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UNDER THE UNCITRAL ARBITRATION RULES AND THE NORTH AMERICAN FREE TRADE AGREEMENT

SUPPLEMENTAL MEMORIAL OF THE INVESTOR (SECOND PHASE)

BETWEEN:

POPE & TALBOT, INC.

Claimant / Investor

- and -

GOVERNMENT OF CANADA

Respondent / Party

1140 Bay Street, Suite 300, Toronto, Ontario M5S 2B4 Tel. (416) 966-8800 Fax. (416) 966-8801 www.appletonlaw.com

816 Connecticut Avenue, NW, 12TH Floor, Washington DC 20006 Tel. (202) 293-0900 Fax. (202) 293-0988

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SUPPLEMENTAL MEMORIAL OF THE INVESTOR (SECOND PHASE)

SECTION ONE: OVERVIEW

I. GENERAL INTRODUCTION

This phase of the Investor's NAFTA Claim concerns Canada's fundamental failure to meet its obligations to provide treatment in accordance with international law and national treatment. In response to Canada's Counter-Memorial (Second Phase), the Investor makes the arguments detailed below.

The NAFTA is designed to facilitate the process of economic integration between its three Parties. Chapter 11 of the NAFTA carries out the NAFTA objective of increasing substantially investment opportunities in the territories of all NAFTA Parties. To encourage investment from all three partner countries, NAFTA Parties have obliged themselves to provide investors from other NAFTA Parties and their investments with legal security, including: national treatment and treatment in accordance with international law. Fundamentally such security means that investors will be free from the risk of arbitrary or discriminatory conduct in any government measure.

Canada has argued, in response to the submissions in the Investor's Memorial (Second Phase), that international law and national treatment should be narrowly construed by this Tribunal. These arguments run counter to the express wording of the NAFTA, its objects and purpose, and the applicable rules of treaty interpretation. In effect, Canada has ignored 50 years of development in international economic law related to trade and investment.

The fundamental difference between the disputing Parties on the interpretation of NAFTA Articles 1102 and 1105 is reflected in the statements of Mr. George and Mr. Valle submitted in support of Canada's Counter-Memorial (Second Phase). These statements are important because they demonstrate the validity of the Investor's claim that Canada's legal world view is reflected through the conduct of its Minister and officials. Canada clearly supports an ad hoc and non-transparent system of discretionary allocations that underpin the Export Control Regime. NAFTA Articles 1102 and 1105 require exactly the opposite.

II. BURDEN OF PROOF AND EFFECT ON NON-PRODUCTION OF EVIDENCE

One of the key features of all Investor-State arbitrations is that there are a number of inherent imbalances between the respective positions of the disputing parties. While such imbalances are somewhat corrected through the equal and consensual nature of international arbitration, there is still inequality in relation to the possession and production of evidence. Canada is in the position that it uniquely possesses the knowledge of how it implemented and operated the Export Control Regime. This imbalance becomes particularly relevant when the NAFTA Party refuses to produce documents as Canada has done over the course of this arbitration. Accordingly, international law provides for the shifting of the burden of proof and the drawing of adverse inferences in those instances in which the state Party fails to produce relevant documents in its possession.

The Investor has made out its case that Canada has violated NAFTA Article 1102 and 1105. The fact that Canada has refused to provide relevant documents strengthens the need for the burden of proof to be shifted to Canada, and that adverse inferences should be made by this Tribunal.

In Canada's response letter to the Investor's Request for Documents dated February 29, 2000, it was stated by Canada that about 100,000 documents were under review.[1] Previous to that, in conversations before the Tribunal figures upwards of over a million pages had been mentioned by counsel for Canada. These figures were relied on by Canada to justify its request to delay the production of the requested documents.

In its letter to the Investor of July 25, 2000, Canada advised the Investor that "Canada **does not disclose** or produce documents that constitute confidences of the Queen's Privy Council of Canada."[2] [Emphasis added] It appears that Canada has admitted in its July 25th letter that there are relevant documents covered by Cabinet confidences that Canada has not disclosed to the Investor or this Tribunal. Canada later provided a letter from the Clerk of the Privy Council to the Tribunal on August 30, 2000 stating that Canada claimed "privilege at this time for twelve documents which are confidences of the Queen's Privy Council for Canada..."[3] The Investor submits that there are likely many additional documents that have not been produced. Canada's statement that there are only twelve documents subject to Cabinet confidences does not address the fact that there are likely numerous related and supporting documents that have also not been produced. It is frequently the case that a cabinet briefing note references, relies and/or attaches

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[1] Schedule 9.

[2] Schedule 10

[3] Schedule 11.

numerous lower level briefing memoranda. Effectively the Investor has been refused access to those documents through Canada's refusal to produce twelve documents.

In summary, the Investor submits that this Tribunal ought to draw an adverse inference from Canada's decision to not produce these relevant documents and the Investor invites the Tribunal to make such adverse inferences from Canada's non-production of particular documents.

SECTION TWO: TREATMENT IN ACCORDANCE WITH INTERNATIONAL LAW

I. OVERVIEW

1. The disputing parties to this arbitration differ widely on the appropriate meaning that this Tribunal should give to NAFTA Article 1105. There is no disagreement between Canada and the Investor with respect to the proposition that the text of NAFTA Article 1105 obliges Canada to provide treatment in accordance with international law[4]. In light of the exchange of memorials between the disputing parties in this phase of the arbitration, there appears to be a significant disagreement as to the meaning that this Tribunal should give that obligation.

2. There is no disagreement between the parties with respect to the fact that NAFTA Article 1105 provides a base upon which government treatment is to be assessed under international law. The difference between the disputing parties appears to arise over where that base is set. Canada suggests that NAFTA Article 1105 only requires minimal protections for foreign investors. In Canada's view, these protections are chiefly procedural in nature and appear to relate exclusively to the concept of "full protection and security". Canada further adds that for there to be a violation of NAFTA Article 1105, the government must engage in a significant level of interference with the interests of the foreign investor otherwise the NAFTA would become a process to deal with every alleged disappointment suffered by it[5].

3. The Investor maintains its arguments made within its Memorial (Second Phase) with respect to the meaning of the term "international law" used in NAFTA Article 1105. The Investor has set out at length in its Memorial (Second Phase) a description of the content of NAFTA Article 1105 as it relates to the issues arising in this Claim. For the Investor, treatment in accordance with international law provides substantive and procedural protections for foreign investors investing in another country. The purpose of these protections is to enhance the ability of foreign investors to engage in investment activities in a predictable fashion. International law imposes a number of treatment obligations upon governments that have developed over the last century into both substantive and procedural obligations. In summary, these obligations provide Investors with legal security once an investment is made.

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[4] Memorial (Second Phase) at para. 101 and Counter-Memorial (Second Phase) at para. 217.

[5] Counter-Memorial (Second Phase) at para. 208.

4. Canada has correctly pointed out that there is no need to demonstrate any difference in treatment between investors or investments in order to demonstrate a breach of NAFTA Article 1105[6]. All that is necessary is to show is that a government has not provided treatment in accordance with international law. The Investor differs with Canada when Canada submits that there is some high threshold that investors must meet in order to demonstrate that there is a violation of NAFTA Article 1105. Neither the NAFTA nor international law itself contains any such threshold test for the erosion of these international obligations.

5. Canada suggests that the test for treatment in accordance with international law has been encapsulated by the 1926 decision of the US-Mexican claims commission in the *Neer* case. The Investor rejects that proposition. While there is no doubt that the types of actions that constituted a violation of denial of justice according to the *Neer* Tribunal would still constitute a violation of international law treatment today, Canada's position fails to properly take into account developments in international law, especially in the area of international economic law since the 1920's.

II. THE PROPER INTERPRETATION OF NAFTA ARTICLE 1105

6. The term "international law" is used in other NAFTA provisions[7] and its meaning is well-known. In its Counter-Memorial (Second Phase), Canada has argued that the term international law used in NAFTA Article 1105 should somehow have a particular meaning so that it should be narrowly interpreted by this Tribunal.[8] Canada has not provided any definition of international law within the NAFTA to be able to support its view, nor could it, because the NAFTA does not contain any definition of international law. More extraordinarily, Canada has argued that treaty law could not constitute part of international law. This suggestion misstates a fundamental and informing principle of international law.

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[6] Counter-Memorial (Second Phase) at para. 237.

[7] For example, NAFTA Article 1131 makes reference to deciding the issues in dispute in accordance with the NAFTA and applicable rules of international law.

[8] Counter-Memorial at para. 219.

7. The Investor has referred to Article 38 of the Statute of the International Court of Justice, which lists four different elements that constitute international law[9]. These four elements are:

> (a) international conventions, whether general or particular, establishing rules expressly recognized by the contesting States;
>
> (b) international custom, as evidence of a general practice accepted as law;
>
> (c) the general principles of law recognized by civilized nations; and
>
> (d) subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determinations of the rules of law.

The first of the elements contained in this list specifically refers to the contribution of treaty law as an integral element of what constitutes international law.

8. The NAFTA is an international convention that establishes rules that have been expressly recognized by each of the NAFTA Parties. Accordingly, treaty obligations in general, and those within the NAFTA in particular, form a part of international law and thus are covered by the scope of NAFTA Article 1105.

9. Counsel for Canada argues that the presumption against redundancy in treaty interpretation means that NAFTA Article 1105 must have a meaning that is different from other obligations contained within Chapter 11 of the NAFTA. This argument displays a lack of understanding of the content of NAFTA Article 1105.

10. NAFTA Article 1105 incorporates international law obligations into NAFTA, including customary international law obligations about subjects such as national treatment and expropriation. NAFTA Articles 1102 and 1110 deal specifically with these subjects and these articles contain specific provisions, which broaden the general international law obligations contained within NAFTA Article 1105. The mere existence of NAFTA Articles 1102 and 1110 does not somehow detract from the existence of the general national treatment or compensation obligations in international law. For example, *Akehurst's Introduction to International Law* (7th ed.) refers to the customary law of expropriation being part of this international law standard when it states:

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[9] This list was set out in paragraph 103 of its Memorial (Second Phase). Reporters Note 1 in § 102 of the *Restatement of the Foreign Relations Law of the United States (Third)* confirms that Article 38 is commonly treated as an authoritative statement of the sources of international law. Investor's Supplemental Book of Authorities, Tab 1.

> The rules on expropriation of foreign property are comprised in the so-called minimum international standard which belongs to the core of the traditional rules of state responsibility for the treatment of aliens[10].

NAFTA Article 1110 goes further than the basic international expropriation rules by codifying a specific process for detailing compensation set at Fair Market Value, and by broadening the types of investments for which the NAFTA will provide compensation.

III. THE EVOLUTION OF INTERNATIONAL LAW

11. The NAFTA must be interpreted in a manner that is consistent with developments in other international economic agreements such as the WTO/General Agreement on Tariffs and Trade ("GATT"). This inter-relationship between the NAFTA and the WTO/GATT is made explicit in the NAFTA's Preamble, which includes a statement that the NAFTA Parties are resolved to:

> BUILD on their respective rights and obligations under the *General Agreement on Tariffs and Trade* and other multilateral and bilateral instruments of cooperation;

This Preamble also states that the NAFTA Parties are resolved to:

> ENSURE a predictable commercial framework for business planning and investment;
>
> ENHANCE the competitiveness of their firms in global markets;

12. There have been significant developments in international economic law since the Tribunal's determination in the *Neer* claim. The advent of the United Nations system and the Bretton Woods Agreements (which created institutions such as the IMF and the World Bank) have increased the level of treatment that states accord foreign investors. Multilateral and plurilateral agreements such as the WTO/GATT have had the significant effect of increasing the level of protection offered to foreign investors operating in other states. Finally, the large number of bilateral or plurilateral investment agreements, such as the NAFTA itself, have also had a significant impact by increasing the types of international protections accorded to international investors and their investments. While the *Neer* case was important in the context of its time, it was before these international economic developments and it therefore cannot be reasonably said to constitute the

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[10] P. Malanczuk (ed.), *Akehurst's Modern Introduction to International Law* (7th ed.) at 235. Investor's Supplemental Book of Authorities, Tab 9.

authoritative statement on the treatment of investors and investments in international law today.

13. Canada has mischaracterized the findings of the NAFTA Tribunal in the *Metalclad* claim in relation to the treatment Mexico was required to provide the investment under international law. The NAFTA Tribunal found that Mexico had not met the NAFTA Article 1105 standard in a large number of circumstances with respect to *Metalclad.* These deficiencies included, for example:

a) the denial of the right to a fair hearing;[11]
b) lack of sufficient evidence on the record;[12]
c) breach of legitimate expectations;[13]
d) absence of transparency rules and processes;[14]
e) acting on the basis or irrelevant considerations;[15] and
f) acting beyond the scope of lawful authority.[16]

The Tribunal held that each and every one of these deficiencies constituted a violation of NAFTA Article 1105. Accordingly, Canada is simply not correct when it advocates that an act of outrage as a necessary precondition for a finding of a violation of a NAFTA Party's obligations under NAFTA Article 1105.

14. The NAFTA provides interpretive guidance on this point. NAFTA Article 102(1) sets out objectives that are to be used in interpreting the NAFTA. This article contains six objectives towards which the NAFTA is to be interpreted, which include to:

> Promote conditions of fair competition in the free trade area: and
> Increase substantially investment opportunities in the territories of the Parties;

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[11] *Metalclad* at para. 51.

[12] *Metalclad* at paras. 51 and 88.

[13] *Metalclad* at para. 80.

[14] *Metalclad* at para. 88.

[15] *Metalclad* at para. 92.

[16] *Metalclad* at paras. 86 and 95.

15. Furthermore, the chapeau of NAFTA Article 102(1) states that these objectives are to be elaborated more specifically through its principles, which include the principle of transparency. Accordingly, there can be little doubt that the international law obligations contained within NAFTA Article 1105 were intended to carry out the goals of the NAFTA, which include the creation of legal security to enhance investment opportunities within a free trade regime governed by fair competition and transparency.

IV. THERE IS NO MINIMAL THRESHOLD FOR INTERNATIONAL LAW TREATMENT

16. The operative obligation contained within NAFTA Article 1105(1) is that Canada provide treatment to investors and their investments from other NAFTA Parties in accordance with international law. Canada has suggested that the title over the obligation "minimum standard of treatment" somehow suggests that NAFTA Article 1105(1) should be interpreted minimally. While the titles over NAFTA obligations are not be ignored in the context of the article, the title "minimum standard of treatment" does not suggest that this obligation should be given a narrow or minimal interpretation.

17. The express meaning of the text of NAFTA Article 1105 is clear: NAFTA Parties are to provide treatment to investments of investors from other NAFTA Parties in accordance with international law. While there may be some need to understand what the content of international law may be, there is no uncertainty as to the meaning of this article. There is accordingly no support for Canada to suggest that the wording of NAFTA Article 1105 is unclear and that interpretive recourse must be made to the title over the operative treaty article[17].

18. NAFTA Article 1105 provides that Canada must provide a level of treatment to foreign investors beneath which it cannot go. This obligation creates "legal security" for foreign investors to ensure that they can understand how they are being treated in the host country and to ensure that they receive fair transparent treatment with respect to their investment activities[18]. Treatment in accordance with international law required by NAFTA Article 1105 is a foundation upon which other international treaty obligations can be built. For example, with Articles 1102 and 1110, the NAFTA Parties respectively incorporated and

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[17] Counter-Memorial (Second Phase) at para. 226.

[18] See paragraphs 101 to 193 of the Memorial (Second Phase).

made specific additions to the international law principle of national treatment and the customary international law formulation of expropriation.[19]

19. Canada has argued that every decision of an international tribunal dealing with treatment in accordance with international law has focussed on a high threshold of harm. In the words of Canada:

> In summary, all tribunals that have applied or commented on the minimum standard have held that a breach may only be found when the facts are extreme and government conduct is egregious[20].

Canada's conclusion about treatment in accordance with international law does not follow from the decisions of international tribunals and results in Canada's inappropriate conclusions about the meaning of international law.

20. There are a number of decisions from the US-Mexican Claims Tribunal that have found governments to have violated their international law obligations owed to foreign investors where the conduct has constituted a breach of international law that is less than "an outrage". For example:

a) In the case of *Samuel Davies* v. *Mexico*[21], the Tribunal awarded Mr. Davies damages for his cords of wood, which had been seized by junior-rank Mexican officials.

b) In *Okie* v. *Mexico*[22], the Tribunal found that the provision of Mexican law that did not permit a refund of overpaid customs fees to Mr. Okie violated international law and it ordered Mexico to repay the funds. This violation of international law was caused by a Mexican regulatory measure of general application and no finding of any particular intent was made by the Tribunal.

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[19] Such as the broad definition of investment that can be expropriated or the specific definition of how to calculate Fair Market Value that is contained in NAFTA Article 1110(2).

[20] Counter-Memorial (Second Phase) at para. 281.

[21] *Samuel Davies* v. *Mexico* (1929) IV RIAA 517. Investor's Supplemental Book of Authorities, Tab 2.

[22] *Okie* v. *Mexico* (1926) IV RIAA 55. Investor's Supplemental Book of Authorities, Tab 4.

c) In *G.W. MacNear, Inc* v. *Mexico*[23], the US-Mexico Claims Tribunal found that the improper detention, and eventual sale, of the investor's wheat at the border, constituted a violation of international law.

In none of these cases did the Tribunal find that there existed a pre-condition that Mexico's conduct include the finding of a particular "intent" before a finding could be made against it. Accordingly, Canada's general argument about the threshold of harm required to demonstrate an act inconsistent with international law is simply incorrect.

21. Counsel for Canada has placed great reliance upon part of the decision taken by the US-Mexico Claims Tribunal in *Neer*. The tribunal in *Neer* provided a test whereby to find that there was a "denial of justice" in this particular case, it would be necessary for the claimant to demonstrate "an outrage, bad faith, wilful neglect of duty or insufficiency of government action so far short of international standards that every reasonable and impartial person would recognise its insufficiency"[24]. Counsel for Canada is incorrect when it suggests that the *Neer* test applies exhaustively to the complete range of governmental acts which are inconsistent with international law. Canada is mistaken for the following reasons:

a. The "*Neer* test" is a statement upon the extent of the customary international law as it was in 1926. This test does not reflect the many developments in international economic law which have taken place since it was decided; and

b. The *Neer* claim is about a particular type of act inconsistent with a State's international law obligation regarding the sufficiency of the judicial process. At no time did the US-Mexican Claims Tribunal find that the high threshold of the "*Neer* test" should be applied to all breaches of international law – indeed the terms of the decision itself are restricted to only dealing with the issue of denial of justice and not any other international law issue[25]. The US-Mexican Claims Tribunal referred to the *Neer* case standard in only three other cases. In each of

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[23] *G.W. MacNear, Inc* v. *Mexico* (1928) IV RIAA 373. Investor's Supplemental Book of Authorities, Tab 3.

[24] Counter-Memorial at para. 238. This threshold has is referred to in this Supplemental Memorial as the "*Neer* test".

[25] *American Journal of International Law* 555 (1927) at 556 (esp. para. 4). It is also important to note that the American judge on the Tribunal dissent from the high threshold test for the finding of a denial of justice in the *Neer* claim.

these cases, it was made clear that this standard only applied to situations involving allegations of denial of justice[26].

22. A large number of "denial of justice" cases have been cited to suggest that the *Neer* test reflects the state of international law in general[27]. Indeed, Counsel for Canada has stated that the *Neer* test has been applied by tribunals other than the US-Mexican Claims commission to be the "seminal standard" of the meaning of the international minimum standard. Canada's specific statement is:

> Other international bodies have applied the *Neer* standard, referring to it as the "standard habitually practised among civilised nations" or even "general principles of law". The formulation of the standard in *Neer* continues to be the seminal statement of the meaning of the international minimum standard[28]. (Footnotes omitted)

This statement is incorrect in fact and leaves an inaccurate impression of the law.

23. Canada relies upon the decision of the French-UK Claims Commission in *Chevreau v. Great Britain*[29] to support its statement that the *Neer* test was applied by that tribunal. The *Chevreau* case was about whether it was appropriate to deny Mr. Chevreau access to counsel before he was summarily deported during wartime. The Tribunal found that while Mr. Chevreau's deportation was within the bounds of international practice, his treatment was not. Nowhere does this Tribunal award make reference to the *Neer* case or to those specific principles outlined as the *Neer* test.

24. Furthermore, Counsel for Canada relies upon the ICSID decision in *AMCO Asia Corp* v. *Indonesia*[30] to support its claim that the *Neer* test is a "general principle of law". This statement is also incorrect. The ICSID Tribunal in *AMCO Asia* considered the situation

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[26] *Walter Faulkner* v. *Mexico* (1928) IV RIAA 67 at 71. Investor's Supplemental Book of Authorities, Tab 6, (regarding arrest and imprisonment); *B.E. Chattin* v. *Mexico* (1927) IV RIAA 282 (regarding denial of justice and illegal arrest). Investor's Supplemental Book of Authorities, Tab 6.; and *Gertrude Massey* v. *Mexico* (1927) IV RIAA 155 at 160. (Especially see paragraph 21 which specifically indicates the narrow circumstances in which the US-Mexican Claims Tribunal used the *Neer* test.) Investor's Supplemental Book of Authorities, Tab 5.

[27] Counter-Memorial at paras. 238, and 258 - 266.

[28] Counter-Memorial at para. 266.

[29] *Chevreau v. Great Britain* (1931), 27 *AJIL* 153. Canada's Book of Authorities, Vol. II, Tab 31.

[30] *AMCO Asia Corp. v. Indonesia*, Award on Merits (1984) 1 ICSID Reports 337 at para. 198. Canada's Book of Authorities, Vol. II, Tab 32.

of conduct by the Government of Indonesia which made the building of a hotel impossible. In coming to its award, the Tribunal found that the denial of due process was a breach of international law as a general principle of law. This statement by the ICSID Tribunal does not include any of the *Neer* test requirements that the government conduct constitute an "outrage, bad faith, willful neglect of duty or insufficiency of government action so far short of international standards that every reasonable and impartial person would recognize it insufficiency". The *AMCO Asia* Tribunal reinforces the position taken by the Investor in this claim that the modern customary international law finds that the denial of due process constitutes a violation of international law.

25. International tribunals have been clear that all acts which are inconsistent with international law can be the basis for a finding by a tribunal. For example, in the case of *Gertrude Massey* v. *Mexico*[31], Mexico argued that the conduct of the Mexican official should not be attributable to Mexico because he was a low level official. In rejecting this argument, the US-Mexico Claims Tribunal pronounced:

> I believe that it is undoubtedly a sound general principle that, whatever misconduct on the part of any such persons, whatever may be their particular status or rank under domestic law, results in the failure of a nation to perform its obligations under international law, the nation must bear the responsibility for the wrongful acts of its servants[32].

26. Canada has further argued that the content of NAFTA Article 1105 should only be applied to the most egregious situations, and that it should not have any application to any other situations[33]. Canada provides no support for this, which have the effect of narrowing the application of the NAFTA obligation from the plain meaning of its text.

27. Counsel for Canada attempts to articulate a single standard for what it calls the "international minimum standard of treatment", which consists of nothing more than a limited expression of the "full protection and security" standard, despite the fact that the text of NAFTA Article 1105 clearly delineates that this is but one aspect of the requirement that NAFTA Parties treat NAFTA investments in accordance with international law.[34] Canada can only find support for this constraining view in sources

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[31] *Gertrude Massey* v. *Mexico* (1927) IV RIAA at 155.

[32] IV RIAA at 159.

[33] Counter-Memorial (Second Phase) at paras. 235-240.

[34] Canada cites Professor Brownlie in support of its position that international law requires no more than observance of the "full protection and security" standard even though Professor Brownlie even acknowledges that there exists no single standard of treatment for foreign investments.

that largely predate not only the Great Depression, but also the rise of the modern regulatory state and the explosion of international rule-making that characterised the second half of the twentieth century.

28. Aside from its strained interpretation of the recent award of the Tribunal in *Metalclad and the Government of the United Mexican States*, the only cases cited by Canada to delimit the scope of its so called "international minimum standard of treatment" are "full protection and security" cases.

29. Canada's failure to acknowledge the wide-ranging development of international norms and principles over the latter part of the twentieth century, with respect to the obligations it owes to foreign investment in its territory, flies in the face of the common wisdom that international law, as a system, possesses an inherently dynamic and evolutionary character. If the Canadian argument that Article 1105 really only requires observance of a rudimentary "full protection and security" standard were correct, it would appear that international law related to foreign investment was frozen sometime prior to the Second World War. In effect, Canada has dismissed the subsequent considerable developments that are widely recognised as establishing the basis for modern international economic law.

V. GOOD FAITH

30. Counsel for Canada has properly submitted that the international law principle that states carry out their treaty obligations in good faith (*pacta sunt servanda*) is not a separate obligation contained within the NAFTA[35]. Canada is incorrect when it argues that this principle does not apply to NAFTA Article 1105. The Investor has already set out the fundamental role of this principle in international law. Any reference to international law must incorporate good faith otherwise NAFTA Article 1105 would be rendered a hollow shell.

31. Counsel for Canada urges that this Tribunal should not accept that it is obliged to carry out its treaty obligations in good faith, as such an interpretation would give meaning to Canada's obligations within the NAFTA. International law and the NAFTA form the governing law of this arbitration. Canada is calling upon this Tribunal to not recognize one of the most fundamental principles of international law in its interpretation of that law. The Investor submits that Canada's most extraordinary contention must be rejected.

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[35] Counter-Memorial (Second Phase) at para. 317.

32. Canada argues that the principle of *pacta sunt servanda* only applies between state parties to international agreements and that it is therefore impossible to apply this principle to the obligation to provide treatment in accordance with international law contained in NAFTA Article 1105 [36]. While international law is negotiated between state governments, international law agreements can and do create obligations for how states must treat foreign investors [37]. *The Restatement of the Foreign Relations Law of the United States (Third)* provides:

> States are responsible for violations of their obligations under international law. See § 206, Comment *e*. In general, the obligation and the remedy run to a particular state. The victim of a violation can make claim for one or more forms of relief, *e.g.*, cessation of the violation, compensation, specific performance, repair or some other restoration of the situation, apology. See § 902. In some circumstances the victim may resort to reasonable forms of self-help. See § 905. By special agreement, the victim may have special remedies, or resort to special "machinery", *e.g.*, judicial or arbitral proceedings, mediation or conciliation by international bodies[38].

The NAFTA specifically created a process through Section B of NAFTA Chapter 11 that permits certain investors to raise claims in situations where another NAFTA Party has acted in a manner inconsistent with any provision contained in Section A of Chapter 11, including the full scope of NAFTA Article 1105.

33. Canada confirmed its agreement to fully and completely carry out its NAFTA obligations in NAFTA Article 105 which obliges NAFTA Parties to "ensure that all necessary measures are taken in order to give effect to the provisions of the Agreement".

34. Counsel for Canada's overly narrow approach to the content of NAFTA Article 1105 demonstrates its misunderstanding of the ordinary content of "international law". For

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[36] Counter-Memorial (Second Phase) at para. 319.

[37] " ... for more than two hundred years international law has laid down a minimum international standard for the treatment of aliens (that is, nationals of other states). States are not obliged to admit aliens to their territory, but, if they permit aliens to come, they must treat them in a civilized manner. .... To put it in technical terms, failure to comply with the minimum international standard "engages the international responsibility" of the defendant state, and the national state of the injured alien may "exercise its right of diplomatic protection", that is, may make a claim, through diplomatic channels, against the other state, in order to obtain compensation or some other form of redress. Such claims are usually settled by negotiation; alternatively, if both parties agree, they may be dealt with by arbitration or judicial settlement." P. Malanczuk (ed.), *Akehurst's Modern Introduction to International Law* (7th ed.) at 256 -257. Investor's Supplemental Book of Authorities, Tab 9.

[38] Introduction to International Law: Character and Sources at 20. Investor's Supplemental Book of Authorities, Tab 1.

example, while Canada has argued that obligations regarding expropriation are not part of international law, the customary international law rules respecting expropriation have for many years conferred specific obligations upon individuals under international law.

35. The NAFTA itself is an example of an international agreement that creates a process whereby citizens from one NAFTA Party are entitled to seek redress in certain circumstances from the government of another Party under international law. In addition to the existence of private rights conveyed by international agreement through bilateral investment treaties completed by each of the NAFTA Parties[39], the WTO Agreement on Trade-Related Intellectual Property (TRIPS Agreement) displays yet another example of an international treaty that creates private rights for their citizens[40]. Other examples can be seen from international human rights agreements entered into by states.

36. Lord McNair in his treatise, the *Law of Treaties* devotes an entire chapter to the principle of *Pacta Sunt Servanda* and the General Presumption against Unilateral Termination. Lord McNair writes:

> In every uncodified legal system there are certain elementary and universally agreed principles for which it is almost impossible to find specific authority. In the Common Law of England and the United States of America, where can you find specific authority for the principle that a man must perform his contracts? Yet almost every decision on a contract presupposes the existence of that principle. The same is true in international law[41].

37. In its Merits Award, the ICSID Tribunal in *AMCO Asia* v. *Indonesia* carefully reviewed how "the principle *pacta sunt servanda* is a principle of international law."[42] This Tribunal concluded that *pacta sunt servanda* was a substantive principle of international law upon which the investor in this claim could rely. This same principle has been relied

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[39] According to the ICSID, up to 1996 the NAFTA Parties were all parties to BITS. The United States was a party to 37 BIT agreements, Canada was a party to 17 and Mexico was a party to two. Since that time, this list has grown. Each of these agreements create international obligations pertaining to the investors of one party operating in the territory of another particular state.

[40] The private rights created by the TRIPs Agreement is explained by the WTO Panel in its Section 301 Decision.

[41] McNair, *The Law of Treaties* at 493.

[42] *AMCO Asia v. Indonesia*, 1 ICSID Reports 377 at 490. Canada's Book of Authorities, Vol. II, Tab II.

upon by other international tribunals dealing with disputes between a foreign investor and a government[43]. For example, the Tribunal in the *Sapphire* award stated:

> It is a fundamental principle of law, which is constantly being proclaimed by international Courts, that contractual undertakings must be respected. The rule "*pacta sunt servanda*' is the basis of every contractual relationship. This Tribunal cannot but reaffirm that is its turn by stating that the maxim *pacta sunt servanda* should be viewed as a fundamental principle of international law [44].

This view has been supported by other tribunals as well [45].

38. The *AMCO Asia* Tribunal went on to note that, in addition to the applicability of the *pacta sunt servanda* rule, Indonesia was also required to observe the international law rule of "respect of acquired rights" which was a derivative of the principle of good faith. Under this rule, states must treat investments in their territories with a level of legal security that permits investors:

> to realize the investment, to operate it with a reasonable expectation to make profit and to have the benefit of the incentives provided by law.[46]

These decisions of international tribunals confirm the submission made by the Investor in this Supplemental Memorial (Second Phase) and the Memorial (Second Phase) that good faith (including the rule of *pacta sunt servanda*) is an integral part of international law as expressed in NAFTA Article 1105.

39. *Pacta sunt servanda* is the very type of longstanding international law principle that informs the content of NAFTA Article 1105 as referred to in its Statement on Implementation[47]. Accordingly, Canada is simply incorrect when it suggests that the longstanding principle of *pacta sunt servanda* cannot be included in international law treatment protected by NAFTA Article 1105. It clearly forms an integral part of international law.

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[43] See for example the award in *Texaco Overseas Petroleum (TOPCO) and California Asiatic Oil Company* v. *Libya*. 53 ILR 422 at 164. Investor's Supplemental Book of Authorities, Tab 12.

[44] *Sapphire Award* (1963) 35 ILR 136 at 181. Investor's Supplemental Book of Authorities, Tab 11.

[45] This quotation was cited with approval in the Tribunal award in *TOPCO* v. *Libya* at para. 51.

[46] *AMCO Asia v. Indonesia* at 493.

[47] See para. 220 of the Memorial (Second Phase) which quotes from this document.

VI. TRANSPARENCY

40. The principle of transparency is a part of international law recognized by NAFTA Article 1105. While Canada suggests that transparency is not an interpretative principle of the NAFTA[48], this observation is inaccurate. NAFTA Article 102 makes clear that the international law principle of transparency is a part of the NAFTA. This article states:

> 1) The objectives of this Agreement, as elaborated more specifically through its principles and rules, including national treatment, most-favoured-nation treatment and **transparency** are: .....
>
> 2) The Parties shall interpret and apply the provisions of this Agreement in the light of its objectives set out in paragraph 1 and in accordance with applicable rules of international law.
> (Emphasis added)

41. Furthermore, the Investor has already pointed out the integral nature of transparency in international law in its Memorial (Second Phase). An earlier NAFTA Investor-State Tribunal has come to the conclusion that NAFTA objectives "specifically include transparency and the substantial increase in investment opportunities in the territories of the Parties"[49].

42. The NAFTA Investor-State Tribunal in the *Metalclad* claim (comprised of a former attorney-general of the United States and chaired by a well-known international law authority) found that NAFTA Article 1105 includes the requirement that a government have a transparent administrative mechanism available whereby an investor can have its applications for government licenses reviewed and processed.[50] The NAFTA Tribunal has recognized the fundamental importance of transparency as an objective of the NAFTA. The Tribunal stated:

> Prominent in the statement of principles and rules that introduces the Agreement is the reference to "transparency" (NAFTA Article 102(1)). The Tribunal understands this to include the idea that all relevant legal requirements for the purpose of initiating, completing and successfully operating investments made, or intended to be made, under the Agreement should be capable of being readily known to all affected investors of another Party. There should be no room for doubt or uncertainty on such matters. Once the authorities of the central government of any Party (whose international responsibility in such matters has been identified in the preceding section) become aware of any scope for misunderstanding or confusion in this connection, it is their duty to ensure that the correct position is promptly determined and clearly stated so that investors can proceed

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[48] Counter-Memorial (Second Phase) at para. 329.

[49] *Re: Metalclad and Mexico* at para. 70. Canada's Book of Authorities, Vol. I, Tab 10.

[50] *Re: Metalclad and Mexico* at para. 88. Canada's Book of Authorities, Vol. I, Tab 10.

> with all appropriate expedition in the confident belief that they are acting in accordance with all relevant laws.[51]

This Tribunal went on to state that the principles which underscore the concept of legal security are contained within a Party's obligations under NAFTA Article 1105. The Tribunal stated:

> Mexico failed to ensure a transparent and predictable framework for Metalclad's business planning and investment. The totality of these circumstances demonstrates a lack of orderly process and timely disposition in relation to an investor of a Party acting in the expectation that it would be treated fairly and justly in accordance with the NAFTA[52].

Accordingly, Canada is not correct when it suggests that the principle of transparency is not an interpretative principle of the NAFTA nor a constituent element of international law covered by NAFTA Article 1105.

43. Canada suggests in its Counter-Memorial (Second Phase) that it has met its obligation of transparency by publishing the *Softwood Lumber Agreement*, the *Export and Import Permits Act*, the regulations made thereunder and the Notices to Exporters[53]. The Investor admits the fact that Canada has published these instruments, but the Investor contends that publication alone does not fully satisfy Canada's obligation of transparency under international law.

44. There is a substantive element to the obligation of transparency.[54] NAFTA Chapter 11 is an example of the development of the principle of transparency borrowing directly from GATT Article X, which was developed in the immediate post-war period. NAFTA Articles 1804 and 1805 contain these same substantive obligations relating to Administrative Proceedings, Review and Appeal, which go further than the basic requirements of Article 1802 (Publication). The language contained under Article 1805 specifically refers to both "tribunals" and "procedures". Thus, Canada's blanket assertion that the Investor could have availed itself of the Federal Court review process does not satisfy the obligations under Article 1805, which includes not only tribunals such as the

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[51] *Metalclad and Mexico* at para.76.

[52] *Re: Metalclad and Mexico* at para. 99. This quotation is also set out in paragraph 150 of the Memorial (Second Phase).

[53] Counter-Memorial (Second Phase) at paras. 334 - 335. Canada's Book of Authorities, Vol. I, Tab 10.

[54] The Investor at paras. 148-165 of its Memorial (Second Phase) has outlined the nature of these substantive obligations under both NAFTA Chapter 18 and GATT Article X.

Federal Court of Canada, but also "procedures" that must contain an adequate review or appeal process within the application of a measure itself.

45. The Investor has re-produced the text of GATT Article X.[55] Specifically, GATT Article X:3 contains, much like the provisions of NAFTA Articles 1804 and 1805, substantive obligations with regard to due process and transparency of government measures. The interpretation of GATT Article X in the WTO *Shrimp/Turtle* case is particularly useful in examining whether or not the Export Control Regime meets the substantive obligations of due process and transparency.

46. Canada questions the applicability of the WTO Appellate Body's consideration of what constitutes an arbitrary application of a measure in the *Shrimp/Turtle* case to Canada's application of the Export Control Regime.[56] The WTO Appellate Body found that where a measure does not contain the necessary transparency and due process safeguards that protect the commercial interests of foreigners, it can be considered to be applied in an arbitrary (and otherwise unjustifiable) manner. The Appellate Body's general analysis of the concept of arbitrary treatment is directly relevant to this Tribunal's consideration of whether the Export Control Regime was administered in accordance with the "fair and equitable" treatment standard of NAFTA Article 1105.

47. The *New Shorter Oxford English Dictionary* defines the term "unfair" as : "Not equitable, unjust, not according to the rules, partial." It defines "arbitrary" as follows:

> 1. Dependent on will or pleasure; *Law* (now *Hist.*) Dependent on the decision of a legally recognised authority; discretionary. 2. Based on mere opinion or preference as opp. To the real nature of things; capricious, unpredictable, inconsistent. 3. Unrestrained in the exercise of will or authority...[57]

The concepts of arbitrariness and fairness are related. Accordingly, one might consider the decisions of international jurists about what constitutes "arbitrary" treatment in determining what sort of treatment fails to meet the "fair and equitable treatment" standard in international law. Accordingly, when the WTO Appellate Body considers a measure to have been arbitrarily applied because it is not transparent or is missing internal due process safeguards (as opposed to external safeguards, such as the

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[55] At para. 156 of its Memorial (Second Phase).

[56] Paras. 343 to 344 of the Counter Memorial (Second Phase).

[57] *The New Shorter Oxford English Dictionary*, Thumb Index Edition (Oxford: Clarendon, 1993) at 3482 and 107, respectively. Investor's Supplemental Book of Authorities, Tab 8.

availability of judicial review), its analysis can be useful in determining whether a NAFTA Party has breached the "fair and equitable treatment" standard under NAFTA Article 1105 when its measure is similarly lacking in transparency or due process safeguards.

VII. CANADA IS NOT EXEMPT FROM INTERNATIONAL LAW RULES

48. Canada argues in its Counter-Memorial (Second Phase) that treatment in accordance with international law "should not be interpreted to require a higher requirement than is required under the domestic law of states with reasonably developed legal systems"[58]. The Investor takes great issue with this assertion. As a Party to the NAFTA, Canada is obliged to act in accordance with international law.[59] Canada apparently believes that since it has a "reasonably developed legal system" that it is completely insulated from its obligation to provide treatment in accordance with international law to investments from investors from other NAFTA Parties. This statement demonstrates Canada's complete misunderstanding of its obligations under international law.

49. Notwithstanding the fact that Canada believes that its legal system is "reasonably developed", that same system can suffer lapses that result in an investment not receiving that treatment required by international law. Thus, if an investment is not treated fairly or transparently, this failure cannot be remedied by the fact that Canada claims that its legal system is "reasonably developed". This Tribunal is required to look to the specific circumstances of the Investor's allegations concerning the specific measures at issue in its Claim to see whether it has received treatment in accordance with international law. Canada's "reasonably developed" legal system cannot stand as a barrier to this Tribunal's ability to conduct such a review.

50. Canada has argued that the Investor is incapable of bringing a complaint about the absence of an independent and fair review process from the Minister's award of quota as the Investor did not avail itself of recourse to Canadian courts prior to the bringing of this NAFTA Claim. With respect, the Tribunal must reject this argument out of hand as it demonstrates Canada's complete failure to appreciate the special nature of an international process created under Section B of NAFTA Chapter 11. The NAFTA does not require that an Investor exhaust local remedies before the filing of a claim. NAFTA Articles 1116 and 1117 both clearly permit a claimant to file a claim on the basis of there

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[58] Counter-Memorial (Second Phase) at para. 240.

[59] This Tribunal acknowledged this basic obligation in its *Decision on Cabinet Confidence*, September 6, 2000.

being a breach of certain NAFTA obligations by a NAFTA Party within certain time limitations. These provisions alter the long-standing international law rule that sometimes requires claimants to exhaust local remedies before invoking the international legal process[60]. This NAFTA variation from international law would explain why the temporal restrictions in NAFTA Chapter 11 are so relatively short.

51. There is no requirement in the NAFTA that an Investor exhaust local remedies before it seeks to have a claim heard under the NAFTA process. The only requirement for bringing a claim under NAFTA Chapter 11 is that there is a breach of certain NAFTA obligations by a NAFTA government, which has caused harm to an Investor from another NAFTA Party within certain specified time limits. Indeed, the NAFTA Chapter 11 Tribunal in *Metalclad* expressly confirms that there is no requirement to exhaust local remedies before bringing a NAFTA Chapter 11 claim[61].

52. At any rate, the judicial review process available in the Federal Court of Canada is an inadequate mechanism for foreign investors seeking due process in the adjudication of their NAFTA rights. The primary reasons why the Federal Court review does not meet Canada's international law obligations under NAFTA Article 1105 are:

a) Canadian courts are neither permitted, nor equipped, to evaluate whether the treatment standards explicitly set out in NAFTA Article 1105 have been accorded to investments;

b) Investors are unable to receive compensation upon a successful judicial review application from the Federal Court of Canada; and

c) Investors are unable to obtain evidence from the government about how allocations are made due to Canada's unrestricted use of certificates issued under section 39 of the *Canada Evidence Act*, which prohibits a domestic court from compelling the production of certain types of evidence.

Accordingly, Canada's own domestic judicial review test permits Canadian officials to engage in conduct that falls below the standards established under international law, pursuant to NAFTA Article 1105.

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[60] Of course, local remedies need not be exhausted when it is clear that the local court will not provide redress for the injured individual. See the *Brown* claim (1923) VI RIAA 120. Investor's Supplemental Book of Authorities, Tab 18.

[61] *Metalclad* at para. 97, footnote 4.

53. This Tribunal has already been exposed to Canada's reliance on Section 39 Certificates to refuse evidence from being revealed to this Tribunal. Despite the fact that Section 39 of the *Canada Evidence Act* could not apply to a NAFTA proceeding, Canada has relied upon it to withhold evidence from the Tribunal. Canada has used this same authority (then known as a Section 37 Certificate) to suppress evidence from the Federal Court in its review of the Export Control Regime in the *Donohue* case.[62]

54. This Tribunal has already provided general observations on how the use of Section 39 Certificates by Canada results in placing disputing parties on an uneven basis in litigation. The Investor submits that this uneven treatment fundamentally deprives a claimant from having a determination before a Canadian tribunal that is consistent with Canada's international law obligations.

55. Counsel for Canada has argued that the effect of the Tribunal supporting the Investor's argument would be to create a regime of special rights for foreigners in Canada. The Investor does not agree with Canada's submissions. The idea underscoring international investment agreements such as the NAFTA is not to provide special treatment for foreign investors but to have NAFTA Parties raise their domestic standards for all investors operating in their territory. The goal is as Professor Melanczuk states:

> If the minimum international standard appears to give aliens a privileged position, the answer is for states to treat their own nationals better, not for them to treat aliens worse; indeed, the whole human rights movement may be seen as an attempt to extend the minimum international standard from aliens to nationals, even though the detailed rules in declarations and conventions on human rights sometimes differ considerably from those in the traditional minimum international standard[63].

56. In conclusion, the Investor submits that NAFTA Article 1105 permits investors to seek compensation from NAFTA Parties, such as Canada, for breaches of various obligations under international law. These standards of treatment are found in international law, not in some singular, minimalist standard that has been frozen for decades. International law has developed significantly over the past seven decades and the text of NAFTA Article 1105 has incorporated these developments by reference to "treatment in accordance with

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[62] See Schedule 4. Federal Court of Canada Docket Summary. This summary illustrates that Canada has suppressed documents in domestic cases involving quota allocations under the Export Control Regime. In the *Donohue* case, Canada also used the S.39 Certificate under the *Canada Evidence Act* to avoid document production relevant to the dispute with a softwood lumber producer.

[63] P. Malanczuk (ed.), *Akehurst's Modern Introduction to International Law* (7th ed.) at 261. Canada's Book of Authorities, Vol. II, Tab 12.

international law." The principles of transparency, non-discrimination and *pacta sunt servanda* are fundamental foundations of modern international economic law. The NAFTA itself is a direct result of this development, in particular in its embodiment of the principle of legal security. These are the standards that Canada, like all NAFTA Parties, agreed to provide under NAFTA Article 1105.

VIII. THE LAW APPLIED TO THE FACTS

57. Canada's actions which have been inconsistent with its NAFTA Article 1105 obligation to provide treatment in accordance with international law have been addressed by the Investor in its Memorial (Second Phase). In summary, Canada has not met its obligation to provide this treatment to the investments of this American investor through the following actions:

a. Canada has failed to provide due process to the Investment by not providing it with a fair and transparent process to review its-own quota allocation. This failure is compounded by Canada's refusal to provide adequate information to the Investor about the wholesaler component of its-own softwood lumber quota.

b. Canada knew that there were serious errors in the structuring of the softwood lumber quota, especially with respect to the wholesaler component. However, rather than take measures to correct these obvious errors, Canada decided out of administrative expediency to take steps to proceed with its allocation procedure despite the negative impact it could have on certain investments.

c. Canada failed to provide treatment that was fair and equitable to the Investment after the Investor commenced the filing of its NAFTA claim. Canada's behaviour in undertaking and administering the Verification Audit upon Pope & Talbot is an example of behaviour that did not meet Canada's international law obligation of treatment.

d. Canada failed to provide treatment that was fair and equitable to the Investment in the specific way in which it implemented its 1999 amendments to the *Softwood Lumber Agreement* with respect to the Super Fee Base. This provides an example of treatment that fails to meet Canada's international law obligation to the Investment.

e. Canada failed to meet its obligation of fair and equitable treatment in international law in its cumulative allocation of quota to the Investment that is detailed in Section Three in this Supplemental Memorial.

Canada has failed to meet its obligations to provide transparency in its treatment of the Investment. As a result, this failure to provide transparency has left the investor unable to have effective remedies in order to protect its legitimate business interests. In response to Canada's Counter-Memorial (Second Phase), the Investor makes the following submissions.

A. Lack of Administrative Fairness

1. Canada's Arbitrary Allocation of Quota - Consultation or Discretion?

58. Canada has provided two main explanations in their Counter-Memorials to explain its initial and on-going allocations of the softwood lumber quota. The first explanation relates to the repeated assertions that Canada relied on consultations with stakeholders from the provinces and industry to arrive at a consensus on which Canada could proceed. By reviewing Mr. Valle's first affidavit, one is left to conclude that the basic elements of the quota allocation were agreed upon by the provinces and industry by the end of August 1996. Mr. Valle states:

> While there remained some divergence of views on the elements of the allocation method, there was a general consensus as to **the basic requirements of the allocation system** at the end of this process. These included a recognition of the need to provide for new entrants and a growth mechanism, and an obvious need to finalize the allocation system so that it could be implemented with the time constraints of the SLA.[64] [emphasis added]

59. In that affidavit, he states that the elements of the allocation were included in the September 10, 1996 announcement of the softwood lumber plan.[65] However, contrary to Mr. Valle's statements, there was no evidence as of the end of September 1996 that any kind of consensus existed on the fundamental and basic issue of whether discretionary allocations would be first deducted from the national established base ("EB") quota allocation of 14.7 billion board feet ("BBF") before the provincial corporate shares. There was simply no "consensus"on this key issue.

60. Canada provided a second, inconsistent explanation for how it conducted its quota allocations. The second explanation dismisses the first explanation by saying that, in the end result, any decisions concerning quota allocation are based on the sole discretion of the Minister rather than upon the achievement of industry consensus. This pattern of alternately reverting to alleged industry consensus for justification of government actions

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[64] Valle Affidavit #1 at para. 88.

[65] Valle Affidavit #1 at para. 89.

versus claiming that the Minister was properly the final umpire and protector of procedural fairness can be found throughout the Counter-Memorial.[66] For example, Mr. Valle states:

> Where disagreements arise, it falls to the Minister to balance conflicting interests and make a decision. By definition, that decision cannot please everyone.[67]

61. Mr. Valle has suggested that Canada's reliance on these consultations did not constitute any real reliance. This is another example where Canada is attempting to proverbially "have its cake and eat it too". Mr. Valle states in his second affidavit in support of the dilution of Canada's reliance on any "consensus":

> The consensus to which I referred in my previous affidavit refers to matters of broad principle and not matters of detail.[68]

62. In Mr. Valle's lengthy description in his first affidavit of how the consensus arose, it appeared that many details were indeed included. Mr. Valle relies on that consensus in his first affidavit to justify the basic elements of the allocation system, but suggests in his second affidavit that there really was no consensus on the key element of whether discretionary allocations would be deducted first before the provincial corporate allocations were made.

2. *The Lack of an Internal Appeal Mechanism - Canada's Allocation Philosophy*

63. Canada's viewpoint on the allocation of softwood lumber quota, as reflected particularly in the affidavits of Mr. Valle and Mr. George, is that it is sufficient for it to provide "informal internal review mechanisms".[69] This philosophy of unchecked discretion is directly relevant to why Canada structured the Export Control Regime without any kind of internal appeal mechanism, despite internal advice to the contrary. The philosophy is stated succinctly by Mr. Valle when discussing how the EICB intended to deal with the problem of faulty wholesaler data. Mr. Valle states that:

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[66] At para. 37 of Canada's Counter-Memorial, Canada states that; "The Advisory Committee recommendations are not determinative, but are factors considered by the Minister in the decision-making process." Valle Affidavit #2 at paras. 15-19. At para. 166, Mr. Valle further confirms that "The Minister exercises ultimate decision-making responsibility subject to judicial review."

[67] Valle Affidavit #2 at para. 19.

[68] Valle Affidavit #2 at para. 47.

[69] Valle Affidavit #2 at para.186.

> Bureau officials and I felt the bureau could manage any errors that might arise through individual allocation adjustments.[70]

64. Accordingly, Canada appears to reject the need for due process, including accountable internal appeal mechanisms (based on transparent policies and procedures) in favour of an ad hoc, secretive approach that ultimately permits arbitrariness and discrimination. Canada's Counter-Memorial (Second Phase) and supporting affidavits reinforce the arguments made in the Investor's Memorial (Second Phase) that Canada has not provided the Investor with any transparent or systemic solutions to what were clearly system wide problems. Rather, Canada's own evidence demonstrates that Canada favours an approach that relied on lobbying by softwood lumber manufacturers for the exercise of Ministerial and bureaucratic discretion.

65. Canada's approach is that of reacting to solve problems on a case by case basis, relying on a self described "discretion" (which is really nothing more than arbitrariness) and secrecy rather than through transparent, predictable and consistent policies and procedures. Canada states:

> Moreover, the Investor tenders no evidence that only investments with the best lobbyists had "access" to the Minister and had their concerns addressed. Canada flatly denies this allegation[71].

66. The Investor responds in two ways. First, Canada does not characterize the Investor's Claim accurately. The Investor has not said that "only" investors who lobbied the Minister had their concerns addressed. The Investor concedes that those who lobbied EICB officials would also have had their concerns addressed. The point made by the Investor is that a pro-active requirement of political style lobbying, whether to the Minister or department officials, whether through committee or direct access to the officials, was a tacit requirement of Canada's allocation system, rather than the provision of an independent and internal appeal mechanism.

67. Because Canada's administration relies so completely on the ability and inclination of the softwood lumber manufacturers to complain to the EICB or the Minister, the Investor submits that a distinct advantage would be given to those mainly Canadian softwood lumber manufacturers who understood that Canada operated under this "squeaky wheel" philosophy.

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[70] Valle Affidavit #2 at para. 71.

[71] At paragraph 44 of its Counter-Memorial (Second Phase).

68. Secondly, the discretionary allocations are examples of the highly political and fundamentally arbitrary nature of Canada's administration of the Export Control Regime and quota allocations. These examples support the proposition that those with the best access to the Minister, his officials and EICB officials had the best chance of having their concerns addressed.

69. Canada admits in its submission that those investments in Canada with the best understanding of the industry and access to officials at the EICB would receive the best treatment under the Export Control Regime. As Mr. Valle states in his affidavit about of the lack of an administrative appeal mechanism:

> The EIPA includes no provision for an appeal or judicial review of a quota allocation decision of the Minister. However, experienced officials and I knew of the various avenues available to persons dissatisfied with the method of allocating quota or an allocation. Industry was also aware of these avenues.[72]

70. The Investor and the Investment were not aware of this informal ad hoc system and the manner in which Canada allocated additional quota to other softwood lumber manufacturers. Pope & Talbot was merely aware of what it was advised through government notices and through the industry associations of which it was a member. If there were special avenues, such as Mr. Valle suggests, it was not aware of them and did not benefit from access to them. As a foreign investment, it is not unreasonable to conclude that Pope & Talbot did not know that if it complained loud and long enough and sought the proper "avenues", it could have had its concerns more fully addressed and satisfied. Mr. Valle summarizes Canada's viewpoint on the issue of raising concerns:

> The companies that received the government's attention with respect to their quota allocation were those that sought it.[73]

71. In summary, the philosophy of Canadian officials was that the onus was on each softwood lumber manufacturer to complain and seek redress through this informal, undisclosed process. This philosophy is simply inconsistent with Canada's international law obligations.

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[72] Valle Affidavit #2 at para. 181.

[73] Valle Affidavit #2 at para. 212.

3. *Canada's Over-Extension of Confidentiality*

72. A further aspect and example of the arbitrary manner in which Canada administered the Export Control Regime relates to its approach to confidentiality of business information. In its Counter-Memorial (Second Phase),[74] Canada states that the reason confidentiality was applied to the Export Quota Regime was that the industry insisted on it. The Investor agrees with the proposition that there are legitimate reasons to protect commercial confidential information, such as the actual amount of quota allocation or the sales and production figures provided in the 1996 Questionnaire. Canada has confused this proposition by using it as a blatant justification for the lack of transparency or due process in its actual administration of the Export Control Regime.

73. The fact that softwood lumber manufacturers sought confidentiality for their commercial business information does not necessarily entail that such companies accepted non-transparency and reduced due process in the whole system as a result. For example, with respect to the wholesaler allocation, primary manufacturers were routinely refused access to the data on which their-own allocation was based on the grounds of confidentiality. As noted in the Investor's Memorial (Second Phase), the real reason, as confirmed by the Minister's Executive Assistant, was that providing this information would "overload the system".[75] The Investor was initially refused this same data in this NAFTA process even though there is a process to deal with third-party confidential information through arbitration. Such third-party confidential processes are not unusual in Canadian administrative law, and yet Canada has consistently refused access to this data.

74. A further example relates to Canada's failure to advise softwood lumber manufacturers, such as Pope & Talbot, of the mere fact that special allocations were made in 1997, when those allocations dramatically impacted upon their investments. The special BC re-allocation in 1997 is a particular example where special deals were made. No details of those allocations were made public concerning the grounds on which they were made. And, more importantly, the policies and processes by which other softwood lumber manufacturers could access such a remedy were never made public. In the Investor's Memorial (Second Phase), it is noted that only oblique references were made to the special British Columbia re-allocation by Canada to the Investment after the fact. This

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[74] At paras. 176-181.

[75] Memorial (Second Phase) at para. 17.

conduct did not meet the requirements of basic transparency and due process under international law.[76]

B. Wholesaler Problem

75. The Investor submits that Canada's conduct with respect to the faulty wholesaler data and co-efficient, and the 1997 British Columbia re-allocation, were breaches of Canada's NAFTA obligations pursuant to NAFTA Articles 1102 and 1105[77]. Canada admits that there was "... no precise data about the volumes of lumber purchased from individual mills and exported by wholesalers..."[78] and that "there was not always a good match between data provided by the primaries and remanufacturers and the data provided by wholesalers."[79] Mr. Valle confirms that it was very difficult in 1996 to properly trace wholesaler sales.[80]

76. Counsel for Canada further states that the EICB and industry groups concluded that "the data derived from the June Questionnaire could be used and that in any event, new data would not yield more accurate or significantly different results."[81] Canada relies on the second affidavit of Mr. Valle who further states that an analysis of the wholesaler data problem was carried out by the EICB in September and October of 1996, but Canada provides no evidence of that analysis.[82] This is in contrast to the fact that Valle indicates that an audit and analysis of remanufacturers and primary producers was undertaken at that time,[83] but no similar audit was conducted with respect to wholesalers or provided to the Investor or this Tribunal.

77. With respect to this unproduced wholesaler "analysis", Mr. Valle further states the unsubstantiated conclusion that "... analysis within the Bureau and discussions between

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[76] Memorial (Second Phase) at paras. 68-75, particularly at para. 72.

[77] Memorial (Second Phase) at paras. 207-219, and 282-287.

[78] Counter-Memorial (Second Phase) at para. 24.

[79] Counter-Memorial (Second Phase) at para. 402.

[80] Valle Affidavit #2 at paras. 61-64, 131.

[81] Counter-Memorial (Second Phase) at para. 27.

[82] Valle Affidavit #2 at para. 71.

[83] Valle Affidavit #2 at para. 78.

the Bureau officials and industry groups suggested that **any margin of error was small.**"[84] (Emphasis added) Again, later in his second affidavit, Valle states with respect to the accuracy of the wholesaler data on which allocations to primaries were based that: "Our conclusion, shared by industry representatives, was that the data received from wholesalers was sufficient for the purposes of the allocation."[85] Although Valle states that industry supported the use of the faulty data, The documents contradict this statement – British Columbia industry representatives saw "a major inequity" in Canada's proposal.[86]

78. In addition, a simple comparison of the list of wholesalers from Pope & Talbot's Questionnaire and the list of wholesalers provided by Canada used to determine Pope & Talbot's wholesaler allocation provides a demonstration of the faulty nature of the wholesaler data.[87] As Mr. Rosen states:

> ...the information provided by Canada to represent the wholesalers' purchases from Pope & Talbot is materially different than the data of sales to wholesalers produced by the Investment.[88]

The margin of error in the data on which Pope & Talbot's wholesaler allocation was based was materially different and certainly not a sufficient basis for the purposes of determining Pope & Talbot's wholesaler allocation.

79. It should be noted that, although Canada states that it relied on industry advice in 1996 as to whether to rely on the faulty wholesaler data, it did not seek the advice of nor provide information to the Investment so that it could assess the adequacy of the information on which the wholesaler portion of its allocation was based to determine the nature of the "match" between data provided. It appears that no primary manufacturers had this opportunity.[89] It was not until the submission of this NAFTA claim that the Investor and its Investment had the opportunity to understand the nature of the wholesaler allocation.

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[84] Counter-Memorial (Second Phase) at para. 28; Valle Affidavit #2 at para.71.

[85] Valle Affidavit #2 at para. 80.

[86] Memorial (Second Phase) at para. 209 - 212 with respect to the September 26, 1996 Memo at Schedule 5 of the Memorial (Second Phase).

[87] Memorial (Second Phase) at para. 74; and Schedule 33 of the Memorial (Second Phase), Witness Statement of Howard Rosen, September 5, 2000.

[88] Statement of Howard Rosen, September 5, 2000 at para. 11.

[89] Valle Affidavit #2 at para. 211.

And, as Howard Rosen notes in his Statement, from the information provided by Canada to the Investor in response to its information requests, it is still impossible for the Investor to independently determine if the wholesaler allocation was even mathematically correct, because of a lack of disclosure by Canada.[90]

80. Further, Canada's justification for the use of faulty data was made in the face of a number of options that would have assured that proper data was obtained.[91] Canada rejected the proposal of British Columbia industry representatives to conduct a re-audit of the data by extending the first come first served system over the first year of the Export Control Regime on the grounds of being too difficult from an administrative point of view.[92] Canada also rejected the option of relying on the data provided by primary producers in their 1996 Questionnaires.[93] As Mr. Rosen points out in his witness statement, if Canada had used the wholesaler sales figures from the Investment's 1996 Questionnaire, it appears that:

> ... the Investment would have received more quota than using the government's formula that was based on incomplete information and a gross-up to account for apparently inaccurate reporting by wholesalers.[94]

81. The paramount concern for Canada was not that the wholesaler allocation be based on reliable data, but that political and operational concerns be met and that any problems that arose from the data could be managed on a case by case basis for solely those who complained.

82. Canada cannot support its unsubstantiated contentions about its analysis of the faulty wholesaler data. It appears that there was no real analysis nor consultation – in particular in relation to Pope & Talbot. There is evidence that there was a large margin of error in

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[90] Statement of Howard Rosen, September 5, 2000 at para. 15.

[91] Valle Affidavit #2 at paras. 72-77.

[92] This is similar to Canada's rejection on the grounds of confidentiality that primary producers be allowed to view their audited wholesaler questionnaires on which that allocation was based, when it was clear that officials merely did not wish to "overload the system": see Memorial (Second Phase) at para. 17.

[93] Valle Affidavit #2 at para. 81.

[94] Statement of Howard Rosen, September 5, 2000 at para. 16.

the Investment's wholesaler data.[95] Accordingly, in light of the *prima facie* evidence available to support this finding and Canada's decision to not produce relevant evidence to refute these conclusions, the Investor requests that the Tribunal relying upon its authority under Article 28(3) of the UNCITRAL Rules draw the inference that Canada's margin of error for all wholesaler data was similarly large.

83. The Investor submits that Canada made its decision concerning the use of the faulty data in an arbitrary and unfair fashion contributing to the violation of the Canada's obligation to provide treatment in accordance with international law.

84. As expected by EICB officials, the wholesaler allocation issue led to problems and complaints, – an "uproar" – [96], from a number of primary manufacturers, particularly in British Columbia. Canada approached the problem in the same manner that it approached all discretionary allocations - it only reacted to those softwood lumber companies that complained. It is interesting to highlight what Canada did not do with respect to other softwood lumber companies that may or may not have had problems with their wholesaler allocation, but were nevertheless required to give up 3% of their quota.

85. For example: Canada did not advise prior to making the BC re-allocation that it was planning to do so and that there was a remedy available; it did not advise companies, such as Pope & Talbot, in advance of the policies and procedures under which a company could seek the wholesaler re-allocation; by not being transparent about the process, Pope & Talbot could not comment nor investigate the remedy for itself; Canada did not advise companies, such as Pope & Talbot, that such a re-allocation of quota in British Columbia would be deducted from their quota allocation; Pope & Talbot was provided with no means to protect its rights.

86. It is important to highlight a key distinction – Pope & Talbot is not the BC Advisory Committee or the "industry". Consultation is always advisable when it affects a company such as Pope & Talbot directly. An "industry" consultation, on which Canada repeatedly justifies its conduct, is simply not sufficient. In particular, when each quota holder receives a reduction as significant as 3.1% with four years left in the Export Control Regime. Canada's obligations were directly related to individual quota holders, such as Pope & Talbot.

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[95] See in particular para. 82 of the Memorial (Second Phase) for a review of the comparison of data provided by Pope & Talbot in comparison with data provided by wholesalers.

[96] As stated in the Memorandum from DMT to EPD, September 26, 1996, Schedule 5 of the Memorial (Second Phase) and at para. 210 of the Memorial (Second Phase).

87. Canada's reiterates its position that any problem addressed by the BC re-allocation related to the BC provincial formula, and not to the faulty wholesaler data and the subsequentiy faulty wholesaler co-efficient.[97] Canada relies on the fact that the BC Softwood Lumber Advisory Committee recommended the provincial formula[98] and, accordingly, any problem with the allocation was in effect a self-inflicted British Columbia problem.

88. The BC Softwood Lumber Advisory Committee made it clear in their letter to the Investment dated June 24, 1997 that the BC Re-allocation was recommended because of "data problems" with wholesaler data.[99] Counsel for Canada has stated again that it relied on the BC Softwood Lumber Advisory Committee to make the BC re-allocation:

> Canada resolved issues raised by the BC Softwood Lumber Advisory Committee and made adjustments to the quota of companies suggested by the BC Softwood Lumber Advisory Committee."[100]

In response to counsel for Canada, the Investor notes that the BC Softwood Lumber Advisory Committee is an entity established by Canada. Furthermore, Canada has already made it abundantly clear that the "Advisory Committee recommendations are not determinative, but are factors considered by the Minister in the decision-making process."[101] Canada seeks to rely on the recommendations of the Committee in terms of which companies should be granted special allocations, but also makes it clear that it did not rely on the Committee's reasons for making the allocation – to ameliorate the effect of faulty wholesaler data.[102]

89. In particular, Mr. Valle uses the re-allocation provided to [redacted] as an example of problems arising from the BC provincial formula and not the faulty wholesaler data.[103] Mr. Valle's statement does not make sense in the context of the "Review of Quota

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[97] Counter-Memorial (Second Phase) at paras. 79, 130, 408; Valle Affidavit #2 at paras. 170-180.

[98] Valle Affidavit #2 at para. 174.

[99] See Schedule 24 of Memorial (Second Phase), or Tab 98 Tribunal Request for Documents.

[100] Counter-Memorial (Second Phase) at para. 80.

[101] Counter-Memorial (Second Phase) at para. 37.

[102] Counter-Memorial (Second Phase) at para. 408.

[103] Valle Affidavit #2 at paras. 174-175.

Allocation" document provided with the BC Committee's recommendation letter dated April 17, 1997[104], which clearly shows that [redacted] had estimated a relatively large percentage, 17% in fact, of its overall shipments to the US were through wholesalers. This is a significantly larger share of US shipments through wholesalers than the average in British Columbia, which was approximately 5%.[105]

90. Without having access to [redacted] quota allocation numbers, it is difficult for this Tribunal to be able to verify Mr. Valle's assessment of [redacted] situation. The Investor submits that it is sufficient to suggest that both the BC provincial formula and the deficiencies of the wholesaler data/wholesaler co-efficient may have had an adverse effect on [redacted] quota allocation. The BC Softwood Lumber Advisory Committee clearly recognized the wholesaler problem with exports attributable to wholesalers in its recommendation.

91. In summary, the wholesaler allocation method and the 1997 British Columbia re-allocation damaged Pope & Talbot. In particular, Canada's conduct represents an egregious lack of administrative fairness relating to failures of transparency and an abuse of discretion under international law. Canada's actions constituted violations of its obligation to provide treatment in accordance with international law under NAFTA Article 1105 as well as also constituting a violation of Canada's obligation to provide national treatment to the Investor and its investment.

C. Verification Review

92. The verification review is a further example of Canada's operational philosophy that, in essence, it need not operate under the principles of due process or transparency, as submitted by the Investor in its Memorial (Second Phase),[106] because those principles do not apply to its conduct.

93. Inherent in and resulting from this general view is the notion that it is permissible for Canada to act in a manner which provides it with systemic advantage in relation to those who were under its regulatory control pursuant to the Export Control Regime. For

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[104] See Memorial (Second Phase), Schedule 21.

[105] Schedule 12. Working Agenda for Preparatory Meeting on Softwood Lumber, Summary Points of Issue for 1997/98 Allocations at 3, para. 5.

[106] Memorial (Second Phase) at paras. 220-238.

example, Counsel for Canada admits that it does not believe Pope & Talbot needed to know the case against it in the verification review process. Canada states:

> It was Canada's intention to clearly explain to the Investor the nature of the errors it might find but not to provide precise data in order to be able to assess the validity of a revised questionnaire, should one eventually be required of the Investment.[107]

Canada goes on to state:

> While Canada did not provide a list detailing the actual errors, it did provide the Investment with a clear description of the kinds of errors that had been made.[108]

94. Canada is attempting to justify withholding the detail of the verification review on the grounds that it wanted to use the six-month review as a reference point for a full review. This is not a satisfactory explanation when it is balanced against the stated need of the Investment to know the case against it.

1) As stated by the Investor prior to the verification review, there exist methods to conduct a full review that are statistically reliable, and Canada rejected those suggestions of the Investor. Accordingly, the Investor submits in response to Counsel for Canada[109] that using the six month review to assess a revised questionnaire was unnecessary.

2) By withholding the data on which the six-month review was conducted, Pope & Talbot was never able to identify the errors in the document on which the recommendation for a revised questionnaire was made. The facts arising from the Interim Measures Motion demonstrate that Pope & Talbot required that information to know the case against it. Otherwise, Canada would have been at a distinctly advantageous position over Pope & Talbot. It appears that Canada accepts this imbalance as the normal state of affairs in its relationship with the softwood lumber companies regulated by it under the Export Control Regime.

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[107] Counter-Memorial (Second Phase) at para. 141.

[108] Counter-Memorial (Second Phase) at para. 148.

[109] Also see George Affidavit #3 at para. 113.

95. Canada states that "the Investment refused this request to submit a revised questionnaire."[110] Mr. George also states in his third affidavit that "Pope & Talbot is the only company that has refused, during my tenure with the EPS, to cooperate with the EICB in the conduct of a softwood lumber verification review."[111] These statements are clearly not factually correct. A verification review did occur in July 1999. As Mr. George states in his third affidavit: "The Investment's allocation has not been adjusted as a consequence of the initial verification review."[112] Canada admits that it was prepared to adjust Pope & Talbot's quota based on the six-month review suggesting that Canada believed that the review was a sufficient basis on which to adjust a quota allocation.[113]

96. The fact are clear. A verification review took place where Canada had full access to certain books and records of the investment over a considerable period of time. After completing its report on the review, Canada decided not to proceed with a revision of the Investment's Questionnaire. Pope & Talbot at no time refused to revise its questionnaire and in the proper circumstances would have been prepared to do so.[114]

97. Canada insists that "At no time was there an "agreement" governing the verification review[115]. Moreover, Canada gave no undertakings to the Investor." The notes of Howard Rosen, made during the verification review in July 1999, presented as part of record at the Interim Measures Motion hearings in January 2000, clearly confirm that assertion and that the verification review was conducted on the basis of an agreement.[116] Indeed, Counsel for Canada actually admits a number of the elements of the agreement at paragraphs 138 and 411(f) of the Counter-Memorial (Second Phase), despite appearing to deny these facts again at paragraph 142.

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[110] Paragraph 411(h) of the Counter-Memorial (Second Phase).

[111] George Affidavit #3 at para. 83 and at para. 114.

[112] George Affidavit #3 at para. 122; Counter-Memorial (Second Phase) at para. 150.

[113] Counter-Memorial (Second Phase) at para. 411(h).

[114] Schedule 13. Letters from Counsel for Pope & Talbot to Douglas George, dated Oct. 25 and Nov. 5, 1999.

[115] Paragraph 142 of the Counter-Memorial (Second Phase).

[116] See Schedule 1. Mr. Howard notes, at 2, that Mr. McLean, counsel for Canada at the review, confirmed that the review was taking place based on the consent of the disputing parties.

98. In summary, the Investor agrees with Canada that "It is not unreasonable to expect a quota holder to cooperate with reasonable requests of the quota administrator."[117] The problem arises when the administrator makes unreasonable requests that are not based on the international standard of administrative fairness and transparency. Administrative fairness is particularly breached in the absence of lawful authority, of which Canada has never provided any evidence. The verification review process is merely another example of Canada's "usual practice" (as Canada readily admits at paragraph 413 of its Counter-Memorial (Second Phase)). Based on the example of Canada's conduct during this verification review, the Investor submits that this practice is clearly unacceptable under international law.

D. Super Fee Base Levy

99. The Investor submits that the SFB levy measure is a violation of Canada's NAFTA obligations pursuant to NAFTA Articles 1102 and 1105.[118] The essence of Canada's conduct is that it unfairly promulgated a measure that had a disproportionate and discriminatory impact on Pope & Talbot.

100. Counsel for Canada states in its Counter-Memorial (Second Phase) that it was aware that the SFB measure would affect only "1% of British Columbia's total lumber exports to the United States."[119] Counsel for Canada also makes clear that the Investment was one of 132 British Columbia companies that would be affected by the repricing of a portion of lower fee base ("LFB") and UFB quota. It is important to note that Canada was aware that Pope & Talbot was one of the largest exporters of softwood lumber in British Columbia at the UFB level in the year prior to the promulgation of the SFB Levy measure and would be most directly affected.

101. Mr. George confirms in his third affidavit that Pope & Talbot was included in the August 18 Memorandum "...because such litigation may be of some relevance to the decision that the Minister is being asked to make."[120] The relevance for the Minister is that it apprised him that the SFB measure may be actionable under the NAFTA case. Canada had clearly considered the effect of the SFB measure on the Investment and elected to proceed without any form of consultation or notice to Pope & Talbot.

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[117] Counter-Memorial (Second Phase) at para. 412.

[118] As set out in the Memorial (Second Phase) at paras. 239-246, and 288-293.

[119] Counter-Memorial (Second Phase) at para. 160, and George Affidavit #3 at paras. 138-139.

[120] George Affidavit #3 at para. 143.

102. Counsel for Canada states that "the Investor provides no evidence to support its claim that SFB more than offset any benefit of reduced stumpage."[121] For a British Columbia softwood lumber company, which operated on the coast and did not export lumber at the LFB or UFB fees levels, the benefits of the SFB would have entirely outweighed the costs. Counsel for Canada has made it clear that the purpose of the SFB levy was to make it "uneconomic" to ship LFB and SFB levy softwood lumber and that the measure would act as a general "export restraint".[122] In the case of Pope & Talbot, the Investor submits that such an export restraint is sufficient evidence during this phase of the arbitration to support the proposition that the Investment has been damaged.

103. In conclusion, Canada has failed to treat the Investment in accordance with international law, as required under NAFTA Article 1105, because it has imposed and operated the Export Control Regime in an arbitrary and non-transparent manner, with unfair and inequitable results. Moreover, Canada has failed to act in accordance with the international law principle of good faith, as expressed in the *pacta sunt servanda* rule and the theory of abuse of rights, by designing and imposing a measure that both violates its international obligations under the GATT generally, and that targeted Pope & Talbot specifically for deciding to pursue this NAFTA Claim.

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[121] Counter-Memorial (Second Phase) at para. 172.

[122] Memorial (Second Phase) at paras. 88-100.

SECTION THREE: NATIONAL TREATMENT

104. Counsel for Canada contends that in order to violate national treatment, the Investor must prove that it was the intent of the host government to discriminate by reason of nationality. With respect, the Investor submits a different view of the law, namely:

a) That it is not intent of the government measure but the effect that matters; and

b) A government's treatment is not based on some average level of treatment provided to all foreigners but whether a given NAFTA Investor, or its investment, receive less favourable treatment than domestic firms receive in like circumstances.

105. In *Procedural Order No. 9*, the Tribunal instructed the Investor that it could respond to issues related to NAFTA Article 1102 arising out of the new materials submitted to it. Canada was instructed that in addition to its response on NAFTA Article 1105 that it "may also include a response to any additional comments made by the Investor in relation to its Article 1102 case." The Investor's Memorial (Second Phase) complied with the explicit directions provided by this Tribunal in its procedural order. Canada has specifically reargued its national treatment case with respect to authorities submitted by the Investor in the Initial Phase of this arbitration. The Investor submits that Canada has grossly exceeded the limited scope permitted to it to respond to the Investor's Memorial (Second Phase).

The Investor has responded to those issues raised by Canada's Counter-Memorial (Second Phase) where appropriate, in particular regarding points of law, while at the same time being mindful of the need to not re-argue the whole of its national treatment case which is hereby incorporated by reference into this Memorial.[123]

I. EFFECTS MATTER, NOT INTENT

106. The established case law of national treatment clearly discloses that the fundamental objective of the obligation is to prohibit measures that have the effect of creating less favourable treatment to foreign investments and investors in like circumstances to domestic competitors. This obligation ensures that government conduct, either intentional or inadvertent, cannot be structured in a manner that causes foreign investors

[123] The Investor's Memorial (Second Phase) at para. 254 provides a summary of the Investor's previous submissions on national treatment.

(and their investments) to be treated in a fashion that is less favourable than similarly situated local investors.

107. Canada's position on national treatment rests on the proposition that for there to be a violation of the NAFTA Article 1102 national treatment obligation, the Investor must demonstrate some outward intent to discriminate. This argument is advanced by counsel for Canada without the support of any textual or international case law to support it.

108. The Investor has relied upon the GATT *Section 337* case in its Supplemental Memorial (Initial Phase) to demonstrate the framework for analysis of the GATT/WTO national treatment obligation for goods.[124] Counsel for Canada has argued that this case does not support the Investor's case but actually supports Canada's contention that national treatment must be "based on nationality". The actual award of this panel demonstrates the erroneous conclusions advanced by Canada. The GATT panel established that the legal test is not whether the government intended to discriminate but whether the government measure resulted in an effect that provided treatment less favourable to investors from other NAFTA Parties or their investments.[125] The obligation to provide treatment no less favourable in GATT Article III:4 is unqualified. Once goods are found to be like products, the national treatment obligation applies to determine whether the treatment is equal. Similarly, once investments are found to be in like circumstances under NAFTA Article 1102, only then does one look at the difference in treatment afforded by the government to the similarly situated investments.

109. There is a good policy reason underscoring this focus on discriminatory effect rather than intent. It is exceedingly difficult to objectively establish intent before an independent international panel, but the question of effect can be objectively assessed [126]. Thus, in the

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[124] Supplemental Memorial (Initial Phase) at para. 55.

[125] *Section 337* at para. 5.11 stated:

> ...it has also been recognized that there may be cases where application of formally identical legal provisions would in practice accord less favourable treatment to imported products and a contracting party might thus have to apply different legal provisions to imported products to ensure that the treatment accorded to them is in fact no less favourable.

[126] Counter-Memorial (Second Phase) at paras 483 - 484. Canada has referred to certain facts regarding the WTO dispute settlement body ruling in the *Japan-Alcohol* case These facts were irrelevant to the judgment made by the panel or by the Appellate Body with respect to the "like products" concept in the first sentence of Article III:2 of the GATT. The facts cited by Canada concerning effects on foreign versus domestic producers were relevant only to the analysis of whether there was similar taxation of competitive and substitutable products "so as to afford protection of domestic production." The requirement to show that dissimilar treatment is applied so as to afford

WTO *Bananas* case, the Appellate Body explicitly held that if like products are being treated less favourably, there is no need for a separate inquiry into whether the measure has been applied so as to afford protection to domestic production.[127] Canada has similarly mis-characterized the conclusions of the GATT panel in *Canada-Beer*[128]. The panel found that a minimum price requirement for beer that was applied identically to domestic and foreign products was inconsistent with Canada's national treatment obligation[129]. Accordingly, Canada's observation that national treatment must be connected to discrimination motivated on the basis of nationality is not correct[130].

II. THE EFFECT IS MEASURED UPON A PARTICULAR INVESTMENT

110. The test that must be applied by this Tribunal is not whether Canada applied national treatment in general, or on balance to a wide group of companies, but whether it provided national treatment in particular to Pope & Talbot, Inc. and its investments in Canada. Counsel for Canada has provided summaries of WTO jurisprudence in *Bananas, Autos, Japan-Alcohol, Spain-Coffee,* all to support its argument that to prove a breach of national treatment, a claimant must demonstrate that most of the discrimination caused by the impugned measure affected foreigners and that the favourable treatment went to domestic firms. There is no requirement to demonstrate an outright intent to discriminate on the basis of nationality in order to establish that a government has not met its obligation to provide national treatment.

111. International economic law has established that a violation of national treatment will occur if the effect of the government measure does not provide treatment as favourable as

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protection to domestic production, is a requirement unique and particular to the analysis of "similar taxation" under the second sentence of Article III:2, which concerns national treatment with respect to taxation measures, and does not, unlike other national treatment provisions, contain the concept of likeness, but rather of "competitive and substitutable".

[127] *EC-Bananas* (AB) at para. 215.

[128] Counter-Memorial (Second Phase) at para. 468.

[129] Investor's Memorial (Second Phase) at paragraph 262. *Canada-Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies* (18 February, 1992) DS17/R-39S/27 at para. 5.27. Investor's Supplemental Book of Authorities, Tab 18.

[130] In the *EC-Bananas* case, Canada attempts to distinguish the facts of the case while ignoring the general legal principle that the Investor relies on at paragraph 59 of its Memorial (Initial Phase). The general principle that is applied and adopted by the Appellate Body in that case was simply that intentional discrimination on the basis of nationality is not required to find a breach of national treatment or most favoured nation treatment.

that provided to similar domestic investments. Thus, the *Japan-Alcohol* and *US-Alcohol* cases involved measures that were **completely** facially neutral with respect to nationality, yet these panels still found that the measures constituted *de facto* discrimination. The panels in these cases in no way attempted to balance domestic against foreign interests that were affected, as Canada seems to suggest is the test[131].

112. If Canada's theory were adopted, this tribunal would have to perform a balancing act to determine if foreign investors affected by a discriminatory measure outnumber the domestic producers protected. It is clear that GATT/WTO panels have routinely dismissed this "balancing" or trade effects type argument in several cases such as the recent WTO *Canada - Patent Terms* case, as well as in the GATT *US-Section 337* case. Canada argued in the recent WTO *Canada -Patent Terms* case that the number of foreign patents discriminated against (that is, the number of patents receiving a period less than 20 years of patent protection required by the WTO *TRIPS Agreement*) was smaller than the number of foreign patents that actually received the minimum 20 years of protection required under the *TRIPS Agreement*. In rejecting Canada's argument on this issue the panel in the *Canada -Patent Terms* case, adopting the Panel's ruling in the *US-Section 337* case, stated as follows:

> To meet the standard enunciated in United States - Section 337, **all** Old Act patents would have to have a term of protection that did not end before 20 years from the date of filing. It cannot be assumed that all Old Act patents had a pendency period of three years or longer and therefore a term of protection that did not end before 20 years from the date of filing because an **average** figure of two to four years necessarily embraces shorter periods which result in patents with a term of protection that ends before 20 years from the date of filing. In fact, the parties agree that many Old Act patents, including many still in force, will expire before 20 years from the date of filing.[132] [emphasis in original]

In ruling against Canada, the Panel held that all that was required to find a breach of the *TRIPS Agreement* was that there was at least one Old Act patent that was discriminated against under the Canadian patent law irrespective of the fact that other foreign patents actually received better treatment than required under the *TRIPS Agreement*.[133]

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[131] For example, in *US-Alcohol* there were some local state measures that provided in-state producers with more favourable treatment than out of state producers. The measures at issue were completely neutral with respect to nationality and therefore did not discriminate on the basis of national origin – the only discriminating feature of the measure was that the in-state producers received more favourable treatment than everyone else with the effect of harming foreign producers from Canada.

[132] *Canada-Patent Terms*, at para.6.99. Investor's Supplemental Book of Authorities, Tab 14.

[133] *Canada-Patent Terms*, at para. 6.100. Investor's Supplemental Book of Authorities, Tab 14.

113. The argument raised by Canada about a "general-average" of effect on investments was unsuccessfully advanced by the Government of the United States in the GATT *US-Section 337* case. In that case, the US argued that in certain circumstances some foreign investors might actually be treated better than US investors, which would offset those foreigners that were treated worse, however, on balance the treatment would not be discriminatory. The GATT panel dismissed this reasoning out of hand and held that the national treatment obligation applied in every instance to every single product was not an obligation that could be aggregated and viewed as part of some general balance of treatment. Every Investor is entitled to receive national treatment under NAFTA Article 1102. Specifically the Panel noted:

> The "no less favourable" treatment requirement of Article III:4 has to be understood as applicable to each individual case of imported products. The Panel rejected any notion of balancing more favourable treatment of some imported products against less favourable treatment of other imported products. If this notion were accepted, it would entitle a contracting party to derogate from the no less favourable treatment obligation in one case, or indeed in respect of one contracting party, on the ground that it accords more favourable treatment in some other case, or to another contracting party. Such as interpretation would lead to great uncertainty about the conditions of competition between imported and domestic products and thus defeat the purposes of Article III.[134]

Accordingly, counsel for the Investor respectfully disagrees with counsel for Canada with respect to their characterization of *de jure* and *de facto* discrimination, which can also be described as facial and effects based discrimination. Counsel for the Investor has argued, and asks the Tribunal to accept, that facial distinction "based on nationality" is not required for **either** *de facto* or *de jure* discrimination.

114. The difference between the two types of discrimination was confirmed in the recent WTO *EC-Asbestos* case, where the Panel made it clear that France's prohibition on asbestos, which contained no distinction based on nationality whatsoever, constituted *de jure* discrimination because asbestos and its substitutes were "like" products and therefore singling out asbestos constituted a violation of national treatment.[135] There was no discussion at all about facial classifications related to national origin in the Panel's consideration of whether the measure violated national treatment.

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[134] *United States-Section 337 of the Tariff Act of 1930* at para. 5.14. See Supplemental Memorial (Initial Phase) at para. 63. Investor's Supplemental Book of Authorities, Tab 54.

[135] *European Communities - Measures Affecting Asbestos and Asbestos -Containing Products*, September 18, 2000, WT/DS135/R, at paras. 8.151 to 8.158. Investor's Supplemental Book of Authorities, Tab 7.

115. In light of Canada's inaccurate argumentation about *de facto* discrimination in its Counter-Memorial (Second Phase), the Investor submits that many of Canada's violations of national treatment with respect to the Investor are in fact *de jure* violations. In other words, the Export Control Regime provides explicitly different and less favourable treatment to the Investor than that provided to Canadian investors in like circumstances. However, since the jurisprudence explicitly recognizes both *de jure* and *de facto* discrimination, it is not necessary to articulate each of these claims as either *de jure* or *de facto* discrimination. The only test that the Investor must meet is that it is in like circumstances to domestic softwood lumber producers and that the Export Control Regime provided the Investor with less favourable treatment (either directly or indirectly).

116. The national treatment obligation reflects the principle of legal security requiring that an investor and its investments are not subjected to discrimination whether it is *de jure* or *de facto*. The NAFTA national treatment standard is clearly not restricted to those limited cases of direct discrimination based upon the nationality of the Investor. The affidavits provided by Mr. George and Mr. Valle in support of Canada's Counter-Memorial (Second Phase) continue to reiterate that it did not intend to discriminate nor that the measure discriminated based on nationality. The presence of such intention or facial discrimination is not required for Canada to have breached NAFTA Article 1102.

III. LIKE CIRCUMSTANCES

117. Counsel for Canada continues to present the national treatment legal test in reverse order to this Tribunal. Canada suggests that the Tribunal must first decide whether discrimination exists or not, and then proceed to determine whether the Investment is in like circumstances to domestic investments. That approach is not consistent with the widely accepted test in international law, which the Investor has set out in its Supplemental Memorial (Initial Phase).[136] The first step is to determine whether the goods are "like" or not. Once it is determined that they are "like", then the second part of the test involves an examination of whether the treatment is discriminatory. This is the test that has been consistently applied by all GATT/ WTO dispute panels and has never been contested by Canada or any other disputing party.

118. Moreover, the Investor submits that counsel for Canada has incorrectly stated the test for determining "like circumstances". Canada has stated that the "like circumstances" test involves an inquiry that "...requires an examination of the circumstances in which the treatment was accorded. It is largely a factual determination. It is not sufficient that the

[136] Supplemental Memorial (Initial Phase) at paras. 37-41.

Investment sells like products as other softwood lumber producers. Article 1102 requires comparison of all the circumstances surrounding the treatment accorded."[137]

119. Counsel for Canada has clearly cast a net too wide for a concept that has been well-developed in the international case law. Very simply, the key element in the test that grounds the analysis of likeness relates to whether equality of competitive opportunity has been assured.[138] Canada has ignored this key element of the likeness test in error.

IV. CANADA IS REQUIRED TO PROVIDE THE "BEST AVAILABLE TREATMENT"

120. Canada argues in its Counter Memorial (Second Phase) that "there is no basis...which supports the Investor's argument that a foreign investor is entitled to the best treatment available to any other investor in the same sector in the same country".[139] Canada has ignored the jurisprudence underlying this well-accepted notion. If the standard was not to provide the "best available treatment" then Canada could be the architect of discriminatory measures by treating some domestic investors less favourably than other domestic investors and then use that as the standard to compare the treatment given to foreign investors. Moreover, treatment no less favourable must mean that a NAFTA Party investment must receive the "best treatment" as otherwise the investor would always receive have "less favourable treatment" as there would be someone receiving better treatment. By not comparing the aggrieved foreign investor with the best treated domestic investor, in like circumstances, there is discrimination because the foreigner is being given less favourable treatment to the "best treated" domestic investor. Canada's refutation of the "best available treatment" standard undermines the essence of the national treatment obligation, which is to prohibit discriminatory measures.

121. In conclusion, Canada has fundamentally misstated the national treatment obligation under NAFTA Article 1102. For Canada to say that the "core of the national treatment obligation is that investors and investments of another NAFTA Party must not be discriminated against because they are foreign owned" or "based on nationality" ignores and misstates the development of the ample GATT/ WTO jurisprudence cited by the Investor in support of the exactly opposite proposition. Canada has not cited a single authority that stands for such a proposition. As with the case of its interpretation of

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[137] Counter-Memorial (Second Phase) at para. 442 - 443.

[138] Memorial (Second Phase) at para. 262 - 263; Supplemental Memorial (Initial Phase) at para. 47 - 57.

[139] Counter-Memorial (Second Phase) at para. 454.

NAFTA Article 1105, Canada's arguments are based on a view of international law, which does not take into account the significant international developments of the past 50 years.

122. The national treatment obligation reflects the principle of legal security requiring that an investor and its investments are not subjected to discrimination whether it is *de jure* or *de facto*. The NAFTA national treatment standard is clearly not restricted to those limited cases of direct discrimination based upon the nationality of the Investor. The affidavits provided by Mr. George and Mr. Valle in support of Canada's Counter-Memorial (Second Phase) continue to reiterate that it did not intend to discriminate, nor did it discriminate, based on nationality. The presence of such intention or facial discrimination is not required for Canada to have breached NAFTA Article 1102.

123. The national treatment obligation in the NAFTA is based on two fundamental tests: (1) whether the investor or investments are in "like circumstances" with domestic investors and investments, and then (2) whether the foreign investor or investment has been accorded "treatment no less favourable" in comparison with like domestic investors. Canada continues to conflate and confuse these two tests to support its base premise that national treatment is "based on nationality" in its application. The focus of national treatment is on nationality, but only in relation to the best treatment provided, and does not require that the "less than best treatment" be directed at foreign nationals solely. There is no *de minimis* test as suggested by Canada.

124. The core of national treatment in the NAFTA is that measures must not affect foreign investors in a manner that provides them with less than the best treatment available. This reflects the fundamental objective of legal security that measures must provide transparency and predictability to avoid arbitrary and discriminatory conduct, whether *de jure* or *de facto*, by the NAFTA state Parties.

V. NATIONAL TREATMENT LAW APPLIED TO THE FACTS

A. General Overview

125. The Investor submits that Canada has breached its obligations with respect to national treatment pursuant to NAFTA Article 1102, as addressed by the Investor in its Memorial (Second Phase). In response to Canada's Counter-Memorial (Second Phase), it is apparent that there is a fundamental difference in view as to the proper interpretation of these legal concepts and their application to the facts. There is less of a disagreement as to the actual conduct of Canada in its implementation of the Export Control Regime.

126. Canada explains its conduct in its submissions based on two inconsistent notions. Canada has repeatedly stated that it relied on "consultation" and "consensus" with the "industry" and the British Columbia Advisory Committee. Canada also states numerous times that the Minister exercised his ultimate decision making ability, regardless of outside inputs. These explanations can only be correct if one accepts, as Canada did, an arbitrary philosophy of quota allocation involving no internal administrative review mechanism, and which favoured an ad hoc and non-transparent system of discretionary allocations. As part of Canada's "squeaky wheel" system of administration, it assured non-transparency of the Export Control Regime by asserting confidentiality over critical aspects of the regime, such as the wholesaler allocation and the 1997 British Columbia re-allocation.

127. In summary, Canada has not met its obligation to provide national treatment to the Investor and its Investments through the following actions:

a. Canada has failed to provide the best treatment available to softwood lumber manufacturers who have been subjected to the Export Control Regime. This has been more fully argued in the Investor's submissions in Phase One of this arbitration and the Investor directs the Tribunal to those submissions;

b. Canada has failed to provide the best treatment available in the allocation of discretionary allocations to softwood lumber manufacturers in other Listed Provinces. In particular, the Investor submits that the cumulative impact of discretionary quota allocation by Canada has violated its national treatment obligation;

c. Canada has failed to provide the best treatment available to the Investment in resolution of the wholesaler allocation issue; and

d. Canada has failed to provide the best treatment available under the Export Control Regime to the Investor and its Investment by providing the best treatment in Canada to softwood lumber manufacturers not subjected to the payments of the SFB Levy.

B. Listed and Non-Listed Provinces

128. Canada argues in its Counter-Memorial (Second Phase) that the "key and conclusive" differentiating circumstance of the treatment accorded to investments in covered provinces compared to non-covered provinces is that the *Softwood Lumber Agreement*

expressly applies to the four covered provinces.[140] Canada's argument stands for the proposition that a distinction that Canada has itself created (e.g. limiting the *Softwood Lumber Agreement* to the four Listed Provinces) and given a legal meaning in a bilateral export restraint agreement, can justify the conclusion that investors are not "in like circumstances". If this proposition were accepted then a NAFTA party could alter, and indeed reduce, the scope of its own national treatment obligations.

129. Under this scenario, Canada could, through its own decisions, entrench in international treaties the very distinctions that it then would later argue to allow less favourable treatment of investors from other NAFTA Parties. In view of these distinctions – which have legal meaning only because Canada has decided to give them such meaning – the investors of other NAFTA Parties are no longer "in like circumstances". The result would directly run counter to providing legal security to other NAFTA investors, one of the key objectives of Chapter 11.[141]

130. Moreover, if Canada's position is correct then the *Softwood Lumber Agreement* should have specifically excluded the Non-Listed Provinces in the treaty. Nowhere in the *Softwood Lumber Agreement* did the Parties to that agreement do so.[142] Thus, Canada cannot now unilaterally alter the meaning of "like circumstances" because of this omission.

131. Simply because the *Softwood Lumber Agreement* expressly included some provinces and did not include others, this can in no way affect the "circumstances" that all softwood lumber producers are in. In effect the *Softwood Lumber Agreement* has included all provinces for the purpose of protection against CVD action, but excluded Non-Listed Provinces from having to pay the price of such protection by being exempt from the Export Control Regime. In other words, all softwood lumber producers in Canada, including Pope & Talbot, are in like circumstances - they compete in the same market for the same commodity, and for the same market share.

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[140] Counter-Memorial (Second Phase) at para. 499.

[141] In effect, Canada's proposition amounts to the notion that the *Softwood Lumber Agreement* represents a reduction of the rights of investor and their investments under NAFTA Chapter 11. Such a proposition is unsupported by the wording, purpose and structure of the *Softwood Lumber Agreement*.

[142] This is counter to Canada's contention that the *Softwood Lumber Agreement* "provides for measures only to apply to those [covered] provinces.": Counter-Memorial (Second Phase) at para. 500.

C. Super Fee Base Levy

132. The Investor submits that the Super Fee Base levy measure is a violation of Canada's NAFTA obligations pursuant to NAFTA Articles 1102 .[143] Canada unfairly created a measure as a part of its Export Control Regime that had a disproportionate and discriminatory impact on Pope & Talbot.

133. The effects of the Super Fee Base levy were to cause treatment that was less favourable to the Investment than the treatment received by other producers of softwood lumber operating in Canada.[144] This more favourable treatment was received by:

a. other softwood lumber manufacturers operating in Non-listed Provinces, who had to pay no levy payments at all;

b. Other softwood lumber manufacturers operating in Listed Provinces, who had a maximum levy payment at the UFB level; or even

c. other softwood lumber manufacturers in British Columbia who received a significantly greater discount in the British Columbia timber stumpage rate (such as those on the coast).

Canada's measure to impose the Super Fee Base levy immediately caused to the Investor and its Investments a difference in treatment that was less favourable than that received by other investments in like circumstances. This treatment is inconsistent with Canada's obligation under NAFTA Article 1102.

D. The Cumulative Impact of Discretionary Quota Allocation

134. The inequitable and unfair manner in which Canada allocated discretionary reserves and Trigger Price Bonus quota is a classic tale of "death by a thousand cuts". In each case, Canada's discretionary approach to reserve and bonus quota allocation negatively impacted upon the Investment's ability to sell its products to the US market.

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[143] As set out in the Memorial (Second Phase) at para. 239-246, and 288-293.

[144] Furthermore, as the Investor has set out earlier in this Supplemental Memorial, the evidence indicates that Canada had prior knowledge that its Super Fee Base measure would cause a large amount of harm specifically to Pope & Talbot, Ltd. While this intent to discriminate is not necessary to the making of a finding of a breach of national treatment, it is certainly relevant.

135. The transitional reserve removed some valuable quota from the Investment, which could have marginally improved its year-one growth formula performance. The new entrants reserve allocation caused widespread harm in British Columbia that Canada did not proportionately remedy with the ministerial hardship reserve. The British Columbia re-allocation exercise and subsequent discretionary awards of bonus quota (largely on the direction of lumber producers selected by the Minister for his "Advisory Committee") provided some remediation for certain members of the British Columbian softwood lumber community, but only to the detriment of the Investment.

136. The Investment suffered harm, as a result of the cumulative effect of these discretionary allocation decisions, because it was entitled to the same re-allocation remedy for the wholesaler problems, but received none (and was forced to lose quota to benefit others). Similarly, the Investment was entitled to a *pro rata* share of all bonus quota, of which it received only a fraction. If not for the hardship caused in the British Columbia community by the manner in which these allocations were made, the Investment would have obtained more access to the US market than it actually obtained.

137. With respect to the manner in which it allocated the transitional reserve, Canada argues that there is no evidence of a rush to the border on the part of some lumber producers. Mr. George actually admits in his second affidavit that the "rush to the border" did take place. This acknowledgement is in perfect accord with the documents discovered by the Investor that discuss the border rush and how it was addressed by allocations of the so-called transitional reserve.[145]

138. Mr. Valle contends that the 170 million board feet ("MMBF") reserved for the minority of companies who over-shipped into the US market in the first two quarters of the Regime (notwithstanding their being warned that they could only export fee free the amount of lumber that would be assigned in their individual allocations for the year) was "insubstantial".[146] The Investor, whose Investment Canada confirms did not rush the border,[147] argues that 170 MMBF is not an inconsequential amount, and could have been used by all other equally deserving quota recipients to improve how they faired in the growth mechanism, applied at the end of year one, had they been given the opportunity to export their fair share. Instead, the 170 MMBF appears to have been awarded to

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[145] Memorial (Second Phase) at paras. 37-40.

[146] Counter-Memorial (Second Phase) at para. 54. Canada confirms that: "As well, a number of quota holders made shipments in the initial six months at levels that exceeded their entire annual quota. A pool of quota was needed for those exports." Also see Valle Affidavit #2 at para. 134.

[147] Counter-Memorial (Second Phase) at para. 60.

exporters who were either not entitled to any fee free exports, or were at least not entitled to export as much as they had actually exported in their rush to the border.

139. Moreover Canada did not decide to extract the reserve "off the top" of the 14.7 MMBF available to all producers – rather than from provincial shares – until after it knew who was rushing the border and therefore likely to be in need of a transitional allocation. This is yet another example of how Canada had the option of choosing an allocation and keeping with the published provincial shares and instead chose to favour producers in one region over another.[148]

140. With respect to the new entrants reserve, Canada disputes that the Investment was "led to assume" that new entrant quota would be allocated by provincial share.[149] In support, Mr. Valle states in his second affidavit that Canada "... did not anticipate criticism based on the argument that a province did not receive its provincial corporate share of new entrant quota."[150] He makes this statement in response to the passage cited from the document titled "Issues Checklist", dated October 6, 1996, which stated with respect to the new entrants allocation that:

> The issue of provincial distribution will also be sensitive, although this quota is not intended to be subject to any constraints related to provincial shares.[151]

141. This passage is actually relevant because it shows, for the first time in the documentary evidence, that the new entrants quota would not be subject to provincial corporate shares. Although in the many documents related to the August 1996 consultations it appears that "stakeholders" accepted the need for a new entrants quota allocation, there was no indication that the quota would not be subject to provincial shares.

142. Canada states that the Investor has tendered no evidence to support its assertion that "Canada unilaterally decided, without consultation or announcement, to first deduct the

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[148] Schedule 43 - Memorial (Second Phase) "issue check list", under the heading 'Overages'.

[149] At paragraph 71 of the Counter-Memorial (Second Phase).

[150] Valle Affidavit #2 at para. 93.

[151] Memorial (Second Phase) at para. 30 and Schedule 43 of the Memorial (Second Phase). It is also interesting to note from this memorandum that Canadian officials pondered: "how transparent and consultative" they should make the process given that producers' views in different provinces would "clearly not converge". Canada apparently concluded, as a result, not to employ a transparent or open process – demonstrating exactly who would be awarded quota, how and why.

discretionary allocations from the national allocation."[152] In response, the Investor notes that Canada had made its position known in its letter of September 30, 1996 to the Investment, and the September 10th Ministerial Press Release. In the next public document provided to the Investment, the letter of November 7th, 1996, Canada's position changed fundamentally, even though it has provided no evidence of consultation in the interim to explain such a radical shift in allocation methodology. These documents stated that British Columbia would be allocated 8.673 BBF, or 59% of 14.7 BBF[153] not 8.369 BBF as later documents state.

143. The Investor, like other softwood lumber manufacturers, including the Investment, could reasonably have been expected to rely on the public statements of the Minister made in September 1996 relating to the quota allocation. Once the Minister made these statements, lumber producers should have been able to expect that any fundamental changes in provincial allocation would not occur without consultation and comment by members of the industry directly affected, such as Pope & Talbot. Pope & Talbot was not consulted or advised that Canada planned to make such a fundamental change to the new quota allocation under the Export Control Regime, nor was any comment sought from them on the proposed changes.

144. Further, Canada has provided no evidence that it consulted with Pope & Talbot or other companies between September 30th and November 7th, 1996, except to rely on Mr. Valle's statement in response to paragraph 30 of the Investor's Memorial (Second Phase) that "The deductions were made only after extensive consultation."[154]

145. In summary, as the evidence concerning the August consultations makes abundantly clear, the bargain that was being worked with the so-called stakeholders placed Central Canada in conflict with the West. British Columbia and Alberta sought to assure their historical provincial corporate shares whereas Ontario and Quebec manufacturers sought discretionary allocations, larger than historical provincial shares, and restrictive definitions to further increase quota for the primary mills. In light of the fact that the question of provincial shares was such a sensitive issue, as Canada suggests, the Investor submits that it would certainly have been the type of issue that would have been addressed by the Minister and his cabinet colleagues from Quebec. The Investor notes the complete

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[152] Paragraph 30 of its Counter-Memorial (Second Phase).

[153] Memorial (Second Phase) at para. 27.

[154] Valle Affidavit #2 at para. 165.

absence of inter-ministerial and cabinet briefing memoranda on this critical issue in the materials provided to the Investor and the Tribunal by Canada.

146. The manner in which Canada eventually allocated the new entrants reserve was of direct and substantial benefit to producers in central Canada[155]. Despite the fact that British Columbia producers clearly qualified for more than 59% of the available new entrants reserve, Canada decided to pro rate its allocation of the new entrants reserve to all qualifying applicants. This decision compounded the impact of Canada's earlier, unilateral decision to ensure that the reserve would be "taken off the top", rather than being apportioned based on agreed upon historical shares.

147. Canada's decision to use the new entrants reserve to move quota from the west to the east created significant hardships in the British Columbia community. When it finally came time to redress some of the harm caused, Canada imposed British Columbia specific solutions (e.g. the British Columbia re-allocation in 1997, and special allocations of bonus quota in later years) that spread the harm around British Columbia, depriving the Investment of quota to which it would have otherwise been entitled.

148. With respect to the ministerial reserve, Mr. Valle states in his second affidavit that when Canada assessed requests for allocations from the Minister's Reserve that:

> ... the province of origin, or identity of investors, of a company seeking hardship relief is irrelevant. I know of no case where officials reviewing a hardship request considered the province of origin, or the identity of investors in, a company seeking hardship relief.[156]

149. Canada also states at paragraph 44 of its Counter-Memorial that it "flatly denies" the allegation that investments with "access" to the Minister had their concerns addressed,[157] however the evidence appears to support that direct lobbying and access to the Minister did in fact result in some softwood lumber producers obtaining more quota, even in cases where they clearly were not entitled to it.[158]

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[155] As stated at paragraphs 42 to 52 of the Memorial (Second Phase).

[156] Valle Affidavit #2 at para. 106.

[157] Counter-Memorial (Second Phase) at para. 44.

[158] Schedule 2, Action Memorandum from K. Aird to MINT dated August 1, 1997 at 5. Minister's Confidential Briefing Memoranda, September 8, 1997 at 1-2. This memorandum was not provided by Canada in response to the Investor's document requests, but obtained through the *Access to Information Act* process. Schedule 3, Action Memorandum from Douglas George, Softwood Lumber Task Force, to The Minister of International Trade, dated November 20, 1997 at para. 7. See also: Schedule 6, a heavily redacted memorandum dated July 18,

150. Accordingly, the Investor submits that this Tribunal should draw an adverse inference that the final decision to first deduct the discretionary allocations from the national allocation, before provincial corporate allocations, was made for regional political considerations, rather than on relevant criteria, such as historic performance.

151. Canada also argues that the historic shares agreed upon to set the provincial corporate shares were themselves "only loosely based" on actual historic export patterns. This statement is correct.[159] In fact, Canada knew that producers in the Province of Quebec were not even entitled to the 23% that the Minister decided to award as the provincial corporate share, despite officials running a number of different statistical scenarios in an effort to justify this number.[160] As indicated in a September 9, 1995 memorandum on the recalculation of provincial corporate shares that stated as follows:

> At the August 19-20 Ad Hoc Consultative Meeting we circulated the following 1995 Provincial Corporate shares numbers as a means of reaching consensus:
>
> | B.C. | Alberta | Ontario | Quebec |
> |---|---|---|---|
> | 59.51% | 7.55 | 10.20 | 22.74 |
>
> – there seemed to be general acceptance on the grounds that:
>
> (i) 1995 was reasonable trade off between B.C., which wanted 1994 data included and Ontario/Quebec, which wanted the latest 12 months
> (ii) the numbers looked O.K.
> (iii) there was nothing agreed until everything was agreed.
>
> • ...
>
> • In recent discussions with B.C. (Industry/government) representatives, they were unwilling to move off the August 19/20 market share numbers, which they saw as the main element of the compromise package.

1997, sent to the Minister's political assistant (via Douglas George), that appears to show how some producer decided to access the Minister's office directly, rather than await a bureaucratic response. While the Minister undoubtedly received many letters directly from producers, it would appear that some received the Minister's particular attention.

[159] Paragraph 182 of the Counter Memorial (Second Phase).

[160] Schedule 44 of the Investor's Memorial (Second Phase).

- We have examined a number of base year permutations to determine if we could approximate the August 19/20 provincial shares. In all cases these yield a significant loss to the Quebec share.
- ...
- Under the *Export and Import Permit's Act* you are given the discretion to determine the elements of the allocation decision, including in this case the relative shares between provinces.
- We propose, therefore, to allocate the provincial corporate shares as follows:

B.C.	Alberta	Ontario	Quebec
59.0	7.7%	10.3%	23.0%

152. It does not appear that industry members were ever informed that the Minister unilaterally decided to gross up the quota to be allocated to Quebec producers, despite the fact that even the members of the British Columbia industry, handpicked by the Minister to advise him, told him that they would accept no less than 59.5% as the "main element of the compromised package". After all was said and done, it appears that not even 57% was the amount that would actually be placed in the hands of British Columbia producers such as the Investment.

153. In addition to the quota re-allocation imposed upon British Columbia manufacturers by the Minister and his hand-picked Quota Allocation Committee in 1997, which addressed the quota allocation concerns and other perceived hardships of a select few manufacturers, the Minister and/or his Committee also used the allocation of trigger price bonus quota to provide particularized assistance to a privileged few.

154. Canada admits that the majority of trigger price bonus allocations were made along provincial lines, and that within each province the norm was to allocate the available quota on a *pro rata* basis.[161] The only general exception to this practice took place for manufacturers based in British Columbia, who received very little bonus quota on a *pro rata* basis. In the case of British Columbia, particularly manufacturers experiencing various forms of hardship were usually allocated a specific amount of quota, with *pro rata* allocations taking place less often and on a less substantial basis. The Investor submits that these various forms of hardship were substantially caused by the inequitable manner in which the Minister made his various discretionary allocations, and that – but

[161] Counter-Memorial (Second Phase) at paras. 104 - 120.

for such inequity – the Investment would have received more quota, representing its appropriate *pro rata* share.

155. Canada's treatment of the Investment in this regard represents both a breach of NAFTA Article 1102 and a breach of the "fair and equitable treatment" standard contained within NAFTA Article 1105. In the allocation of trigger price bonus quota, the Investment was entitled to the best treatment available in Canada – that is, the *pro rata* apportionment that was consistently made available to other producers operating in like circumstances in Ontario, Alberta and/or Quebec. Instead, the Investment received what can best be described as "table scraps" from the Minister's hand-picked industry advisory committee (which itself was attempting to come to terms with a great deal of hardship among British Columbia producers as a result of the operation of Canada's inequitable and unfair allocation process). Similarly, the Investment was entitled to receive the same treatment provided to other victims of the wholesaler problem in British Columbia – that is: the ability to partake in receiving extra quota from a re-allocation, rather than being subjected to the further loss of quota as part of that same re-allocation.

156. The cumulative impact of the discretionary manner in which the Minister conceived of, and then applied, the allocations to be made to producers in each province constitutes unfair and inequitable treatment of many British Columbia manufacturers, including the Investment. Both the re-allocation to address the wholesaler problem and the particularized allocations of trigger price quota made to ameliorate the losses of specific British Columbia manufacturers are evidence of Canada's unfair and inequitable treatment of the Investment. At the very least, the Investment should have received an allocation that was not reduced by "off the top" national reserves that were applied in an inequitable manner so as to cause further injury to the Investment when it came time to receive trigger price bonus allocations or suffer re-allocation to address a wholesaler problem that Canada did not even bother to inform the Investment that it actually had.

E. Conclusion

157. In conclusion, Canada has breached its NAFTA Article 1102 obligations by failing to provide the Investor and the Investment with as good a level of treatment as it has provided to some of their Canadian competitors. Competitors operating in like circumstances in provinces such as Manitoba or Saskatchewan were essentially exempted from the measure. Competitors operating in like circumstances in provinces such as Quebec or Ontario received comparatively less harm, and more opportunities to obtain and keep quota, than did Pope & Talbot. Finally, competitors both outside of British Columbia, and even inside the province fared comparatively better than did Pope & Talbot as a result of the combination of lower stumpage fees and imposition of the SFB

levy. NAFTA Article 1102 simply requires more from Canada, with respect to the way it has treated Pope & Talbot, in comparison to any of its domestic competitors, operating in like circumstances.

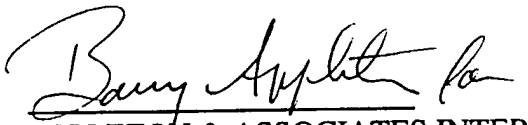
SECTION FOUR: CONCLUSIONS AND RELIEF

157. The Investor has stated throughout this arbitration that it has been the victim of unfair treatment as a result of Canada's Export Control Regime which did not provide it and its investment with national treatment in accordance with NAFTA Article 1102 or treatment in accordance with international law as required by NAFTA Article 1105. In reply, Canada has merely argued in a number of ways that the Investor is not entitled to the level of treatment that NAFTA mandates.

158. Canada has made arguments throughout this arbitration that if accepted would have the effect of rewriting the significant protections provided to NAFTA Investors through Chapter 11 of the NAFTA and specifically in Sections 1102 and 1105. The Investor submits that to accept Canada's arguments would have the result of undermining the legal security and protection that was guaranteed to it and all other NAFTA investors.

159. For the foregoing reasons, the Investor hereby reconfirms its request for the relief that it has previously sought in its earlier pleadings in this claim.

Submitted this 25th day of October 2000 at Toronto, Canada.



APPLETON & ASSOCIATES INTERNATIONAL LAWYERS
Counsel for the Investor, Pope & Talbot, Inc.

1140 Bay Street, Suite 300
Toronto, Ontario M5S 2B4