

IN THE MATTER OF AN ARBITRATION UNDER CHAPTER ELEVEN
OF THE NORTH AMERICAN FREE TRADE AGREEMENT
AND THE 1976 UNCITRAL ARBITRATION RULES
BETWEEN

WILLIAM RALPH CLAYTON, WILLIAM RICHARD
CLAYTON, DOUGLAS CLAYTON, DANIEL
CLAYTON, AND BILCON OF DELAWARE, INC.

Claimants/Investors,

-and-

GOVERNMENT OF CANADA,

Respondent/Party.

(PCA Case No. 2009-04)

SUBMISSION OF THE UNITED STATES OF AMERICA

1. Pursuant to Article 1128 of the North American Free Trade Agreement (NAFTA), the United States of America makes this submission on questions of interpretation of the NAFTA. The United States does not take a position in this submission on how the interpretation offered below applies to the facts of this case, and no inference should be drawn from the absence of comment on any issue not addressed below.

Limitations on Claims for Loss or Damage under Articles 1116(1) and 1117(1)

2. Each claim by an investor must fall within either NAFTA Article 1116 or NAFTA Article 1117 and is limited to the type of loss or damage available under the Article invoked.¹ Article 1116(1) permits an investor to present a claim for loss or damage incurred by the investor itself:

¹ An investor may bring separate claims under both Articles 1116 and 1117; however, the relief available for each claim is limited to the article under which that particular claim falls.

An investor of a Party may submit to arbitration under this Section a claim that another Party has breached an obligation . . . and that the *investor* has incurred loss or damage by reason of, or arising out of, that breach. (emphasis added).

3. Article 1117(1), in contrast, permits an investor to present a claim on behalf of an enterprise that it owns or controls for loss or damage incurred by that enterprise:

An investor of a Party, *on behalf of an enterprise* of another Party that is a juridical person that the investor owns or controls directly or indirectly, may submit to arbitration under this Section a claim that another Party has breached an obligation . . . and that the *enterprise* has incurred loss or damage by reason of, or arising out of, that breach. (emphasis added).

4. Articles 1116 and 1117 serve to address discrete and non-overlapping types of injury.² Where the investor seeks to recover loss or damage that it incurred *directly*, it may bring a claim under Article 1116. However, where the alleged loss or damage is only to an enterprise that the investor owns or controls, the investor's injury is only *indirect*,³ and therefore, the investor must bring a derivative claim under Article 1117.⁴

5. The United States' position on the interpretation and functions of Articles 1116(1) and 1117(1) is long-standing and consistent.⁵ The United States therefore agrees with Canada⁶ and

² See North American Free Trade Agreement, Implementation Act, Statement of Administrative Action, H.R. Doc. No. 103-159, Vol. I, 103d Cong., 1st Sess., at 145 (1993) (“Articles 1116 and 1117 set forth the kinds of claims that may be submitted to arbitration: respectively, allegations of direct injury to an investor, and allegations of indirect injury to an investor caused by injury to a firm in the host country that is owned or controlled by an investor.”).

³ The disputing parties use the term “reflective loss” to describe the damages the claimants are seeking in this case. For the purposes of this submission, the United States treats “indirect” loss or damage as synonymous with “reflective” loss or damage.

⁴ See, e.g., Lee M. Caplan & Jeremy K. Sharpe, *Commentary on the 2012 U.S. Model BIT*, in COMMENTARIES ON SELECTED MODEL INVESTMENT TREATIES 824-25 (Chester Brown ed., 2013) (“Caplan & Sharpe”) (noting that Article 24(1)(a), nearly identically worded to NAFTA Article 1116(1), “entitles a claimant to submit claims for loss or damage suffered directly by it in its capacity as an investor,” while Article 24(1)(b), nearly identically worded to NAFTA Article 1117(1) “creates a derivative right of action, allowing an investor to claim for losses or damages suffered not directly by it, but by a locally organized company that the investor owns or controls”).

⁵ See, e.g., *S.D. Myers, Inc. v. Government of Canada*, NAFTA/UNCITRAL, Submission of the United States of America ¶¶ 6-10 (Sept. 18, 2001) (“Articles 1116 and 1117 of the NAFTA serve distinct purposes. Article 1116 provides recourse for an investor to recover for loss or damage suffered by it. Article 1117 permits an investor to bring a claim on behalf of an investment for loss or damage suffered by that investment.”); *Pope & Talbot, Inc. v. Government of Canada*, NAFTA/UNCITRAL, Seventh Submission of the United States of America ¶¶ 2-10 (Nov. 6, 2001) (same); *GAMI Investments, Inc. v. United Mexican States*, NAFTA/UNCITRAL, Submission of the United States of America ¶¶ 2-18 (June 30, 2003); *International Thunderbird Gaming Corp. v. United Mexican States*, NAFTA/UNCITRAL, Submission of the United States of America (May 21, 2004).

⁶ See, e.g., *William Ralph Clayton & Bilcon of Delaware Inc. et al. v. Government of Canada*, NAFTA/UNCITRAL, Government of Canada Counter-Memorial on Damages ¶ 28 (June 9, 2017); *id.* n.50 (authorities cited including Canada's prior statements on same); *S.D. Myers, Inc. v. Government of Canada*, NAFTA/UNCITRAL, Counter-Memorial (Damages Phase) ¶¶ 108-109 (June 7, 2001).

Mexico⁷ that investors must allege direct damage to recover under Article 1116 and that indirect damage to an investor, based on injury to an enterprise the investor owns or controls, may only be claimed through Article 1117. Pursuant to Article 31(3)(a)-(b) of the Vienna Convention on the Law of Treaties, this subsequent agreement or subsequent practice of the NAFTA Parties “shall be taken into account” in interpreting Articles 1116 and 1117.⁸

6. This distinction between Articles 1116 and 1117 was drafted purposefully in light of two existing principles of customary international law addressing the status of corporations. The first of these principles is that no claim by or on behalf of a shareholder may be asserted for loss or damage suffered directly by a corporation in which that shareholder holds shares. This is so because, as recently reaffirmed by the International Court of Justice in *Diallo*, “international law has repeatedly acknowledged the principle of domestic law that a company has a legal personality distinct from that of its shareholders.”⁹ As the *Diallo* Court further reaffirmed, quoting *Barcelona Traction*: “a wrong done to the company frequently causes prejudice to its shareholders.” Nonetheless, “whenever a shareholder’s interests are harmed by an act done to the company, it is to the latter that he must look to institute appropriate action; for although two separate entities may have suffered from the same wrong, it is only one entity whose rights have been infringed.”¹⁰ Thus, only *direct* loss or damage suffered by shareholders is cognizable under international law.¹¹

7. How a claim for loss or damage is characterized is therefore not determinative of whether the injury is direct or indirect. Rather, as *Diallo* and *Barcelona Traction* have found, what is

⁷ See, e.g., *S.D. Myers, Inc. v. Government of Canada*, NAFTA/UNCITRAL, Submission of the United Mexican States (Damages Phase) ¶¶ 41-45 (Sept. 12, 2001) (explaining that Article 1116 allows an investor to bring a claim for loss or damage suffered by the investor and that Article 1117 allows an investor to bring a claim for loss or damage on behalf of an enterprise (that the investor owns or controls) for loss or damage suffered by the enterprise); *GAMI Investments, Inc. v. United Mexican States*, NAFTA/UNCITRAL, Statement of Defense ¶¶ 167(e) and (h) (Nov. 24, 2003).

⁸ Vienna Convention on the Law of Treaties, May 23, 1969, 1155 U.N.T.S. 331, 8 I.L.M. 679 (1969) (“VCLT”), arts. 31(3) (a)-(b) (“There shall be taken into account, together with the context: (a) Any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions; (b) Any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation[.]”). The International Court of Justice concluded that Article 31 of the VCLT reflects customary international law. See, e.g., *Kasikili/Sedudu Island (Botswana v. Namibia)*, 1999 I.C.J. 1045, 1059 (Judgment of Dec. 13). Although the United States is not a party to the VCLT, it has recognized since at least 1971 that the Convention is the “authoritative guide” to treaty law and practice. See Letter of Submittal from Secretary of State Rogers to President Nixon transmitting the VCLT (Oct. 18, 1971), reprinted in 65 DEP’T ST. BULL. 684, 685 (Dec. 13, 1971).

⁹ *Ahmadou Sadio Diallo (Republic of Guinea v. Democratic Republic of the Congo)*, 2010 I.C.J. 639, ¶¶ 155-156 (Judgment of Nov. 30) (noting also that “[t]his remains true even in the case of [a corporation] which may have become unipersonal”).

¹⁰ *Id.* ¶ 156 (quoting *Barcelona Traction, Light and Power Company, Ltd. (Belgium v. Spain)*, 1970 I.C.J. 3, ¶ 44 (Second Phase, Judgment of Feb. 5) (“*Barcelona Traction*”). See also *Barcelona Traction* ¶ 46 (“[A]n act directed against and infringing only the company’s rights does not involve responsibility towards the shareholders, even if their interests are affected.”).

¹¹ See *Barcelona Traction* ¶ 47 (“Whenever one of his direct rights is infringed, the shareholder has an independent right of action.”). The United States notes that some authors have asserted or proposed exceptions to this rule.

determinative is whether the right that has been infringed belongs to the shareholder or the corporation.

8. Examples of claims that would allow a shareholding investor to seek direct loss or damage include where the investor alleges that it was denied its right to a declared dividend, to vote its shares, or to share in the residual assets of the enterprise upon dissolution.¹² Another example of a direct loss or damage suffered by shareholders is where the disputing State wrongfully expropriates the shareholders' ownership interests – whether directly through an expropriation of the shares or indirectly by expropriating the enterprise as a whole.¹³

9. The second principle of customary international law against which Articles 1116 and 1117 were drafted is that no international claim may be asserted against a State on behalf of the State's own nationals.¹⁴

10. Under these background principles, a common situation is left without a remedy under customary international law. Investors often choose to make an investment through a separate enterprise, such as a corporation, incorporated in the host State. If the host State were to injure that enterprise in a manner that does not directly injure the investor/shareholders, no remedy would ordinarily be available under customary international law. In such a case, the loss or damage is only directly suffered by the enterprise. As the investor has not suffered a direct loss or damage, it cannot bring an international claim. Nor may the enterprise maintain an international claim against the State of which it is a national under the principle of non-responsibility.¹⁵

11. Article 1117(1) addresses this issue by creating a right to present a claim not found in customary international law.¹⁶ Where the investment is an enterprise of another Party,¹⁷ an

¹² *Id.* In such cases, the Court in *Barcelona Traction* held that the shareholder (or the shareholder's State that has espoused the claim) may bring a claim under customary international law.

¹³ Under Article 1110, an expropriation may either be direct or indirect, and acts constituting an expropriation may occur under a variety of circumstances. Determining whether an expropriation has occurred therefore requires a case-specific and fact-based inquiry.

¹⁴ JENNINGS & WATTS, *OPPENHEIM'S INTERNATIONAL LAW* 512-13 (9th ed. 1992) (“[F]rom the time of the occurrence of the injury until the making of the award, the claim must continuously and without interruption have belonged to a person or series of persons (a) having the nationality of the state by whom it is put forward, and (b) not having the nationality of the state against whom it is put forward.”) (footnote omitted).

¹⁵ Some investment treaties allow an investment to assume the nationality of the investor that owns or controls that investment pursuant to ICSID Article 25(2)(b), therefore permitting an enterprise to bring a claim on its own behalf even though it was constituted under the laws of the disputing Party. *See, e.g.*, U.S.-Argentina Bilateral Investment Treaty, S. TREATY DOC. NO. 103-2, 103d Cong., 1st Sess., art. VIII(8) (1994) (“For purposes of an arbitration held under paragraph 3 of this Article, any company legally constituted under the applicable laws and regulations of a Party or a political subdivision thereof but that, immediately before the occurrence of the event or events giving rise to the dispute, was an investment of nationals or companies of the other Party, shall be treated as a national or company of such other Party in accordance with Article 25(2)(b) of the ICSID Convention.”); Energy Charter Treaty, art. 26(7), Apr. 16, 1998 (entry into force), 2080 U.N.T.S. 95; 34 I.L.M. 360 (1995).

¹⁶ *See* Daniel M. Price & P. Bryan Christy, III, *An Overview of the NAFTA Investment Chapter: Substantive Rules and Investor-State Dispute Settlement*, in *THE NORTH AMERICAN FREE TRADE AGREEMENT: A NEW FRONTIER IN INTERNATIONAL TRADE AND INVESTMENT IN THE AMERICAS* 165, 177 (Judith H. Bello et al. eds., 1994) (“Article

investor of a Party that owns or controls the enterprise may submit a claim on behalf of the enterprise for loss or damage incurred by the enterprise. However, minority shareholders who do not own or control the enterprise may not bring a claim for loss or damage under Article 1117, thereby reducing the risk of multiple actions with respect to the same disputed measures.

12. Article 1116, in contrast, adheres to the principle of customary international law that shareholders may assert claims only for *direct* injuries to their rights.¹⁸ Were shareholders to be permitted to claim under Article 1116 for indirect injury, Article 1117's limited carve out from customary international law would be superfluous. Moreover, it is well-recognized that an international agreement should not be held to have tacitly dispensed with an important principle of international law "in the absence of words making clear an intention to do so."¹⁹ Nothing in the text of Article 1116 suggests that the NAFTA Parties intended to derogate from customary international law restrictions on the assertion of shareholder claims.²⁰

13. Similarly, Article 1121(1)(b)'s reference to an investor's "interest in an enterprise" cannot be read to allow an investor to claim for indirect loss or damage for injuries suffered by the enterprise. In defining an "investment", Article 1139 uses the term "interest in an enterprise" to refer to legal entitlements or rights belonging to the investor (not the enterprise).²¹ For

1117 is intended to resolve the *Barcelona Traction* problem by permitting the investor to assert a claim for injury to its investment even where the investor itself does not suffer loss or damage independent from that of the injury to its investment.").

¹⁷ See NAFTA Article 1139 ("enterprise of a Party means an enterprise constituted or organized under the law of a Party, and a branch located in the territory of a Party and carrying out business activities there"); NAFTA Article 201 ("enterprise means any entity constituted or organized under applicable law, whether or not for profit, and whether privately-owned or governmentally-owned, including any corporation, trust, partnership, sole proprietorship, joint venture or other association").

¹⁸ Article 1116(1) derogates from customary international law only to the extent that it permits individual investors (including minority shareholders) to assert claims that could otherwise be asserted only by States. See, e.g., *Nottebohm (Liechtenstein v. Guatemala)*, 1955 I.C.J. 4, 24 (Judgment of Apr. 6) ("[B]y taking up the case of one of its subjects and by resorting to diplomatic action or international judicial proceedings on his behalf, a State is in reality asserting its own rights – its right to ensure, in the person of its subjects, respect for the rules of international law[.]") (internal quotation omitted); F.V. GARCÍA-AMADOR ET AL., RECENT CODIFICATION OF THE LAW OF STATE RESPONSIBILITY FOR INJURIES TO ALIENS 86 (1974) ("[I]nternational responsibility had been viewed as a strictly 'interstate' legal relationship. Whatever may be the nature of the imputed act or omission or of its consequences, the injured interest is in reality always vested in the State alone."); IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 585 (5th ed. 1998) ("[T]he assumption of the classical law that only states have procedural capacity is still dominant and affects the content of most treaties providing for the settlement of disputes which raise questions of state responsibility, in spite of the fact that frequently the claims presented are in respect of losses suffered by individuals and private corporations.").

¹⁹ *Elettronica Sicula S.p.A. (ELSI) (U.S. v. Italy)* 1989 I.C.J. 15, ¶ 50 (Judgment of July 1989) ("Yet the Chamber finds itself unable to accept that an important principle of customary international law should be held to have been tacitly dispensed with [by an international agreement], in the absence of any words making clear an intention to do so."); *Loewen Group, Inc. v. United States of America*, NAFTA/ICSID Case No. ARB(AF)/98/3, Award ¶ 160 (June 26, 2003); see also *id.* ¶ 162 ("It would be strange indeed if sub silentio the international rule were to be swept away.").

²⁰ As noted earlier, the United States expressly drew a distinction between direct and indirect injury in its Statement of Administrative Action. See n.2, *supra*.

²¹ See Article 1139 (excluding from the term "investment" claims to money "that do not involve the kinds of interests set out in subparagraphs (a) through (h)").

example, Article 1139(e) includes within the definition of “investment” “an interest in an enterprise that entitles the owner to share in income or profits of the enterprise,” while Article 1139(f) includes within this definition “an interest in an enterprise that entitles the owner to share in the assets of that enterprise on dissolution.” Thus, such “interest in an enterprise” under Article 1121(1)(b) contemplates the kinds of *direct* loss or damage sustained by a shareholder mentioned above.

14. The approach taken by other tribunals allowing shareholders to claim indirect loss is inapposite in the context of the NAFTA, as those cases typically involved investment treaties that do not address the limitations of shareholder claims under customary international law and reference “shares” only in the context of the definition of an investment.²² NAFTA, in contrast, creates an explicit regime, which must be treated as *lex specialis*.²³

15. The above conclusions on the distinction between Articles 1116(1) and 1117(1) are reinforced in several complementary NAFTA provisions, all of which serve to recognize relevant principles of domestic law²⁴ aimed at preserving the separate legal identity of a corporation,²⁵ promoting judicial economy,²⁶ and protecting the rights of creditors and other shareholders.²⁷

²² See, e.g., *Impregilo S.p.A. v. Argentina*, ICSID Case No. ARB/07/17, Award ¶ 138 (June 21, 2011); *Venezuela Holdings B.V., et al. v. Venezuela*, ICSID Case No. ARB/07/27, Decision on Jurisdiction ¶ 165 (June 10, 2010); *Suez, Sociedad General de Aguas de Barcelona S.A. and Interagua Servicios Integrados de Agua S.A. v. Argentina*, ICSID Case No. ARB/03/17, Decision on Jurisdiction ¶ 49 (May 16, 2006); *Yury Bogdanov v. Republic of Moldova*, SSC Case No. V (114/2009), Final Arbitral Award ¶¶ 67-68 (Mar. 30, 2010). See also David Gaukrodger, “Investment Treaties as Corporate Law: Shareholder Claims and Issues of Consistency,” OECD Working Papers on International Investment, 2013/03, at 25-27 (2013) (“Gaukrodger (2103)”).

²³ See ZACHARY DOUGLAS, *THE INTERNATIONAL LAW OF INVESTMENT CLAIMS* 446 (2009) (“DOUGLAS”) (“Articles 1116 and 1117 of NAFTA create a sophisticated mechanism for dealing, *inter alia*, with shareholder actions.”); Gaukrodger (2013), at 52 (“NAFTA contains a significantly more developed system for shareholder claims than most investment treaties.”).

²⁴ See, e.g., *Barcelona Traction* ¶ 50 (“If the Court were to decide the case in disregard of the relevant institutions of municipal law it would, without justification, invite serious legal difficulties. It would lose touch with reality, for there are no corresponding institutions of international law to which the Court could resort. Thus the Court has . . . not only to take cognizance of municipal law but also to refer to it.”).

²⁵ See, e.g., *Bolivar v. Pocklington*, 975 F.2d 28, 33 (1st Cir. 1992) (“a sole shareholder cannot commandeer corporation assets by discarding the corporate veil at his convenience”). See generally David Gaukrodger, “Investment Treaties and Shareholder Claims for Reflective Loss: Insights from Advanced Systems of Corporate Law,” OECD Working Papers on International Investment, 2014/02, at 13-25 (2014) (discussing the impact that shareholder claims for indirect loss may have on corporate identity).

²⁶ See, e.g., *Johnson v. Gore Wood & Co.* [2002] 2 AC 1, 62 (House of Lords) (“If the shareholder is allowed to recover in respect of [indirect] loss, then either there will be double recovery at the expense of the defendant or the shareholder will recover at the expense of the company and its creditors and other shareholders. Neither course can be permitted. This is a matter of principle; there is no discretion involved. . . . Justice to the defendant requires the exclusion of one claim or the other; protection of the interests of the company’s creditors requires that it is the company which is allowed to recover to the exclusion of the shareholder.”); *Gaubert v. United States*, 885 F.2d 1284, 1291 (5th Cir. 1989) (“One rationale behind this prohibition [on indirect loss] rests on principles of judicial economy.”), *reversed on other grounds*, 499 U.S. 315 (1991).

²⁷ See, e.g., *Gaubert*, 885 F.2d at 1291 (“Another rationale for the prohibition [on shareholder claims for indirect loss] is fairness to creditors of the corporation. Common shareholders are usually at or near the bottom of the corporate financial pecking order. First come the secured then unsecured creditors, then the bondholders in order of preference, then the preferred shareholders, and lastly the common shareholders. Any recovery for injuries to the

16. For example, Article 1117(3) provides that claims brought on behalf of an investor under Article 1116(1) and an enterprise under Article 1117(1) that arise from the same events should be heard together by the same arbitral tribunal.²⁸ This provision promotes judicial economy by providing for the consolidation of claims, thereby reducing the risk of double recovery and inconsistent awards when the claims are based on the same events. Article 1117(3) also makes clear that nothing prevents an investor that owns or controls an enterprise, in an appropriate case, from submitting claims under both Articles 1116 and 1117.²⁹ This allowance would be unnecessary if the controlling investor could claim for indirect loss under Article 1116(1).

17. Article 1117(4) is aimed at further reducing the possibility of multiple actions by preventing the investment, which includes an enterprise under NAFTA Article 1139, from bringing a claim on its own behalf.³⁰

18. Articles 1121(1)(b) and 1121(2)(b) also reinforce the distinction between Articles 1116 and 1117, respectively, in order to reduce the likelihood of multiple actions and double recovery.³¹ Regardless of whether an investor submits a claim for injury to its own interest under Article 1116, or to the interest of an enterprise that the investor owns or controls under

corporation is paid into the corporation, and the various creditors, bondholders, and equity-holders are ‘paid’ in that order. Were common shareholders allowed to sue directly and individually for damages to the value of their shares, we would be allowing them to bypass the corporate structure and effectively preference themselves at the expense of the other persons with a superior financial interest in the corporation.”); Caplan & Sharpe, at 826 (noting that with respect art. 24(1)(b) of the U.S. Model BIT, substantively identical to NAFTA Article 1117(1), that the provision maintains the “distinction between the rights of shareholders and the corporation [and] prevents investors from effectively stripping away a corporate asset . . . to the detriment of others with a legitimate interest in that asset, such as the enterprise’s creditors”) (internal citation omitted).

²⁸ Article 1117(3) reads in full: “Where an investor makes a claim under this Article and the investor or a non-controlling investor in the enterprise makes a claim under Article 1116 arising out of the same events that gave rise to the claim under this Article, and two or more of the claims are submitted to arbitration under Article 1120, the claims should be heard together by a Tribunal established under Article 1126, unless the Tribunal finds that the interest of a disputing party would be prejudiced thereby.”

²⁹ For example, if a NAFTA Party violated Article 1109(1)’s requirement that “all transfers relating to an investment of an investor of another Party in the territory of the Party to be made freely and without delay,” the investor might be able to claim under Article 1116 damages stemming from interference with its right to be paid corporate dividends. If the investor owns or controls the enterprise, it might also be able to claim under Article 1117 damages relating to its enterprise’s inability to make payments necessary for the day-to-day conduct of the enterprise’s operations. A minority or non-controlling shareholder under such a scenario, however, could submit only a claim for direct damages – the loss of dividends – under Article 1116.

³⁰ See MEG N. KINNEAR, ANDREA K. BJORKLUND & JOHN F.G. HANNAFORD, INVESTMENT DISPUTES UNDER THE NAFTA: AN ANNOTATED GUIDE TO NAFTA CHAPTER 11, at 1117-4 (2008 Supp.) (“KINNEAR”) (“[Article 1117(4)] is likely . . . designed to forestall the possibility that the investment could make one claim while its controlling owner advanced a different claim. The rule of non-responsibility should prohibit that result, in any event, but given the different approach taken in the ICSID Convention [under Article 25(2)(b)], the provision provides extra guidance to tribunals as to the route an Article 1117 claim should take.”).

³¹ See, e.g., *GAMI Investments, Inc. v. United Mexican States*, NAFTA/UNCITRAL, Final Award ¶¶ 116-121 (Nov. 15, 2004) (“*GAMI* Final Award”) (finding that “[t]he overwhelming *implausibility* of a simultaneous resolution of the problem [of double recovery] by national and international jurisdictions impels consideration of the practically *certain* scenario of unsynchronized resolution”) (emphasis in original).

Article 1117, the enterprise must waive its right to seek available remedies under domestic law for the same injury. Otherwise, a NAFTA Party could be forced to defend against such claims in concurrent or consecutive proceedings, risking duplicative and potentially inconsistent decisions for the same loss or damage arising from the same breach.

19. Finally, under Article 1135(2)(a) and (b), where a claim is made under Article 1117(1), the award must provide that any restitution be made, or monetary damages be paid, to the enterprise. This requirement – which follows the practice of many domestic legal systems with respect to shareholder derivative actions³² – is aimed at preventing the investor from effectively stripping away a corporate asset (the claim) to the detriment of others with a legitimate interest in that asset, such as the enterprise’s creditors.³³ Instead, any award in the claimant’s favor will make the enterprise whole and the value of the shares and assets will be restored. This goal is reflected in Article 1135(2)(c), which provides that where a claim is made under Article 1117(1), the award must provide that it is made without prejudice to any person’s right (under applicable domestic law) in the relief.

20. Allowing an investor to claim for any indirect loss under Article 1116(1) would render the above framework ineffective.³⁴ For example, if an investor had the right to bring its own claim for loss or damage suffered by an enterprise, that investor might choose to make a claim under Article 1116(1) rather than Article 1117(1) in order to protect the award from creditors or other shareholders.³⁵ Under such circumstances, the provisions of Article 1135 – designed to ensure any award based on injury to an enterprise is paid to the enterprise in order to protect the interests of creditors and other shareholders – would be rendered meaningless.³⁶

³² See Gaukrodger (2013), at 19-20.

³³ Indeed, international tribunals have rejected shareholder claims in part because of the difficulty in determining what relief can fairly be granted in light of potential claims by creditors and other interested parties. See, e.g., Eduardo Jiménez de Aréchaga, *Diplomatic Protection of Shareholders in International Law*, 4 PHIL. INT’L L.J. 71, 77, 78 (1965).

³⁴ It is well-established under customary international law that provisions of a treaty must be interpreted in such a manner that renders their terms effective. See *Territorial Dispute (Libya v. Chad)*, 1994 I.C.J. 6, ¶ 51 (Judgment of Feb. 3) (rejecting construction that was “contrary to one of the fundamental principles of interpretation of treaties, consistently upheld by international jurisprudence, namely that of effectiveness”) (collecting authorities); *accord Corfu Channel (United Kingdom v. Albania)*, 1949 I.C.J. 4, 24 (Judgment of Apr. 9) (“It would indeed be incompatible with the generally accepted rules of interpretation to admit that a provision of this sort occurring in a special agreement should be devoid of purport or effect.”).

³⁵ See DOUGLAS, at 452 (“It is difficult to imagine why a shareholder would elect to bring a claim for the account of its company if it had the option of bypassing the company altogether. The company might be liable to pay creditors, local taxes and discharge other obligations before distributing the residual amount of any damages recovered to the shareholders.”).

³⁶ See, e.g., *Marvin Feldman v. United Mexican States*, NAFTA/ICSID Case No. ARB(AF)/99/1, Correction and Interpretation of the Award ¶¶ 12-13 (June 13, 2003) (revising the award to comply with the requirement of Article 1135(2) that damages under Article 1117 be paid to the enterprise). Allowing an investor to bring a claim for indirect loss under Article 1116 would also permit a class of claims (by minority shareholders and creditors, which do not own or control the enterprise at issue) never envisioned by the NAFTA Parties. In such a case, Article 1121(1)(b) would not prevent the enterprise from also seeking available remedies under domestic law for the same injury. Nor would Article 1117(3) require the consolidation of these investors’ claims. As a result, there would be an increased risk of forum shopping, multiple actions, double recovery and inconsistent awards.

21. Against this backdrop, no NAFTA tribunal that has considered the distinction between Article 1116 and 1117 has ever awarded damages for indirect loss under Article 1116.³⁷ Rather, two NAFTA tribunals that have considered the implications of allowing for indirect loss under Article 1116 instead recognized the importance of the distinction between Article 1116 and 1117 and the policies that this distinction is intended to promote.³⁸ In *Mondev*, the tribunal found that “[h]aving regard to the distinctions drawn between claims brought under Articles 1116 and 1117, a NAFTA tribunal should be careful not to allow any recovery, in a claim that should have been brought under Article 1117, to be paid directly to the investor.”³⁹ It further cautioned future claimants to “consider carefully whether to bring proceedings under Articles 1116 and 1117, either concurrently or in the alternative, and that they fully comply with the procedural requirements under Articles 1117 and 1121 if they are suing on behalf of an enterprise.”⁴⁰ In *GAMI*, the tribunal, in addressing the claimant’s expropriation claim under Article 1116, considered at length “difficulties attributable to the derivative nature” of the claim, including the dangers of inconsistent judgments and double recovery.⁴¹

22. A tribunal cannot simply overlook an investor’s error in claiming indirect losses under Article 1116(1). Under Article 1122, the scope of a NAFTA Party’s consent to arbitrate an investment dispute is conditioned on compliance with the procedural requirements of Chapter Eleven. Those procedures include, *inter alia*, the requirements of Articles 1116.⁴² The disputing Party’s consent is limited to a claim for loss or damage available under the specific article(s) pled – NAFTA Article 1116(1) or Article 1117(1) or both – and an investor’s recovery of loss or

³⁷ While the tribunals in *Pope & Talbot* and *S.D. Myers* found the disputing Party liable for breaches of the NAFTA, the tribunals awarded damages only for losses suffered directly by the investor bringing the claim, and not by the investment/enterprise. In *Pope & Talbot*, the damages found by the tribunal consisted of the investor’s out of pocket expenses (accountants’ fees, legal fees and lobbying fees). See *Pope & Talbot, Inc. v. Government of Canada*, NAFTA/UNCITRAL, Award in Respect of Damages ¶ 85 (May 31, 2002) (“*Pope & Talbot* Damage Award”). In *S.D. Myers*, the tribunal awarded the claimant damages only for its lost/delayed income stream from the PCB inventory it could have reasonably expected to import into the United States and process at its U.S. facilities. See *S.D. Myers, Inc. v. Government of Canada*, NAFTA/UNCITRAL, Second Partial Award ¶¶ 222-228 (Oct. 21, 2002) (“*S.D. Myers* Second Partial Award”).

³⁸ See KINNEAR, at 1116-7 (noting generally, however, that NAFTA tribunals have not adequately considered policy questions with respect to double recovery and the preservation of basic corporate structure). See also Gaukrodger (2013), at 8 (“ISDS tribunals have given limited consideration to policy aspects and the consequences of allowing shareholder claims for reflective loss.”).

³⁹ *Mondev International Ltd. v. United States of America*, NAFTA/ICSID Case No. ARB(AF)/99/02, Award ¶ 86 (Oct. 11, 2002). The tribunal specifically noted that paying damages to the enterprise could make a difference in terms of claims by third parties with security interests or other rights, as well as tax treatment of those damages. *Id.* ¶ 84.

⁴⁰ *Id.* ¶ 86.

⁴¹ *GAMI* Final Award ¶¶ 116-121.

⁴² *Methanex Corp. v. United States of America*, NAFTA/UNCITRAL, First Partial Award ¶ 120 (Aug. 7, 2002) (“In order to establish the necessary consent to arbitration, it is sufficient to show (i) that Chapter 11 applies in the first place, i.e. that the requirements of Article 1101 are met, and (ii) that a claim has been brought by a claimant investor in accordance with Articles 1116 or 1117 (and that all pre-conditions and formalities required under Articles 1118-1121 are satisfied). Where these requirements are met by a claimant, Article 1122 is satisfied; and the NAFTA Party’s consent to arbitration is established.”).

damage must accordingly be limited to that available under the specific article(s). In addition, how an investor pleads a claim for loss or damage (*i.e.*, under which article) can have implications on a disputing Party's litigation strategy. For example, whether a claim for loss or damage has been brought pursuant to Article 1116 or 1117 can impact a disputing Party's ability to assess the potential scope of claimed damages both with respect to any settlement negotiations regarding the dispute and with respect to its defense against such claims. Indeed, the difference in the scope of damages available to an investor under Article 1116 and to the investor's enterprise under Article 1117 can be quite substantial.

Causation under Articles 1116 and 1117

23. Articles 1116 and 1117 allow an investor to recover loss or damage incurred "by reason of, or arising out of" a breach of an obligation under NAFTA Chapter Eleven, Section A.

24. The ordinary meaning of these terms requires an investor to establish the causal nexus between the alleged breach and the claimed loss or damage.⁴³ In this connection, it is well-established that "causality in fact is a necessary but not a sufficient condition for reparation."⁴⁴ The standard for factual causation is known as the "but-for" or "*sine qua non*" test whereby an act causes an outcome if the outcome would not have occurred in the absence of the act. This test is not met if the same result would have occurred had the breaching State acted in compliance with its obligations.⁴⁵ As the International Court of Justice found in the *Bosnian Genocide Case*:

The question is whether there is a sufficiently direct and certain causal nexus between the wrongful act, the Respondent's breach of the obligation to prevent genocide, and the injury suffered by the Applicant, consisting of all damage of any type, material or moral, caused by the acts of genocide. Such a nexus could be considered established only if the Court were able to conclude from the case as a whole and with a sufficient degree of certainty that the genocide at Srebrenica

⁴³ H.L.A. HART & TONY HONORÉ, CAUSATION IN THE LAW 422 (2d ed. 1985) (noting that it is generally the claimant's burden to "persuade the tribunal of fact of the existence of causal connection between wrongful act and harm"); see also *Islamic Republic of Iran v. United States of America*, AWD 601-A3/A8/A9/A14/B/61-FT ¶ 153 (July 17, 2009), 38 Iran-U.S. C.T.R. 197, 223 ("Iran, as the Claimant, is required to prove that it has suffered losses . . . and that such losses were *caused by* the United States") (emphasis added).

⁴⁴ International Law Commission, Draft Articles on Responsibility of States for Internationally Wrongful Acts, With Commentaries, art. 31, comment 10 (2001) ("ILC Draft Articles"). The Iran-U.S. Claims Tribunal reaffirmed this principle in the remedies phase of Case A/15(IV) when it held that it must determine whether the "United States breach caused 'factually' the harm and that that loss was also a 'proximate' consequence of the United States' breach." *Islamic Republic of Iran v. United States of America*, AWD 602-A15(IV)/A24-FT ¶ 52 (July 2, 2014) ("A/15(IV) Award").

⁴⁵ A/15(IV) Award ¶ 52 ("[I]f one were to reach the conclusion that both tortious (or obligation-breaching) and non-tortious (obligation-compliant) conduct of the same person would have led to the same result, one might question that the tortious (or obligation-breaching) conduct was *condicio sine qua non* of the loss the claimant seeks to recover.").

would in fact have been averted if the Respondent had acted in compliance with its legal obligations. However, the Court clearly cannot do so.⁴⁶

25. The ordinary meaning of the term “by reason of, or arising out of” also requires an investor to demonstrate proximate causation. All three NAFTA Parties agree.⁴⁷ Indeed, proximate causation is an “applicable rule[] of international law” that under Article 1131(1) must be taken into account in fixing the appropriate amount of monetary damages.⁴⁸ Articles 1116 and 1117 contain no indication that the NAFTA Parties intended to vary from this established rule.⁴⁹

26. NAFTA tribunals have consistently imposed a requirement of proximate causation under Articles 1116 and 1117. The *S.D. Myers* tribunal held that damages may only be awarded to the extent that there is a “sufficient causal link” between the breach of a specific NAFTA provision and the loss sustained by the investor,⁵⁰ and then subsequently clarified that “[o]ther ways of expressing the same concept might be that the harm must not be too remote, or that the breach of the specific NAFTA provision must be the *proximate* cause of the harm.”⁵¹ In *Pope & Talbot*, the tribunal held that under Article 1116 the claimant bears the burden to “prove that loss or damage was caused to its interest, and that it was causally connected to the breach complained of.”⁵² The *ADM* tribunal required “a sufficiently clear direct link between the wrongful act and the alleged injury, in order to trigger the obligation to compensate for such an injury.”⁵³

⁴⁶ *Application of the Convention on the Prevention and Punishment of the Crime of Genocide (Bosnia and Herzegovina v. Serbia and Montenegro)*, 2007 I.C.J. 40, ¶ 462 (Judgment of Feb. 26).

⁴⁷ See, e.g., *Methanex Corp. v. United States of America*, NAFTA/UNCITRAL, Fourth Submission of the United Mexican States ¶ 2 (Jan. 30, 2004) (“Mexico agrees . . . that Chapter Eleven incorporates a standard of proximate cause through the use of the phrase ‘has incurred loss or damage by reason of, or arising out of’ a Party’s breach of one of the NAFTA provisions listed in Articles 1116 and 1117.”) (footnote omitted); *Methanex Corp. v. United States of America*, NAFTA/UNCITRAL, Second Submission of Canada Pursuant to NAFTA Article 1128, ¶ 47 (Apr. 30, 2001) (“The ordinary meaning of the words ‘by reason of, or arising out of’ establishes that there must be a clear and direct nexus between the breach and the loss or damage incurred.”).

⁴⁸ See ILC Draft Articles, art. 31, comment 10. See also *Administrative Decision No. II (U.S. v. Germany)*, 7 R.I.A.A. 23, 29 (1923) (proximate cause is “a rule of general application both in private and public law – which clearly the parties to the Treaty had no intention of abrogating”); *United States Steel Products (U.S. v. Germany)*, 7 R.I.A.A. 44, 54-55, 58-59, 62-63 (1923) (rejecting on proximate cause grounds a group of claims seeking reimbursement for war-risk insurance premiums); *Dix (U.S. v. Venezuela)*, 9 R.I.A.A. 119, 121 (undated) (“International as well as municipal law denies compensation for remote consequences, in the absence of evidence of deliberate intention to injure.”); *H. G. Venable (U.S. v. Mexico)*, 4 R.I.A.A. 219, 225 (1927) (construing the phrase “originating from” as requiring that “only those damages can be considered as losses or damages caused by [the official] which are immediate and direct results of his [action]”). See also BIN CHENG, GENERAL PRINCIPLES OF LAW 244-45 (1953) (“it is ‘a rule of general application both in private and public law,’ equally applicable in the international legal order, that the relation of cause and effect operative in the field of reparation is that of proximate causality in legal contemplation”).

⁴⁹ See n.19, *supra*.

⁵⁰ *S.D. Myers, Inc. v. Government of Canada*, NAFTA/UNCITRAL, First Partial Award ¶ 316 (Nov. 13, 2000).

⁵¹ *S.D. Myers* Second Partial Award ¶ 140.

⁵² *Pope & Talbot* Damage Award ¶ 80.

⁵³ *Archer Daniels Midland Co. v. United Mexican States*, NAFTA/ICSID Case No. ARB(AF)/04/05, Award ¶ 282 (Nov. 21, 2007).

27. Accordingly, any loss or damage cannot be based on an assessment of acts, events or circumstances not attributable to the alleged breach.⁵⁴ Events that develop subsequent to the alleged breach may increase or decrease the amount of damages suffered by a claimant. At the same time, injuries that are not sufficiently “direct”, “foreseeable”, or “proximate” may not, consistent with applicable rules of international law, be considered when calculating a damage award.⁵⁵ Valuing damages as of the date of an award, rather than as of the time of breach, could fail to appropriately exclude injuries resulting from events subsequent to the date of breach that lack sufficient causal connection to the breach.⁵⁶ Tribunals should exercise caution also because compensation for such injuries may, depending on the circumstances, also be construed as intending to deter or punish the conduct of the disputing State, contrary to Article 1135(3).⁵⁷

Restrictions on Parallel Proceedings under Article 1121

28. The relevance or applicability of domestic judicial review of a challenged measure should be considered both in the context of the claim made and NAFTA Article 1121.

29. Article 1121(1)(b) allows an investor to choose to take its claim to arbitration rather than to the courts of the NAFTA Party that allegedly breached its NAFTA obligations.⁵⁸ Once an investor has chosen this option, Article 1121(1)(b) requires a waiver of a claimant’s “right to initiate or continue . . . any proceedings *with respect to* the measure of the disputing Party that is alleged to be a breach referred to in Article 1116[.]”⁵⁹ As the United States has previously explained, the phrase “with respect to” in Article 1121(1)(b) should be interpreted broadly.⁶⁰

⁵⁴ See ILC Draft Articles, art. 31, comment 9 (noting that the language of Article 31(2) providing that injury includes damage “caused by the internationally wrongful act of a State,” “is used to make clear that the subject matter of reparation is, globally, the injury *resulting from and ascribable to the wrongful act, rather than any and all consequences flowing from an internationally wrongful act.*”) (emphasis added).

⁵⁵ As the commentary to the ILC Draft Articles explains, causality in fact is a necessary but not sufficient condition for reparation: “There is a further element, associated with the exclusion of injury that is too “remote” or “consequential” to be the subject of reparation. In some cases, the criterion of “directness” may be used, in others “foreseeability” or “proximity”. . . . The notion of a sufficient causal link which is not too remote is embodied in the general requirement in article 31 that the injury should be in consequence of the wrongful act[.]” ILC Draft Articles, art. 31, comment 10 (footnotes omitted).

⁵⁶ See, e.g., *Murphy Exploration & Production Co. v. Republic of Ecuador*, UNCITRAL, Partial Final Award ¶¶ 482-485 (May 6, 2016); *Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica*, ICSID Case No. ARB/96/1, Final Award ¶¶ 83-84 (Feb. 17, 2000).

⁵⁷ Article 1135(3) expressly provides that “[a] Tribunal may not order a Party to pay punitive damages.” See also ILC Draft Articles, art. 36, comment 4 (“[A]rticle 36 is purely compensatory, as its title indicates. . . . It is not concerned to punish the responsible State, nor does compensation have an expressive or exemplary character.”) (citing the *Velásquez Rodríguez*, Compensatory Damages case, where “the Inter-American Court of Human Rights held that international law did not recognize the concept of punitive or exemplary damages (Series C, No. 7 (1989))”).

⁵⁸ See U.S. Statement of Administrative Action (Under Chapter Eleven, “if a U.S. firm incurs loss or damage due to the failure of a NAFTA party to honor its NAFTA obligations regarding investments, it may take its claim to arbitration, rather than to the courts of that country.”).

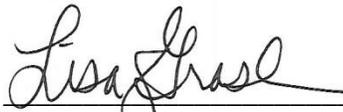
⁵⁹ NAFTA art. 1121(1)(b) (emphasis added).

⁶⁰ *Detroit International Bridge Company v. Government of Canada*, Submission of the United States of America ¶ 6 (Feb. 14, 2014) (citing *Consolidated Softwood Lumber Proceedings*, NAFTA/UNCITRAL, Reply Post-Hearing Submission of Respondent United States of America, at n.2 (Mar. 10, 2006); *Canfor v. United States of America*,

This construction of the phrase is consistent with the purpose of this waiver provision: to avoid the need for a respondent to litigate concurrent and overlapping proceedings in multiple forums, and to minimize not only the risk of double recovery, but also the risk of “conflicting outcomes (and thus legal uncertainty).”⁶¹ As the tribunal in *Commerce Group* observed, the waiver provision permits other concurrent or parallel domestic proceedings where claims relating to different measures at issue in such proceedings are “separate and distinct” and the measures can be “teased apart.”⁶²

30. Article 1121(1)(b) includes an exception to the waiver requirement for “proceedings for injunctive, declaratory or other extraordinary relief, not involving the payment of damages, before an administrative tribunal or court under the law of the disputing Party.” The purpose of this exception is to allow a claimant to initiate or continue certain proceedings to preserve its rights during the pendency of the arbitration, in a manner consistent with the broader purposes of the waiver requirement, as set forth in the preceding paragraph.

Respectfully submitted,



Lisa J. Grosh

Assistant Legal Adviser

John D. Daley

Deputy Assistant Legal Adviser

Nicole C. Thornton

Chief of Investment Arbitration

Matthew L. Olmsted

Attorney Adviser

*Office of International Claims and
Investment Disputes*

UNITED STATES DEPARTMENT OF STATE

Washington, D.C. 20520

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NAFTA/UNCITRAL, Reply on Jurisdiction of Respondent United States of America, at n.12 (Aug. 6, 2004)); accord *Consolidated Softwood Lumber Proceedings*, NAFTA/UNCITRAL, Decision on Preliminary Question ¶ 201 (June 6, 2006) (“[T]he Tribunal is of the view that the words ‘with respect to’ are to be interpreted broadly.”).

⁶¹ *International Thunderbird Gaming Corp. v. United Mexican States*, NAFTA/UNCITRAL, Award ¶ 118 (Jan. 26, 2006) (“In construing Article 1121 of the NAFTA, one must also take into account the rationale and purpose of that article. The consent and waiver requirements set forth in Article 1121 serve a specific purpose, namely to prevent a party from pursuing concurrent domestic and international remedies, which could either give rise to conflicting outcomes (and thus legal uncertainty) or lead to double redress for the same conduct or measure.”).

⁶² *Commerce Group Corp. and San Sebastian Mines, Inc. v. El Salvador*, CAFTA-DR/ICSID Case No. ARB/09/17, Award ¶ 111-112 (Mar. 14, 2011) (holding that the waiver barred the claimant from pursuing a claim in a domestic proceeding that was “part and parcel” of its claim in a pending CAFTA-DR arbitration, because the measures subject to the claims in the respective proceedings could not be “teased apart”). Article 1121 does not require a waiver of domestic proceedings where the measure at issue in the NAFTA arbitration is, for example, only tangentially or incidentally related to the measure at issue in those domestic proceedings.