appeals for Civil Matters for the First Circuit, S.J.F. y su Gaceta, XVII, June 2003, Jurisprudencia I.7o.C.J/9, p. 727 (10 April 2003).



in that case in such a way as to represent that the tribunal actually deferred to the decisions of the Mexican domestic courts. In its decision on jurisdiction, the tribunal merely noted that “a NAFTA tribunal does not have ‘plenary appellate jurisdiction’ in respect of decisions of national courts, and whatever may have been decided by those courts as to national law will stand unless shown to be contrary to NAFTA itself.”<sup>79</sup> Indeed, if the Tribunal reviews Canada’s brief closely, it will see that no specific pin cite is provided for the alleged “deferral” to the Mexican courts.<sup>80</sup>

#### IV.

#### CONCLUSION

23. For all the reasons stated here and in prior oral and written submissions by the Claimants, we respectfully urge the Tribunal to hold that the Guidelines violate Canada’s obligations under Articles 1105 and 1106 of the NAFTA and to award Claimants full damages to compensate for this violation.

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<sup>79</sup> **RA-132**, *Waste Management Inc. v. United Mexican States*, Decision on Mexico’s Preliminary Objection to Jurisdiction (ICSID Case No. ARB(AF)/00/3), 26 June 2002, ¶ 47.

<sup>80</sup> See Canada’s Reply PHB, ¶¶ 44-45 & nn. 79-81.

Respectfully submitted,



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