Public Version

INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

Koch Industries, Inc. and Koch Supply & Trading, LP

v.

Government of Canada

(ICSID Case No. ARB/20/52)

GOVERNMENT OF CANADA

COUNTER-MEMORIAL ON JURISDICTION AND THE MERITS

17 February 2022

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I. INTRODUCTION 1

II. FACTUAL BACKGROUND 3

A. Ontario Adopts a Cap and Trade Program for Carbon Emissions Abatement 3

1. Regional Governments Form the Western Climate Initiative (WCI) 3
2. Ontario Develops a Cap and Trade Program Based on the WCI Model 4
3. Ontario Launches its Program and Holds Auctions in 2017 14
4. KS&T Participates in the Ontario Program in 2017 16
5. Ontario Harmonizes its Cap and Trade Program 17
6. KS&T Transfers the Balance of its Ontario CITSS Account to California 19
7. Ontario Participates in Joint Auctions in 2018 19
8. KS&T Participates in the February 2018 Joint Auction and Transfers the Balance of its Ontario CITSS Account to California 21

B. Ontario's Cap and Trade Program Enters a Period of Uncertainty 22

1. The Progressive Conservative Party Campaigns on Cancelling Cap and Trade 22
2. Industry Experts Highlight the Cap and Trade Program's Uncertain Future 24
3. The May 2018 Auction Takes Place During the Election Campaign 25
4. KS&T Participates in the May 2018 Joint Auction 25
5. The Progressive Conservative Party Wins a Majority and Prepares for Its Swearing-in 26
6. Ontario Does Not Provide Notice of Participation in the August 2018 Joint Auction 26
7. California De-Links its CITSS Accounts from Ontario CITSS Accounts 27

C. Ontario Winds Down the Cap and Trade Program and Provides Compensation on a Principled Basis 28

1. Regulation 386/18 Comes into Force on July 3, 2018 28
2. The Government Introduces Bill 4 Before the Ontario Legislative Assembly 29
3. The *Cancellation Act* Comes into Force 31
4. KS&T Applies for Compensation Despite Its Ineligibility 37

III. THE CLAIMANTS HAVE FAILED TO ESTABLISH THE JURISDICTION OF THE TRIBUNAL 38

A. The Claimants Bear the Burden of Proving that the Tribunal Has Jurisdiction 39

B. The Claimants Must Establish Jurisdiction Under Both the ICSID Convention and NAFTA Chapter Eleven 40

C. The Claimants' Activities Do Not Constitute an "Investment" Within the Meaning of Article 25 of the ICSID Convention 42

1. The Claimants Have Not Made a Contribution of Money or Assets 42

2. The Claimants Have Not Met the "Certain Duration" Requirement 44

3. The Claimants Have Not Undertaken an Investment Risk 45

4. The Claimants Have Not Contributed to the Host State's Economic Development 46

D. The Claimants Do Not Hold Protected "Investments" Under Article 1101 and Article 1139 of the NAFTA 47

1. The Emission Allowances Held by KS&T Were Not "Property" Under NAFTA Article 1139(g) 49

2. KS&T Did Not Hold "Interests Arising from the Commitment of Capital or other Resources in the Territory of a Party to Economic Activity in Such Territory" Under NAFTA Article 1139(h) 56

3. Koch Industries Does Not Hold Protected "Investments" Under Article 1101 and Article 1139 61

E. Koch Industries Lacks Standing Under NAFTA Article 1116 Because It Has Not Pled Any Cognizable Loss or Damage 64

IV. THE CLAIMANTS HAVE FAILED TO ESTABLISH A VIOLATION OF NAFTA CHAPTER ELEVEN 65

A. The Claimants Have Not Established a Breach of Article 1105 65

1. Summary of Canada's Position 65

2. The Claimants' Overly Broad Interpretation of NAFTA Article 1105 Must be Rejected 67

3. The Claimants Have Failed to Establish a Violation of Article 1105 75

B. The Claimants Have Failed to Establish a Breach of Article 1110 82

1. Summary of Canada's Position 82

2. NAFTA Article 1110(1) Incorporates Customary International Law Rules on Expropriation 84

3. The Claimants' Expropriation Claim Fails Because There Was No "Investment" Capable of Expropriation 87

4. The Claimants Have Not Established That Ontario Expropriated Any of Their Alleged Property Rights 93

V. THE CLAIMANTS HAVE FAILED TO ESTABLISH THAT THEY ARE ENTITLED TO COMPENSATION....................110

A. The Claimants Have Failed to Prove that Ontario Caused the Loss They Claim in Relation to the Emission Allowances 112

B. The Claimants Fail to Prove Legal Causation for Each of their Claims....................116

1. The Claimants Have Failed to Establish Actual and Specific Loss Pursuant to the Alleged Breaches of the Minimum Standard of Treatment....................116

2. The Claimants Have Failed to Establish Actual and Specific Loss of their "Emissions Trading Business in Ontario"....................118

3. The Claimants Have Failed to Establish Actual and Specific Loss with Respect to KS&T's Related Party Contracts....................119

4. The Claimants Have Failed to Establish that They Are Entitled to Lobbying Costs....................119

C. Any Damages Awarded Must Be Diminished or Disallowed As a Result of the Claimants' Role in their Loss....................120

D. The Claimants' Request for Interest Must Be Rejected....................123

VI. REQUEST FOR RELIEF....................123

I. INTRODUCTION

1. In May 2018, the Claimant Koch Supply & Trading, LP (**KS&T**), a U.S. entity, bought emission allowances in Ontario for resale in California. In June 2018, California disallowed incoming transfers of emission allowances from Ontario, and KS&T was unable to resell them in California as it had planned. KS&T and its indirect parent, Koch Industries, Inc. (the **Claimants**), now come to this Tribunal seeking compensation.

2. There is no NAFTA case here. KS&T's cross-border purchase of emission allowances in Ontario for resale in the United States is not an investment in Canada. The emission allowances have none of the characteristics of an "investment" under Article 25 of the ICSID Convention, and they fall outside the scope of an "investment" protected under NAFTA Article 1101 and Article 1139.

3. Perhaps aware of these deficiencies, the Claimants attempt to characterize KS&T's purchases of emission allowances as a "business" in Ontario; they also rely on unrelated and unidentified "interests" of Koch Industries. This is a transparent attempt to create jurisdiction where none exists. KS&T has no subsidiary or personnel in Canada. KS&T's business development efforts, which were led from the United States and related to cross-border sales, are plainly not an investment in Canada. Koch Industries not only has no "investment" relevant to this dispute, but also lacks standing because it has not alleged any cognizable loss.

4. The Ontario legislation that created the emission allowances provided that "no compensation" would be payable and that "no expropriation" could result from changes to the cap and trade program. KS&T assumed these risks and purchased emission allowances in Ontario in 2017, wagering that Ontario would harmonize its cap and trade program with that of California. While Ontario did harmonize its program with California in early 2018, there was never any guarantee that this would remain the case. From January to April 2018, KS&T systematically transferred all of the allowances it had acquired in Ontario to California. When KS&T again bought allowances in Ontario in May 2018 (instead of in California, where it was also registered), there were clear indications that the future of the Ontario cap and trade program was uncertain.

5. In June 2018, Ontario voters elected a party that had made winding down the cap and trade program a central plank of its campaign platform over the preceding months. Once in power, the new

government proceeded with the orderly wind down of the cap and trade program. The government also adopted a compensation scheme that focused on participants whose *actual emissions* of GHGs were lower than their holdings of purchased emission allowances. Given the clear provisions of the legislation that had created the cap and trade program, the Claimants could not reasonably expect that Ontario would offer compensation to any and all participants in the event of a regulatory change. Ontario's rational, non-discriminatory, legitimate policy-based measures fall far short of internationally wrongful conduct.

6. The Claimants have failed to meet their tripartite burden to establish this Tribunal's jurisdiction, to show a violation of NAFTA Chapter Eleven, and to prove any compensable damages.

7. In **Part II** of this submission, Canada sets out the relevant factual background of this dispute, including Ontario's establishment of a cap and trade program, the harmonization of Ontario's program with those of other sub-national jurisdictions, the election of a new government, and the orderly wind-down of the cap and trade program. Canada corrects the Claimants' exaggerated view of the role of market participants in cap and trade programs generally and their misleading statements about KS&T's participation in the Ontario cap and trade program in particular.

8. In **Part III**, Canada explains why the Tribunal lacks jurisdiction to hear the dispute. The alleged investments do not meet the objective requirements of Article 25 of the ICSID Convention. In addition, the Tribunal lacks subject-matter jurisdiction under the NAFTA because the Claimants do not hold "investments" in Canada within the meaning of NAFTA Articles 1101 and 1139(a)-(h). The emission allowances are not "property" under Article 1139(g), nor did their purchase give rise to "interests" arising out of the commitment of capital or other resources within the meaning of Article 1139(h). Neither Claimant held relevant enterprises (or interests in enterprises) in Canada under Article 1139(a) or (e). The Tribunal also lacks personal jurisdiction over Koch Industries because it has not alleged a cognizable loss, as required by NAFTA Article 1116. Given the Claimants' failure to establish jurisdiction over their claim, the Tribunal's inquiry should end there.

9. Even if the Tribunal were to conclude it had jurisdiction over the claim, Ontario's actions did not constitute a breach of NAFTA Article 1105 (Minimum Standard of Treatment) or Article 1110 (Expropriation and Compensation), as demonstrated in **Part IV**. Ontario's measures with respect to

winding down its cap and trade program were neither manifestly arbitrary nor discriminatory, but were rather based on legitimate policy goals. Nor could Ontario's actions give rise to an expropriation because the emission allowances did not give rise to rights capable of expropriation and in any event Ontario's measures constituted a valid exercise of police powers.

10. Finally, with respect to damages, the Claimants seek to recover the purchase price of the emission allowances bought at the May 2018 auction. However, shown in **Part V**, the Claimants have failed to establish that Canada's actions caused the losses they seek to recover. Even assuming that such causation could be established, the Claimants contributed to their own losses, such that the full quantum they claim should not be compensable.

11. Canada's submission is accompanied by statements from two witnesses: Mr. Alexander Wood, Assistant Deputy Minister at Ontario's Ministry of the Environment, Conservation and Parks (**MECP**); and Ms. Nadia Ramlal, Senior Manager, Program Systems and Oversight at MECP. Canada also submits reports by two experts. Mr. Franz Litz was one of the architects of the cap and trade model on which Ontario's system was based; Professor Larissa Katz is a leading authority on property rights under Ontario law.

II. FACTUAL BACKGROUND

A. Ontario Adopts a Cap and Trade Program for Carbon Emissions Abatement

1. Regional Governments Form the Western Climate Initiative (WCI)

12. Climate change is a looming environmental catastrophe largely caused by human activity.[1] Burning fossil fuels releases greenhouse gases (**GHGs**) into the Earth's atmosphere and higher levels of GHGs trap solar energy, increasing air and water temperature and significantly affecting our global climate. Carbon dioxide (**CO_2**) is the most abundant GHG emitted by human activity.

13. Over the last 20 years, national, regional and international efforts proposed to put a "price on

[1] **R-1**, Government of Canada, "Causes of Climate Change", last updated 28 March 2019.

carbon" for each ton of CO_2 or equivalent GHG (**CO_2e**) emitted.[2] Carbon pricing is intended to incentivize producers and consumers to change their behaviours and use lower-carbon technologies. Carbon pricing can be implemented with a cap and trade system, a carbon tax, or a combination of the two.

14. In response to international initiatives such as the 2005 Kyoto Protocol, which encouraged using flexible market mechanisms to reduce emissions,[3] several U.S. states and Canadian provinces joined forces to address climate change on a regional scale. In July 2008, Ontario announced that it would join the Western Climate Initiative (**WCI**), a coalition of seven U.S. states and three Canadian provinces developing a regional cap and trade system to reduce GHG emissions.[4]

15. In a cap and trade program, the government sets an overall "cap" on GHG emissions in one or more sectors of the economy, and then issues "emission allowances", each one representing a limited authorization for a compliance entity to emit one tonne of GHGs. The total number of emission allowances issued in a year is equivalent to the cap on emissions set by the government for that year. Over time, the emissions cap decreases, as does the corresponding number of allowances available. The theory is that due to the increasingly limited availability of allowances, the cost of polluting should rise over time, thus incentivizing compliance entities to optimize their operations to reduce their GHG emissions.

2. Ontario Develops a Cap and Trade Program Based on the WCI Model

16. In 2008, the WCI partner jurisdictions engaged environmental and economic experts to design a model cap and trade program. The understanding was that the WCI partner jurisdictions would work together to develop the underlying policy, and each jurisdiction would then implement its own

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[2] **R-2**, United Nations Climate Change, "Frequently Asked Questions": "What is "CO2 equivalent"? "GHG emissions/removals can be expressed either in physical units (such as grams, tonnes, etc.) or in terms of CO2 equivalent (grams CO2 equivalent, tonnes CO2 equivalent, etc.)."

[3] **R-3**, United Nations Climate Change, "What is the Kyoto Protocol?", adopted December 1997 and ratified 16 February 2005.

[4] In February 2007 the governors of Arizona, California, New Mexico, Oregon and Washington signed a Memorandum of Understanding, *see* **R-4**, Western Regional Climate Action Initiative, 26 February 2007. The premiers and governors of British Columbia, Manitoba, Utah, Montana, Québec, and Ontario would later sign the MOU.

standalone system.[5]

17. The WCI partner jurisdictions reflected their collaboration in two key documents: the 2008 *Design Recommendations for the WCI Regional Cap and Trade Program* (**2008 WCI Recommendations**)[6] and the 2010 *Design for the WCI Regional Program* (**2010 WCI Design Document**).[7] Franz Litz, Canada's expert witness in this arbitration, was integral to producing these WCI documents and has extensive experience advising governments on designing and implementing cap and trade programs. Ontario participated in the WCI policy discussions but did not move forward with developing its own program until several years later.

18. In 2015, Ontario began the process of developing its own cap and trade program based on WCI principles. The core elements of the WCI system design were adopted and implemented into Ontario's domestic legislation on May 18, 2016, when Ontario enacted the *Climate Change Mitigation and Low-carbon Economy Act, 2016* (***Climate Change Act***).[8] The *Climate Change Act* was accompanied by the *Reporting Regulation*[9] and the *Cap and Trade Regulation*[10] (**Cap and Trade Regulation** or **Regulation 144/16**). The *Climate Change Act* had the dual purpose of reducing GHG emissions in the Province and enabling Ontario to coordinate its efforts with other sub-national jurisdictions.[11]

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[5] The WCI Partner Jurisdictions acknowledged and respected the particular objectives and legislative environments of each participating jurisdiction by emphasizing that, "each Partner jurisdiction is subject to its own legislative and administrative processes", *see* **C-15**, WCI, Design for the WCI Regional Program, 27 July 2010 ("2010 WCI Design Document"), p. DD-2, s. 1.3 and Design Summary, s. 12: "each jurisdiction maintains sovereignty in the administration of its program."

[6] **R-5**, WCI Design Recommendation for the WCI Regional Cap-and-Trade Program, 23 September 2008 ("2008 WCI Recommendations").

[7] **C-15**, 2010 WCI Design Document.

[8] **R-6**, *Climate Change Mitigation and Low-carbon Economy Act*, 2016, S.O. 2016, c. 7 ("*Climate Change Act*").

[9] **RS-48**, *Quantification, Reporting and Verification of Greenhouse Gas Emissions*, O. Reg. 143/16 ("Regulation 143/16").

[10] **R-7**, *The Cap and Trade Program*, O. Reg. 144/16 ("Regulation 144/16").

[11] **R-6**, *Climate Change Act*, s. 2(1) and preamble: "A key purpose of this Act is to establish a broad carbon price through a cap and trade program that will change the behaviour of everyone across the Province, including spurring low-carbon innovation. A cap and trade program in Ontario will allow Ontario to link to other regional cap and trade markets as part of the international, national and interprovincial responses to reduce greenhouse gas."

19. In their Memorial, the Claimants make misleading statements about Ontario's cap and trade program and KS&T's participation in that program as a market participant. Canada explains the key elements of Ontario's cap and trade program below.

a) The Emissions Cap and the Creation of Emission Allowances

20. An **emissions cap** is the maximum level of allowable pollution, measured in tons of CO_2e and established by the government for a specified economic sector. In setting the overall emissions cap the government must ensure that the cap is low enough to incentivize emitters to reduce their emissions, while also considering potential economic impacts on industry and consumers.[12]

21. Extensive emissions reporting from covered economic sectors helps to inform governments in setting their emissions cap. Ontario's approach to reporting was formulated in the 2008 WCI Recommendations and the 2010 WCI Design Document. Each WCI partner jurisdiction was required to conduct extensive reporting across industries prior to joining the program in order to determine the historic level of emissions and the reductions necessary to achieve the WCI goal of 15% reduction below 2005 levels of GHG emissions by 2020.[13] In Ontario, large industrial facilities had been required to submit annual reports quantifying their GHG emissions since 2009.[14]

22. Each ton of GHG emissions up to the maximum set by the emissions cap is represented by an **emission allowance**. An emission allowance is a "limited authorization to emit" one ton of CO_2e of GHGs.[15] As Mr. Litz explains in his expert report, emission allowances have a specific and limited

[12] Setting the emission cap such that it achieves a reduction in emissions without an excessive impact on the economy can be difficult. As Mr. Litz explains in his expert report, "nearly every cap and trade program to date has had periods of 'slack cap', where the emissions cap is too high to create a scarcity in allowances." **RER-2**, Expert Report of Franz Litz, 15 February 2022 ("Litz - Expert Report"), ¶ 34. Governments have often had to course-correct along the way. For example, in the first phase of the European Union's Emissions Trading System ("ETS"), allowance prices dropped precipitously as soon as it became clear that cap levels in many countries were far higher than their verified emissions. As a result, there were far more allowances available than were needed to cover emissions. The oversupply was largely due to a lack of quality emissions data at the time the caps were set, and the EU would work to improve the quality of emissions data, eventually creating a EU-wide emissions registry. The EU would also develop mechanisms for reducing allowance supply. Litz - Expert Report, ¶ 126.

[13] **R-5**, 2008 WCI Recommendations, s. 3.1; **C-15**, 2010 WCI Design Document, Design Summary, s. 1.

[14] **R-8**, *Environmental Protection Act* (Greenhouse Gas Emissions Reporting), O.Reg. 452/09, s. 5(1) and Table 2.

[15] *See* **C-15**, 2010 WCI Design Document", p. DD-3, s. 2.3: "Allowance. A type of compliance instrument that is a limited authorization by the program authority or a participating jurisdiction under the Partner jurisdiction's Cap-and-Trade

function in a cap and trade program: "to allow regulated pollution sources the flexibility to either reduce their emissions or surrender allowances to cover those emissions."[16] This goes to the ultimate objective of the program, which is to incentivize facilities to use lower-carbon technologies and reduce emissions in a cost effective manner.[17] Further, Mr. Litz notes that a key feature of allowances is that they "are tradable, so that allowances can get from entities that do not need them for compliance to those for whom allowances represent the lowest cost path to compliance."[18]

23. The "authorization to emit" is inherently limited. The 2010 WCI Design Document provides that "[t]he program authority or a participating Partner Jurisdiction shall retain the right to terminate or limit such authorization"[19] and that a "compliance instrument under the Partner Jurisdiction's Cap-and-Trade Program does not constitute a property right for any purpose."[20] As Mr. Litz explains, this is consistent with how emission allowances are defined and treated in other cap and trade programs such as the Regional Greenhouse Gas Initiative (**RGGI**).[21]

24. Emission allowances held by participants in the system are recorded in a purpose-built electronic tracking system administered by WCI, Inc., the Compliance Instrument Tracking System Service (**CITSS**, pronounced "kits").[22] Under the *Climate Change Act*, only registered participants

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Program to emit up to one metric ton in carbon dioxide equivalent (CO2e) of GHGs, subject to all applicable limitations contained in this detailed program design summary, that may be allocated by the program authority out of its annual allowance budget under section 5.1."

[16] **RER-2**, Litz - Expert Report, ¶ 49.

[17] **R-6**, *Climate Change Act*, s. 2(1) and preamble.

[18] **RER-2**, Litz - Expert Report, ¶ 49.

[19] **C-15**, 2010 WCI Design Document, p. DD-20, s. 4.4.6.

[20] **C-15**, 2010 WCI Design Document, p. DD-21, s. 4.4.7.

[21] The RGGI is the first mandatory Cap and Trade Program in the United States to limit carbon dioxide from the power sector. Eleven states currently participate in RGGI; Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, Vermont and Virginia. Pennsylvania is expected to join in 2022. The Model Rule governing the RGGI states that, "A CO_2 allowance under the CO_2 Budget Trading Program does not constitute a property right". *See*, **R-9**, The Regional Greenhouse Gas Initiative, "Model Rule", s. XX-1.5(c)(9).

[22] Allowances were associated with a given year, known as their "vintage", largely for tracking and compliance purposes. **RS-6**, Environmental Commissioner of Ontario ("ECO"), "Introduction to Cap and Trade in Ontario", Appendix A to the ECO's Greenhouse Gas Progress Report 2016" ("ECO: Introduction to Cap and Trade in Ontario"), November 2016, p. 14. To satisfy its compliance obligations in a given compliance period, participants could submit only "current vintage" emission allowances, i.e. emission allowances having a vintage year that is a year in a compliance period or an earlier year, but not "future vintage" emission allowances. **R-7**, Regulation 144/16, s. 13(1).

(discussed below) could "purchase, sell, trade or otherwise deal" in emission allowances.[23] Allowances were tradable among participants in the system, so that entities holding allowances that they did not need for compliance could sell them to entities needing additional allowances.[24]

25. If, at the end of a compliance period, a compliance entity did not have enough allowances to cover its reported GHG emissions, it would be required to surrender additional emission allowances in an amount equal to three times the shortfall. This was provided for in both the 2010 WCI Detailed Design[25] and Ontario's legislation.[26]

b) Compliance Entities and Compliance Obligations

26. Under Ontario's legislative regime, a **capped participant** was an entity that was subject to the Province-wide cap on GHG emissions. Capped participants are also referred to as **compliance entities** because they have compliance obligations under the *Climate Change Act*. The activities of capped participants are foundational to the purpose of a cap and trade program: the abatement of GHG emissions. The Claimant KS&T was not a capped participant.[27]

27. Capped participants could be either mandatory or voluntary participants.[28] **Mandatory participants** comprised facilities that undertook a prescribed GHG activity[29] and emitted at least 25,000 of CO_2e annually; natural gas distributors that deliver an amount of natural gas that, if consumed, would emit at least 25,000 tonnes of CO_2e a year; fuel suppliers that sell more than 200

[23] **R-6**, *Climate Change Act*, s. 21.

[24] **RER-2**, Litz - Expert Report, ¶¶ 49-50.

[25] **C-15**, 2010 WCI Design Document, p. DD-37, s. 7.2.5.4.

[26] **R-6**, *Climate Change Act*, ss. 14(1), 14(7)(2) and 14(8); **R-7**, Regulation 144/16, ss. 18-20.

[27] The Claimant Koch Industries was not a participant of any kind.

[28] **R-7**, Regulation 144/16, s. 1(1) definition of "capped participant".

[29] Adipic acid production; ammonia production; carbonate use; cement production; coal storage; copper and nickel production; electricity generation; ferroalloy production; general stationary combustion; glass production; HCFC-22 production and HFC-23 destruction; hydrogen production; indirect useful thermal energy use; iron and steel production; lead production; lime production; magnesium production; nitric acid production; operation of equipment for a transmission system or a distribution system (electricity); operation of equipment related to the transmission, storage and transportation of natural gas; petrochemical production; petroleum refining; phosphoric acid production; primary aluminum production; pulp and paper production; refinery fuel gas use; soda ash production; or zinc production. *See* **RS-48**, Regulation 143/16, s. 1(1) definition of "specified GHG activity" and Schedule 2.

litres of fuel per year; and electricity importers.[30] **Voluntary participants** consisted of owners or operators of facilities that undertook prescribed GHG activities that emitted between 10,000-25,000 tonnes of CO_2e a year and elected to submit to the regime.[31] As discussed below, Ontario's program also allowed for another category of participants in the system, market participants, that did not have compliance obligations.

28. A **compliance obligation** is the requirement for an entity to surrender sufficient compliance instruments[32] to cover verified GHG emissions during the compliance period. A **compliance period** is the time frame during which the capped participant's emissions are monitored and reported.[33]

29. Capped participants received both a holding account and a compliance account in CITSS. Market participants, which had no compliance obligations, received only a holding account.[34] The *Climate Change Act* required each compliance entity to submit emission allowances or credits to the Minister in an amount equal to the aggregate amount of all GHG emissions reported by that participant for a compliance period, or face a penalty as discussed above.[35]

c) Distribution of Allowances for Free or by Auction

30. After their creation by the government, emission allowances were distributed to participants either for free or by auction. During the first compliance period, Ontario distributed free allowances to large GHG emitters to ease the transition to cap and trade and lessen the burden on Ontario businesses.[36]

[30] **RS-48**, Regulation 143/16, s. 13.

[31] **R-7**, Regulation 144/16, ss. 29-31.1.

[32] Ontario's program provided for several types of "compliance instrument", including emission allowances and credits. **R-6**, *Climate Change Act*, ss. 1, 35. Emission allowances are the only type of compliance instrument at issue in this arbitration.

[33] **R-7**, Regulation 144/16, s. 3(2). The Regulation established January 1, 2017 to December 31, 2020 as the first compliance period.

[34] **R-7**, Regulation 144/16, s. 39(1).

[35] **R-6**, *Climate Change Act*, s. 14(1).

[36] **RS-6**, ECO: Introduction to Cap and Trade in Ontario, p. 22.

31. In addition to free distribution, emission allowances in Ontario's cap and trade program were distributed via highly regulated **auctions**, also referred to as "the primary market".[37] Auctions were held four times a year in order to "create[] regular market price signals."[38] Auctions would have a "reserve" or "floor" price, *i.e.* the lowest price at which any allowance could be sold, to address "an inadvertent over-allocation of allowances to the market and the risk of persistently low compliance costs."[39] Auctions were open to anyone with an account in CITSS who was able to meet pre-qualification financial assurance requirements.[40] To promote transparency and price discovery, the auction settlement price and the total number of purchased allowances were publicly disclosed after the auction.[41]

d) The Secondary Market

32. While free distribution and allowance auctions were the primary mechanisms for compliance entities to obtain allowances in the Ontario system, compliance entities could also purchase allowances from other registered participants in what is referred to as the **secondary market**. As Mr. Litz explains, the secondary market refers to the transactions that occur between buyers and sellers after the allowances have been auctioned or otherwise initially distributed by the government.[42]

33. In a cap and trade system like Ontario's, compliance entities can obtain allowances at quarterly auctions and do not need to seek them out on the secondary market. Indeed, as Mr. Litz notes, the secondary market tends to be less active in programs using auctions as compared to those without. This was the case for Ontario's cap and trade program, which saw only ████ bilateral trades
of Ontario emission allowances in 2017.[43]

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[37] **RWS-2**, Ramlal – Witness Statement, ¶¶ 26-27.

[38] **C-15**, 2010 WCI Design Document, Design Summary s. 9, p. 18.

[39] **C-15**, 2010 WCI Design Document, Design Summary s. 9, p. 18.

[40] **C-15**, 2010 WCI Design Document, Design Summary s. 9, p. 19.

[41] **C-15**, 2010 WCI Design Document, Design Summary s. 9, p. 19.

[42] **RER-2**, Litz - Expert Report, ¶ 72. The secondary market can be divided into the (i) the spot market, including free or costed transfers between registered participants, and (ii) the derivative market.

[43] **R-10**, Monitoring Analytics, LLC, "WCI Cap-and-Trade Program Ontario Market 2017 Annual Report", 31 January 2018, pp. 10-11 (excerpt).

e) Holding Limits and Corporate Association Groups

34. Irrespective of the means by which an allowance holder obtained allowances (for free, by auction, or via private transactions on the secondary market), the number of allowances it could hold in its CITSS account was subject to a holding limit. A **holding limit** is the maximum number of emission allowances that may be held, at any point in time, by a single cap and trade participant or by a group of participants that are "related persons".[44] The Claimant KS&T was subject to holding limits in Ontario's cap and trade program in 2017 and 2018.[45]

35. "Related persons" included those that shared the same ultimate parent.[46] Participants submitted a "Business Relationship Disclosure Form" detailing how the holding limit would be shared among related person participants, dividing it so that each related person had a percentage share for a total of 100%.[47] Based on the information provided in the Business Relationship Disclosure Forms, the Ministry created a Corporate Association Groups (**CAG**) in CITSS, comprimising all "related person" participants.[48] The distribution of holding limits was entirely up to the participants themselves; the Ministry had no role in decision-making with respect to how the 100% holding limit for a CAG would be distributed among its members in CITSS.[49]

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[44] The *Cap and Trade Regulation* prescribed the formulas used to calculate the holding limits. **R-7**, Regulation 144/16, ss. 40(1), 42(1); *see also* **C-45**, Ontario, Tip Sheet #4, Holding Limits & Purchase Limits for Ontario's Cap and Trade Market ("Ontario Tip Sheet #4"), pp. 1-3. Mr. Litz explains that, "between issuance of the 2008 Design Recommendations and the 2010 Design Document, the WCI markets committee examined a number of potential measures to prevent market manipulation and to allow for better market oversight, including limits on the number of allowances individual entities and associated corporate groups might hold at one point in time." **RER-2**, Litz - Expert Report, ¶ 102.

[45] In 2017, KS&T disclosed that Invista and Komsa (both capped entities in Ontario's program) were owned by its same ultimate parent. In 2018, KS&T updated this disclosure to indicate that it also shared the same ultimate parent with other entities registered in the California program. *See* **R-11**, KS&T, Business Relationship Disclosure Form, [redacted] **R-12**, KS&T, Business Relationship Disclosure Form, [redacted]

[46] **C-45**, Ontario Tip Sheet #4, p. 4. *See also* **R-7**, Regulation 144/16, ss. 40(1), (2) and 42(1), (2); **R-13**, *The Cap and Trade Program Ontario Regulation*, O. Reg. 450/17 Amending O. Reg. 144/16 ("Regulation 450/17"), ss. 17, 18.

[47] **C-45**, Ontario Tip Sheet #4, p. 4.

[48] **C-45**, Ontario Tip Sheet #4, p. 4.

[49] **C-45**, Ontario Tip Sheet #4, pp. 4-5.

f) The Role of Market Participants

36. The Ontario legislation, and the underlying 2010 WCI Design Document,[50] allowed entities without compliance obligations to participate. **Market participants** were participants without compliance obligations that could voluntarily open CITSS accounts, participate in auctions, and trade in allowances. The Claimant KS&T was a market participant in Ontario's cap and trade program.[51]

37. As Mr. Litz explains, during the WCI program design phase concerns were raised about allowing market participants to participate.[52] The WCI partner jurisdictions ultimately decided to allow for market participants, but only to a limited extent. In Ontario, market participants were limited to purchasing 4% of the total allowances offered for sale at auction (compared to the 25% limit that applied to capped participants).[53] As Mr. Litz explains, the rationale behind limiting their auction participation was that it would be easier for the jurisdictions to observe and limit any unintended effects of such participation.[54]

38. The Claimants exaggerate the importance of market participants in Ontario's cap and trade program. For example, market participants were not required for price discovery of emission allowances.[55] As Mr. Litz explains, auctions serve that purpose as they "play a fundamental role in price discovery, liquidity, and the efficient, low-cost distribution of allowances" to compliance entities.[56] The Claimants' assertions that market participants were critical to price discovery and cost-

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[50] **R-14**, Western Climate Initiative, "Market Oversight Draft Recommendations", 1 April 2010, s. 4.2; **R-6**, *Climate Change Act*, s.17; *See also*, **C-15**, 2010 WCI Design Document, "design summary" s. 10, pp. 19, 20-21.

[51] The Claimant Koch Industries was not a participant in the Ontario cap and trade program. **RWS-2**, Ramlal – Witness Statement, ¶ 44.

[52] For example, the WCI partner jurisdictions were concerned that since market participants had an interest in seeing prices rise, the rise in allowance prices could outpace the ability of compliance entities to invest in low-carbon technologies, thereby increasing short-term operational costs. Moreover, allowing non-compliance entities to hold allowances might make it more difficult for compliance entities to obtain the allowances necessary to satisfy their compliance obligations, and could increase the risk for market manipulation. **RER-2**, Litz - Expert Report, ¶ 79.

[53] **R-7**, Regulation 144/16, s. 69(3).

[54] **RER-2**, Litz - Expert Report, ¶ 36.

[55] It is also not accurate to state that "secondary markets are critical to the ability of cap and trade programs to achieve emissions reductions cost-effectively." Claimants' Memorial on Jurisdiction and Merits, 6 October 2021 ("Claimants' Memorial"), ¶ 32.

[56] **RER-2**, Litz - Expert Report, ¶ 69.

effectiveness[57] may have been germane to earlier types of cap and trade systems, such as the Acid Rain program in the 1990s, but they are not accurate in the WCI or Ontario context.[58]

39. Moreover, contrary to the Claimants' assertion, Ontario did not "actively invite[] and encourage[] market participants" to take part in the cap and trade program."[59] In support of this statement, the Claimants point to Ontario's guidance documents about the program, offers of training to assist participants with CITSS registration, and reminders of the deadline to register.[60] Ontario provided guidance to *all* categories of participants listed in the *Climate Change Act*: mandatory participants, voluntary participants, and market participants.[61]

g) Limitation on Crown Liability and Exclusion of Compensation

40. The government's need to maintain broad regulatory flexibility was reflected in the *Climate Change Act*. The *Climate Change Act* specified that there was no right to compensation, no expropriation, and no amount payable by the Crown (*i.e.* the government) with respect to actions or inactions under the Act:

> **No right to compensation**
>
> **70** (1) Despite any other Act or law, no person is entitled to be compensated for any loss or damages, including loss of revenues, loss of profit or loss of expected earnings that would otherwise have been payable to any person in respect of any action taken by the Minister or the Director under this Act, or by any person acting

[57] Claimants' Memorial, ¶¶ 7, 70, 76. In Ontario's first compliance period, the majority of compliance entities were eligible to receive most of their required emission allowances free of charge. **R-7**, Regulation 144/16, ss. 85-90; RS-6, ECO: Introduction to Cap and Trade in Ontario, p. 18 and Table 4.

[58] As Mr. Litz explains in his report, "Early programs established by the U.S. federal government, such as the Acid Rain Program, typically distributed allowances to covered pollution sources at no cost based on a set formula. In contrast, more recently designed programs in North America, including RGGI and the Western Climate Initiative have relied more on the regular auctioning of allowances." *See* **RER-2**, Litz - Expert Report, ¶ 52.

[59] Claimants' Memorial, ¶ 105.

[60] Claimants' Memorial, ¶¶ 105-110, citing **C-30**, Ontario Government, "What you need to know about Ontario's carbon market using a cap and trade program, including how it works and who is required to register", 2 June 2016; **C-31**, Ontario Government, "Cap and Trade CITSS Registration"; **C-32**, Ontario Government, "Cap and Trade: Register and Participate in CITSS", 20 July 2016 and **C-33**, Email from MOECC to Koch Supply & Trading, 28 July 2016.

[61] Market participants that did register were not required to participate in auctions or "mandated" to trade in allowances. *See* Claimants' Memorial, ¶¶ 7, 111, and 216.

> on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts.
>
> **No expropriation, etc.**
>
> (2) Nothing done or not done in accordance with this Act or the regulations constitutes an expropriation or injurious affection for the purposes of the *Expropriations Act* or otherwise at law.
>
> **No payment**
>
> (3) No amount is payable by the Crown with respect to any action taken by the Minister or the Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts.[62]

41. All participants in the Ontario cap and trade program – whether they had compliance obligations (capped participants) or not (market participants) – were aware, or should have been aware, of these regulatory provisions at the outset of the program.

3. Ontario Launches its Program and Holds Auctions in 2017

42. The Ontario cap and trade program went live on January 1, 2017, with a four-year compliance period. As provided for in the *Cap and Trade Regulation*, Ontario created 143,332,000 emission allowances in CITSS[63] and, as planned, distributed emission allowances for free in accordance with the Regulation.[64] Ontario anticipated that eligible compliance entities would receive the majority of their required emission allowances for free during the first compliance period.[65]

43. Ontario held four auctions of emission allowances in 2017, each of which was administered by WCI, Inc. and its subcontractors.[66] The four auctions in 2017 were Ontario-only: Ontario-created

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[62] **R-6**, *Climate Change Act*, s. 70.

[63] **R-13**, Regulation 450/17, s. 54.

[64] **R-13**, Regulation 450/17, ss. 85-90.

[65] **RS-6**, ECO: Introduction to Cap and Trade in Ontario, p. 18 and Table 4.

[66] **R-15**, "Detailed Auction Requirements and Instructions: Ontario Cap and Trade Program Auction of Greenhouse Gas Allowances", 9 January 2017 ("Detailed Auction Requirements and Instructions, 2017"). Auctions involved the following vendors: **WCI, Inc.**, a not-for-profit organization incorporated in Delaware, that supported the WCI partner jurisdictions in developing and implementing their cap and trade programs. Ontario had a contract with WCI, Inc. for support services both during the stand-alone period in 2017 and for the two joint auctions in 2018; **Deutsche Bank**, a WCI Inc.

emission allowances were offered to participants with Ontario CITSS accounts, and could only be used for compliance obligations in Ontario.

44. Regulation 144/16 set out how Ontario allowances would be reserved and distributed for the purposes of the four auctions to be held in a given year.[67] Regulation 144/16 required that the Minister of MECP[68] provide notice to the public of an auction at least 60 days before an auction was to be held. That notice was to include detailed information including the day and time an auction was to be held, a summary of the auction process, and the total number of allowances being offered.[69]

45. To participate in an auction, participants were required to apply through their CITSS representative (either the Primary Account Representative (**PAR**) or Alternative Account Representative (**AAR**)).[70] In seeking approval, a participant was required to submit a "bid guarantee" that set the upper limit of the amount it could spend in the auction. Bid guarantees were sent directly to Deutsche Bank, as the Financial Services Administrator subcontracted by WCI, Inc., in New York or Frankfurt.[71]

46. After an auction, the process and results of the auction were independently verified by a

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subcontractor based in the U.S. that acted as the Financial Services Administrator for emission allowance auctions, including holding bid guarantees, settling payment for successful bids, and aggregating payments from participants and remitting to jurisdictions; SRA International, Inc. (**SRA**), a Virginia-based entity and WCI, Inc. subcontractor that provided hosting services for CITSS (i.e. the technical hardware and software infrastructure); Markit Group Limited, LLC (**Markit**), a London, U.K.-based company, subcontracted by WCI, Inc. to provide auction services; and **Monitoring Analytics, LLC**, a Pennsylvania-based company and WCI, Inc. subcontractor that provided market monitoring services, including certification of auction results. **R-16**, Western Climate Initiative, Inc., "Justification of Competitive Procurement Process: Financial Services for Auctions and Reserve Sales", 18 October 2016; **R-17**, Western Climate Initiative Inc., "Justification of Competitive Procurement Process: Auction and Reserve Sale Administrator Services, 14 June 2016; **R-18**, Western Climate Initiative Inc., "Justification of Competitive Procurement Process: Cap-and-Trade Market Monitoring Services", 8 October 2015; **R-19**, Western Climate Initiative, Inc., "Interim Hosting and Jurisdictional Functionality for the Compliance Instrument Tracking System Service (CITSS), 8 May 2012, **R-20**, Western Climate Initiative Inc., "Contract Amendment: 2012-01-005", 1 January 2016; **R-21**, Western Climate Initiative Inc., "Contract Amendment: 2012-01-006", 12 October 2017.

[67] **R-7**, Regulation 144/16, ss. 57 and 58.

[68] Until mid-2018, MECP (Ministry of the Environment, Conservation and Parks) was called MOECC (Ministry of the Environment and Climate Change).

[69] **R-7**, Regulation 144/16, s. 60(1). *See also* **RWS-2**, Ramlal – Witness Statement, ¶ 28.

[70] **R-15**, Detailed Auction Requirements and Instructions, 2017, p. 12.

[71] **R-15**, Detailed Auction Requirements and Instructions, 2017, pp. 17-18 21-22.

market monitor and certified by MECP.[72] This process took several weeks.[73] Once the auction results were confirmed, successful bidders were required to settle their accounts with the Financial Services Administrator, which then remitted the proceeds to Ontario.[74]

47. Throughout 2017, the secondary market in Ontario was largely inactive. As of December 31, 2017, there were a total of ████ bilateral trades in Ontario emission allowances.[75] Only ████ such trade involved KS&T, as seen immediately below.[76]

4. KS&T Participates in the Ontario Program in 2017

48. KS&T is a Delaware entity based in Kansas. It describes itself as a global commodities trader focusing on oil, gas, power, environmental credits and metals.[77] In 2012 or 2013, KS&T registered to participate in the California cap and trade program as a market participant, and was assigned a California CITSS account.[78]

49. Despite having no compliance obligations or physical presence in Ontario, in late 2016 KS&T decided to also register in the Ontario's cap and trade program as a market participant, and was assigned an Ontario CITSS account.[79]

50. KS&T placed bids in each of the four Ontario-only auctions in 2017, successfully acquiring

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[72] **RWS-2**, Ramlal – Witness Statement, ¶¶ 30-32.

[73] **R-15**, Detailed Auction Requirements and Instructions, 2017, pp. 33-35.

[74] **R-15**, Detailed Auction Requirements and Instructions, 2017, pp. 36-38.

[75] **R-10**, Monitoring Analytics, LLC, "WCI Cap-and-Trade Program Ontario Market 2017 Annual Report" (excerpt), 31 January 2018, pp. 10-11.

[76] **RWS-2**, Ramlal – Witness Statement, ¶ 51 and Attachment 1, ████

[77] **CWS-2**, Witness Statement of Graeme Martin, 4 October 2021 ("Martin - Witness Statement"), ¶ 4; **R-22**, KS&T Energy Derivatives Brochure, "The Global Source for Commodities", pp. 1-6.

[78] **CWS-2**, Martin - Witness Statement, ¶ 18; **RWS-2**, Ramlal – Witness Statement, ¶ 38. Under the California regulations these participants were called "voluntary associated entities." **RER-2**, Litz - Expert Report, ¶ 77; **R-23**, Detailed Auction Requirements and Instructions, California Cap-and-Trade Program, Québec Cap-and-Trade System, and Ontario Cap-and-Trade Program Joint Auction of Greenhouse Gas Allowances, 26 January 2018 ("Detailed Auction Requirements and Instructions, 2018"), p. 5 definition of "General Market Participant".

[79] **RWS-2**, Ramlal – Witness Statement, ¶ 38; **NR-13**, KS&T Participant Registration Form, ████ **C-51**, KS&T, Ontario Business Relationship Disclosure Form, ████.

allowances in [redacted].[80] KS&T did not use any of these emission allowances to satisfy regulatory requirements in Ontario.[81]

51. The Claimants' witness Mr. Frank King states that KS&T "traded those allowances in the secondary market over the course of 2017."[82] In fact, KS&T's [redacted] transfer of Ontario emission allowances in 2017 was recorded in CITSS on [redacted], when KS&T transferred [redacted] emission allowances of 2017 vintage to a third party in Ontario.[83]

5. Ontario Harmonizes its Cap and Trade Program

52. One of the stated purposes of the *Climate Change Act* was "to enable Ontario to collaborate and coordinate with other jurisdictions" in its efforts to reduce GHG emissions.[84] The *Climate Change Act* was drafted to allow for the eventual linkage of the Ontario system with those of California and Québec.[85]

53. The WCI partner jurisdictions had anticipated the possibility of linkage in the 2010 WCI Design Document. The idea was that linkage would provide the opportunity to reduce emissions over a wider territory, thus improving market liquidity and reducing the likelihood of manipulation, while at all times "protect[ing] the integrity of each jurisdiction's program and the regional effort".[86] As Mr. Litz explains, the WCI partner jurisdictions acknowledged the paramount importance of maintaining the integrity of their respective systems, and "ensur[ing] that there are no transfers which are incompatible with the partner jurisdiction's implementation of the Cap-and-Trade program."[87]

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[80] **RWS-2**, Ramlal – Witness Statement, ¶ 45 and Attachment 1, [redacted] *See* Claimants' Memorial, ¶ 148.

[81] Two indirect subsidiaries of the Claimant Koch Industries were registered in Ontario's cap and trade program as mandatory participants: Invista (Canada) Company ("Invista") and KOMSA Sarl ("Komsa"). **RWS-2**, Ramlal – Witness Statement, ¶¶ 63-64 and Attachment 2. Neither entity is a party to this arbitration.

[82] **CWS-4**, King – Witness Statement, ¶ 20; Claimants' Memorial, ¶¶ 141, 153.

[83] **RWS-2**, Ramlal – Witness Statement, ¶ 51 and Attachment 1, transfer No. [redacted].

[84] **R-6**, *Climate Change Act*, s. 2(1)(b).

[85] **R-6**, *Climate Change Act*, s. 2(1)(b).

[86] **C-15**, 2010 WCI Design Document, p. 22.

[87] **RER-2**, Litz - Expert Report, ¶ 111.

Linkage was to be "achieved by recognizing each other's instruments for compliance purposes"[88]. The objective was to hold joint auctions and to allow for allowances created by one jurisdiction to be recognized for compliance purposes in the other jurisdictions.

54. In late 2017, Ontario amended its regulations to allow for harmonization in early 2018.[89] On January 1, 2018, Ontario amendments came into force that allowed for the recognition of emission allowances created by California and Québec as equivalent to Ontario emission allowances.[90] The emission allowances would thus be fungible for compliance purposes within the three jurisdictions, regardless of which jurisdiction had created them. Ontario also updated its rules on business relationships and set out the procedures for transfers between CITSS accounts in Ontario and CITSS accounts in other jurisdictions.[91]

55. The harmonization of the three regimes was recognized in September 2017 in a non-binding agreement between the Government of California, the Government of Ontario, and the Gouvernement du Québec (**Harmonization Agreement**).[92] The Harmonization Agreement recognized the regulatory autonomy of each party:

> WHEREAS, the Parties further recognize that the present Agreement does not, will not and cannot be interpreted to restrict, limit or otherwise prevail over relevant national obligations of each Party, if applicable, and each Party's

[88] **C-15**, 2010 WCI Design Document, p. 22.

[89] **R-13**, Regulation 450/17, s. 4; **R-7**, Regulation 144/16, s. 10.1.

[90] **R-13**, Regulation 450/17, s. 4; **R-7**, Regulation 144/16, s. 10.1.

[91] **RWS-2**, Ramlal – Witness Statement, ¶¶ 25, 43; **R-13**, Regulation 450/17, ss. 2, 11, 14, 15, 17, 18, 22, 46; **R-7**, Regulation 144/16, ss. 2, 26, 34, 37, 40, 42, 51, 51.1, 51.1.1, 51.1.2. As a result, Ontario participants were required to update their business relationship disclosure forms. *See* **R-7**, Regulation 144/16, ss. 26(5), (6), (7), 34(5), (6), (7), 37(2), (3), (4). **R-24**, KS&T, Business Relationship Disclosure Form, pp. 4-7; **R-12**, KS&T, Business Relationship Disclosure Form, pp. 4-6.

[92] **R-25**, Ontario Newsroom, "Agreement on the Harmonization and Integration of Cap-and-Trade Programs for Reducing Greenhouse Gas Emissions between the Gouvernement du Québec, the Government of California and the Government of Ontario", 22 September 2017 ("Harmonization Agreement), Art. 1(b) and (f).

> sovereign right and authority to adopt, maintain, modify, repeal or revoke any of their respective program regulations or enabling legislation[.][93]

56. The Harmonization Agreement did not provide for any fixed term. The Harmonization Agreement acknowledged that a party could withdraw from the Agreement, and included a "best-efforts" provision regarding notice of an intent to withdraw.[94]

6. KS&T Transfers the Balance of its Ontario CITSS Account to California

57. The regulatory changes allowing for Ontario and California CITSS accounts to be linked came into effect on January 1, 2018. [redacted] the Claimant KS&T transferred the [redacted] of emission allowances in its Ontario CITSS to its California CITSS account.[95]

7. Ontario Participates in Joint Auctions in 2018

58. Once the three systems were harmonized, California, Québec, and Ontario could offer emission allowances for sale in joint auctions. Ontario participated in two joint Ontario-California-Québec auctions in February and May 2018. Like the Ontario-only auctions in 2017, the joint auctions were administered by a WCI, Inc. subcontractor.[96]

59. Under Ontario's regulations, in order to participate in an auction, Ontario was required to provide a public notice 60 days in advance of the auction.[97] The participating jurisdictions would work together to complete necessary administrative tasks in support of the auction process. In its notice of participation, Ontario was required to state the number of emission allowances it would contribute to the auction.[98]

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[93] **R-25**, Harmonization Agreement, Preamble.

[94] **R-25**, Harmonization Agreement, Art. 17: A party "shall endeavour" to give 12 months notice of its intent to withdraw.

[95] [redacted] KS&T's Ontario CITSS account held [redacted] emission allowances. On [redacted] [redacted] emission allowances were transferred to KS&T's California CITSS account. **RWS-2**, Ramlal – Witness Statement, ¶¶ 45, 51-52 and Attachment 1, [redacted]

[96] **R-15**, Detailed Auction Requirements and Instructions, 2017, p. 4 definition of "Auction Administrator"; **R-23**, Detailed Auction Requirements and Instructions, 2018, p. 3 definition of "Auction Administrator".

[97] **RWS-2**, Ramlal – Witness Statement, ¶ 28; **R-7**, Regulation 144/16, s. 60(1).

[98] **R-23**, Detailed Auction Requirements and Instructions, 2018, p. 7.

60. The procedures for the joint auction itself were similar to those for the Ontario-only auctions. Participants would register to bid and would provide a financial guarantee that set the upper limit of its purchase amount. Auctions were conducted through an electronic, internet-based Auction Platform using a "single round, sealed bid auction format". The Auction Administrator would rank all bids received from highest to lowest. Emission allowances were then awarded until the entire supply of allowances was exhausted or all qualified bids had been filled. The actual settlement price was set as the bid price at which all allowances had been distributed (or all qualified bids were filled). This then became the price per allowance that all entities were to be charged for the allowances won in the auction.[99]

61. These allowances contributed by each jurisdiction would be pooled by the auction administrator, and successful bidders would acquire a mixture of each jurisdiction's emission allowances in proportion to each jurisdiction's contribution to the auction. Once payment was settled by the Financial Services Administrator, each of the three jurisdictions transferred its share of allowances into each successful qualified bidder's CITSS account.[100] The detailed auction instructions explain:

> In a simple case, where the Current Auction allowances are all the same vintage, each bid lot would be comprised of allowances from all jurisdictions proportional to the quantity of each jurisdiction's contribution to the total Current Auction amount. For example, if the Current Auction amount included 60% California 2018 vintage allowances, 20% Québec 2018 vintage allowances, and 20% Ontario 2018 vintage allowances, each bid lot of 1000 allowances would include 600 California 2018 vintage allowances, 200 Québec 2018 vintage allowances, and 200 Ontario 2018 vintage allowances. Each jurisdiction conducts separate transfers for the proportion of allowances awarded from the jurisdiction; therefore, successful qualified bidders in this example will see three (3) allowance transfers, one from California, one from Québec, and one from Ontario.[101]

[99] **R-23**, Detailed Auction Requirements and Instructions, 2018, pp. 35, 43.

[100] **R-23**, Detailed Auction Requirements and Instructions, 2018, pp. 51-52.

[101] **R-23**, Detailed Auction Requirements and Instructions, 2018, pp. 51-52. *See also* **RER-2**, Litz - Expert Report, ¶ 113: "At the allowance auctions, allowances are sold in lots of 1,000 allowances. Each 1000-allowance lot consisted of a proportionate share of allowances from each of California, Ontario and Quebec. The origin of individual allowances, while known to program administrators, is not known to the allowance purchaser. Thus, when an auction participant in California with no connection at all to Ontario purchased lots from the joint allowance auctions in early 2018, that

62. Jurisdictions only received proceeds of sale commensurate to the number of emission allowances that they had created. After payments were aggregated by the Financial Services Administrator in New York, proceeds were sent to the three jurisdictions in an amount proportional to the number of allowances the jurisdiction had contributed to the auction.

8. KS&T Participates in the February 2018 Joint Auction and Transfers the Balance of its Ontario CITSS Account to California

63. In the February 2018 joint auction, KS&T acquired [redacted] emission allowances of the current vintage[102] at USD 14.61 each, for a total of USD [redacted].[103] Ontario's share in this amount was USD [redacted] for [redacted] emission allowances of 2018 vintage.[104] Soon after the emission allowances from all three jurisdictions were deposited to KS&T's Ontario CITSS account, KS&T transferred [redacted] emission allowances in its Ontario CITSS account to its California CITSS account.[105]

64. As discussed in II.B.4 below, KS&T also participated in the next joint auction, in May 2018, through its Ontario CITSS account, acquiring [redacted] allowances.[106] However, the Claimants'

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participant received Ontario and Quebec allowances in its California CITSS account as part of every 1,000-allowance lot purchased, just as a participant in Ontario received California and Quebec allowances as part of every 1,000-allowance lot purchased."

[102] California and Québec offered for sale emission allowances of both 2016 and 2018 vintages, while Ontario offered for sale emission allowances of 2018 vintage only. As a successful bidder in a joint auction, KS&T received emission allowances of both 2016 and 2018 vintages in its winning lot. *See* **R-26**, "Auction Notice: California Cap-and-Trade Program, Québec Cap-and-Trade System, and Ontario Cap-and-Trade Program Joint Auction of Greenhouse Gas Allowances on February 21, 2018", 10 January 2018, p. 4: "For the February 2018 Joint Auction #14, there will be multiple vintages offered within the Current Auction. When submitting bids for the Current Auction, all bids are placed as 'Current' vintage."; **R-27**, "California Cap-and-Trade Program, Ontario Cap-and-Trade Program, and Québec Cap-and-Trade System February 2018 Joint Auction #14 Summary Results Report", 28 February 2018, p. 2, Table 1: Auction Results for February 2018 Joint Auction #14.

[103] **C-89**, WCI Inc., Results from Joint Auction #14, KS&T Financial Statement, 28 February 2018.

[104] California's share in the auction proceeds was US$22,414,384.41 for 306,836 emission allowances of 2016 vintage and 1,227,345 emission allowances of 2018 vintage, and Québec's share was US$3,342,168.99 for 45,752 emission allowances of 2016 vintage and 183,007 emission allowances of 2018 vintage. *See* **RWS-2**, Ramlal – Witness Statement, ¶¶ 47, 54 and Attachment 1, transfer[redacted] No. [redacted]

[105] **RWS-2**, Ramlal – Witness Statement, ¶ 54 and Attachment 1, [redacted]

[106] **RWS-2**, Ramlal – Witness Statement, ¶¶ 48, 57.

assertion that KS&T "paid USD 30,158,240.95 into Ontario public coffers"[107] in the May 2018 auction is false.[108] Of the ██████ emission allowances received by KS&T in that auction, Ontario had created ██████ allowances; of the USD ██████ paid by KS&T, Ontario received USD ██████[109]

65. In 2018, KS&T's secondary market activity in Ontario consisted of ██████, an apparent pass-through transaction from KS&T's California account. On ██████ KS&T transferred ██████ emission allowances from its California CITSS account to its Ontario CITSS account. Two days later, KS&T transferred ██████ allowances from its Ontario CITSS account to the Ontario CITSS account of an unrelated participant.[110]

B. Ontario's Cap and Trade Program Enters a Period of Uncertainty

1. The Progressive Conservative Party Campaigns on Cancelling Cap and Trade

66. In 2018, Ontario's cap and trade program was up and running and its CITSS accounts were newly linked with those of California and Quebéc. In 2018, Ontario was also preparing for its provincial election. Provincial elections in Ontario occur every four years,[111] and on May 8, 2018 then-Premier of the Ontario Liberal Party Kathleen Wynne formally announced that Ontario's next

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[107] Claimants' Memorial, ¶ 206.

[108] Participants in joint auctions that bid through their Ontario CITSS accounts could bid in either USD or CAD. KS&T elected to make its bids in the joint auctions through its Ontario CITSS account in USD. **R-23**, Detailed Auction Requirements and Instructions, 2018, p. 18: "Entities registered in the California Cap-and-Trade Program can only select USD. QC and ON entities may select USD or CAD and must use the selected currency for participation throughout the auction, including submitting the bid guarantee, submitting bids during the joint auction, and completing financial settlement. The selected currency cannot be changed after the close of an auction application period." *See* **C-89**, WCI, Inc., Results from Joint Auction #14, KS&T Financial Statement, 28 February 2018; **C-96**, WCI, Inc., Results from Joint Auction #15, KS&T Financial Statement, 23 May 2018.

[109] Ontario received US$██████ for ██████ emission allowances transferred to KS&T at US$14.65 each. **RWS-2**, Ramlal – Witness Statement, ¶ 48 and Attachment 1, ██████

[110] **RWS-2**, Ramlal – Witness Statement, ¶ 56 and Attachment 1, ██████

[111] **R-28**, *Election Act*, R.S.O. 1990, c. E.6, s. 9; **R-29**, *Election Statute Law Amendment Act, 2016*, S.O. 2016, c.33, s. 7. In 2016, Ontario's Election Act was amended to provide that, subject to the Lieutenant Governor's power to dissolve the Legislature earlier, "general elections shall be held on the first Thursday in June in the fourth calendar year following polling day in the most recent general election." Because the previous election was held on June 12, 2014, it was known well in advance that the provincial election would be held on Thursday, June 7, 2018.

general election would take place on June 7, 2018.[112]

67. Ontario's cap and trade program was a hot election issue from the outset. In November 2017, the Progressive Conservative Party of Ontario (**Progressive Conservative Party**) unveiled its platform, called the "People's Guarantee". The platform put forward 130 policy resolutions following a wide public consultation process that began in March 2016.[113] One of these resolutions was called "Change that works for the environment" that was aimed at "protect[ing] our environment without making life unaffordable for families".[114] More specifically, it included a plan to "dismantle Cap-and-Trade" and "withdraw from the Western Climate Initiative".[115] In mid-February 2018, Doug Ford was elected leader of the party and began to publicly campaign against cap and trade.[116]

68. The criticism against cap and trade followed a 2016 report of Ontario's Auditor General, which concluded that "the cap-and-trade system will result in only a small portion of the required greenhouse-gas reductions needed to meet Ontario's 2020 target"[117] and "at significant cost to Ontario businesses and households".[118] Ontario's cap and trade program was also criticized by think tanks such as the Fraser Institute.[119]

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[112] **R-30**, Ontario Newsroom, "Ontario Election on June 7, 2018", May 8, 2018.

[113] **R-31**, Ontario PC, "Patrick Brown and the Ontario PCs release the People's Guarantee", 25 November 2017.

[114] **R-32**, PC Party of Ontario, "People's Guarantee", p. 25.

[115] **R-32**, PC Party of Ontario, "People's Guarantee", p. 25.

[116] **R-34**, PC Party of Ontario, "Doug Ford Will Fight a Carbon Tax and Scrap Kathleen Wynne's 'Cap and Trade' Slush Fund", 23 April 2018; **R-35**, Ontario PC Party, "Doug Ford's Plan for the People Will Put More Money in the Pockets of Ontario Parents", 28 April 2018.

[117] **R-36**, Minister of the Environment and Climate Change, 2016 Annual Report of the Office of the Auditor General of Ontario, Chapter 3, p. 149, s. 3.02. *See also* p. 167, s. 4.3: "Ontario Cap and Trade Will Not Significantly Lower Actual Emissions up to 2020"; *see also* **R-37**, Office of the Auditor General of Ontario, News Release "Ontario's Cap and Trade Will Not Significantly Lower Emissions Within the Province by 2020: Auditor General", 30 November 2016.

[118] **R-36**, Minister of the Environment and Climate Change, 2016 Annual Report of the Office of the Auditor General of Ontario, Chapter 3 Section 3.02, pp. 149 and 150. Preliminary estimates by the Ministry of Finance estimated that the direct costs to the average Ontario household in 2019 would be $210, plus an additional $75 in indirect costs (e.g., goods and services). Furthermore, cap and trade was expected to bring higher electricity prices, which could lead people to switch to cheaper natural gas, a fossil fuel that also produces greenhouse gases. Electricity prices were projected to increase by 14% for businesses and 25% for households.

[119] **R-42**, Fraser Institute Blog, "Ontario government's cap-and-trade plan places politics over policy", 26 February 2016; **R-43**, Fraser Institute, "Ontario's climate action plan undermines case for cap and trade", 18 May 2016. The Fraser Institute received funding from the Charles Koch Foundation. *See* **R-38**, Charles Koch Foundation, "Who we support";

2. Industry Experts Highlight the Cap and Trade Program's Uncertain Future

69. In late 2017, analysts started to connect poor auction performance with the uncertainty about the future of the Ontario's cap and trade program. In December 2017, a report by the International Emissions Trading Association stated that the fourth and final Ontario auction of 2017 "saw only 83% of the current allowances get picked up at the price floor as concerns mounted that the opposition Progressive Conservative Party would replace the market with the federal government's 'backstop' tax regime should they win next June's election."[120]

70. Specialized international media also noted the uncertain future of cap and trade in Ontario. Soon after the May 2018 auction, Argus Media noted that the auction had been held "just ahead of a 7 June election that could upend the nascent carbon market alliance", and that the "Progressive Conservative Party has threatened to do away with the cap-and-trade program if it takes over as the majority government."[121] Argus Media also reported that "not all market signals suggest widespread optimism about prospects for Ontario's carbon market" and that "[a] carbon trader for one California fuel wholesaler said that market participants had already accounted for the possibility of Ontario's departure well before the event."[122] The carbon trader's representative was quoted saying "With the December 2018 futures trading down to $15, we priced in most of the risk already."[123]

71. The Claimants' fact witnesses in this arbitration acknowledge that they knew in early 2018 that Ontario's cap and trade program might be cancelled.[124] As of early 2018, there was a high degree

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R-39, Charles Koch Foundation, "2017 Form 990-PF", p. 105; **R-40**, Charles Koch Foundation, "2018 Form 990-PF", pg. 138.

[120] **R-44**, IETA Insights, "Greenhouse Gas Market Report" No. 4, December 2017, p. 2. The federal backstop consists of two elements: a price on carbon applied to fossil fuels under Part 1 of the Greenhouse Gas Pollution Pricing Act (GGPPA) and administered by the Canada Revenue Agency, and an output-based pricing system (OBPS), a regulatory trading system administered by Environment and Climate Change Canada for industrial facilities under Part 2 of the GGPPA. *See* **R-45**, Government of Canada, "Carbon pollution pricing systems across Canada".

[121] **R-46**, Argus Media, "Carbon auction suggests optimism over Ontario", 24 May 2018.

[122] **R-46**, Argus Media, "Carbon auction suggests optimism over Ontario", 24 May 2018.

[123] **R-46**, Argus Media, "Carbon auction suggests optimism over Ontario", 24 May 2018.

[124] Paul Brown states that "[t]he first time [he] heard that the Ontario Cap and Trade Program might be cancelled was early in 2018, when the Ontario Progressive Conservative (PC) Party signalled that they were not supportive of the Ontario Cap and Trade Program and that if they were to win the election they might repeal it." **CWS-3**, Brown - Witness Statement, ¶ 35. Graeme Martin testifies that "Doug Ford represented the Ontario Conservative Party, which we knew

of uncertainty surrounding the future of Ontario's cap and trade program.

3. The May 2018 Auction Takes Place During the Election Campaign

72. In accordance with Ontario's regulations, and in cooperation with the other jurisdictions, the public notice of the May 15, 2018 joint auction had been published in March 2018. The auction notice provided a clear timeline for the settlement of accounts after the auction, and stated that emission allowances would be transferred to winning bidders' accounts on June 11, 2018.[125]

73. In this arbitration, the Claimants rely on the fact that "the auction was held *prior* to the election."[126] This is true, but the Claimants were also well aware that the transfer of allowances into winning bidders' CITSS accounts would only occur on June 11, 2018, after the election.[127] A sophisticated entity like KS&T would have been aware of the risks associated with participating in the May auction in these circumstances.

74. Despite these risks, KS&T chose to participate in the May 2018 auction through its Ontario CITSS account rather than its California CITSS account.

4. KS&T Participates in the May 2018 Joint Auction

75. KS&T registered to bid in the May 2018 through its Ontario CITSS account. KS&T acquired [redacted] emission allowances of the current vintage (i.e. a combination of 2016 and 2018 vintages) at USD 14.65 each, for the total price of USD [redacted].

76. On June 11, 2018, the three jurisdictions transferred emission allowances from the May 2018 joint auction. KS&T's Ontario CITSS account held [redacted] emission allowances.[128] Of those [redacted]

had included opposition to the Cap and Trade Program as part of its campaign platform." **CWS-2**, Martin - Witness Statement, ¶ 49.

[125] **R-47**, Auction Notice, "California Cap-and-Trade Program, Québec Cap-and-Trade System, and Ontario Cap-and-Trade Program Joint Auction of Greenhouse Gas Allowances On May 15, 2018", 16 March 2018 ("Auction Notice, 16 March 2018"), p. 8, "Distribution of auction proceeds completion | Monday, June 11, 2018".

[126] Claimants' Memorial, ¶ 187 (emphasis in original).

[127] The Ontario election date of June 7, 2018 was known advance. **R-28**, *Election Act*, R.S.O. 1990, c. E.6, s. 9; **R-29**, *Election Statute Law Amendment Act, 2016*, S.O. 2016, c.33, s. 7.

[128] **RWS-2**, Ramlal – Witness Statement, ¶¶ 55, 57.

███ allowances, ███ had been created by Ontario. Once payments had been aggregated by the Financial Services Administrator, Ontario would receive (as part of a lump sum including payment for other participants' allowances) USD ███ for the ███ allowances.[129]

5. The Progressive Conservative Party Wins a Majority and Prepares for Its Swearing-in

77. Following an election, the Lieutenant Governor of Ontario invites the leader of the party that has secured a majority of seats in the legislature to form the next government.[130] After receiving and accepting this invitation, the leader is known as the "Premier-Designate".

78. On June 8, 2018, Mr. Ford accepted the invitation of the Lieutenant Governor to form the next government. The date for the formal transition of power and swearing-in of the new government was set for June 29, 2018.[131] During the transition period, it is routine for the Premier-Designate to make statements outlining the incoming government's priorities and intentions for once it assumes office.[132]

6. Ontario Does Not Provide Notice of Participation in the August 2018 Joint Auction

79. Between the moment an election is called (once the "writ" of election is issued) and until a new government is sworn-in, the bureaucracy is in what is known as the "caretaker period". During the caretaker period, key principles must be observed. Mr. Wood, Assistant Deputy Minister of the Climate Change and Resiliency Division at MECP, explains that "the current government cannot

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[129] **RWS-2**, Ramlal – Witness Statement, ¶¶ 48, 57 and Attachment 1, ███

[130] **R-48**, Lieutenant Governor of Ontario, "Constitutional Role": "Canada is a constitutional monarchy with The Queen as Sovereign and head of state. In Ontario, the Lieutenant Governor is The Queen's representative."

[131] **R-49**, Ontario Newsroom, "Doug Ford to Become Ontario's 26th Premier", 8 June 2018.

[132] For example, Premier-Designate Ford made announcements that he "will be working with [his] team to fulfill [his] campaign commitments and deliver change for the people", *see* **R-49**, Office of the Premier-Designate, News Release, "Doug Ford to Become Ontario's 26th Premier", 8 June 2018, that he had "confirmed his commitment to keeping the Pickering Nuclear Generating Station in operation until 2024", *see* **R-51**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Commits to Protecting Jobs at Pickering Nuclear Generating Station", 21 June 2018, and that he committed to building a public memorial to honour Canadian heroes of the war in Afghanistan, **R-52**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford will build Memorial to Honour Canadian Heroes of the War in Afghanistan", 27 June 2018.

presume that it will form the next government and as such it must not make decisions that would frustrate the goals of any incoming government."[133]

80. Only routine or ongoing administrative decisions may be made during the caretaker period. In addition, urgent or time sensitive decisions may need to be made during this period.[134] To ensure that caretaker principles are observed, senior members of the public service identify the time sensitive decisions that must be made during the caretaker period. To perform this role, "the bureaucracy must be particularly aware of any issues that arise during the election campaign and that may affect the implementation of future policies of the next government."[135]

81. In accordance with these caretaker principles, Mr. Wood explains that as soon as the writ of election was issued on May 8, 2018, the bureaucracy began to the decisions that would need to be made during the caretaker period.[136] As noted above, if Ontario wished to participate in an auction, it was required to issue a public notice 60 days in advance.[137] The next joint auction was scheduled for August 14, 2018, meaning that if Ontario wished to participate it would need to issue a notice by June 15, 2018.[138] As explained by Mr. Wood, it would have been contrary to the caretaker principles for the Minister or his delegate to issue the auction notice because to do so would have frustrated the incoming government's policy intentions.[139]

7. California De-Links its CITSS Accounts from Ontario CITSS Accounts

82. At 8:25 pm Central Time on June 15, 2018, the California Air Resources Board released a

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[133] **RWS-1**, Wood – Witness Statement, ¶ 10.

[134] **R-53**, Memo to Deputy Ministers from Secretary Steve Orsini, "Public Service Responsibilities and Procedures Leading To and During the Election Period", 28 February 2018.

[135] **RWS-1**, Wood – Witness Statement, ¶ 12.

[136] **RWS-1**, Wood – Witness Statement, ¶ 13.

[137] **R-7**, Regulation 144/16, s. 60.

[138] **RWS-1**, Wood – Witness Statement, ¶ 12.

[139] As Mr. Wood explains, Premier-Designate Ford addressed this policy intention in a public announcement on June 15, 2018 at around 10 am, when he stated that his first act following the swearing-in of his government would be to end Ontario's cap and trade program. **RWS-1**, Wood – Witness Statement, ¶ 15. *See* **C-7**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Announces an End to Ontario's Cap-and-Trade Carbon Tax", 15 June 2018.

"Market Notice" announcing that the CITSS had been "modified to prevent transfers of compliance instruments between entities registered in Ontario and entities registered in either California or Québec".[140] Therefore, as of the evening of June 15, 2018, participants could no longer transfer their compliance instruments from an Ontario CITSS account to a California CITSS account or *vice versa*.

C. Ontario Winds Down the Cap and Trade Program and Provides Compensation on a Principled Basis

83. As soon as the Progressive Conservative Party was sworn-in on June 29, 2018, and as promised during the election campaign, the new government began the orderly wind-down of Ontario's cap and trade program. The government followed a principled and rational approach to winding down the cap and trade program by first making Regulation 386/18 on July 3, 2018 and then introducing the *Bill 4, the Cap and Trade Cancellation Act, 2018* (**Bill 4**) on July 25, 2018 before the Legislative Assembly of Ontario.

1. Regulation 386/18 Comes into Force on July 3, 2018

84. On his first day in office, Premier Ford announced that he was recalling the Legislative Assembly for a summer session on July 11, 2018, to deal with top priority issues that were discussed during the election campaign. Members of his Cabinet confirmed that "cap-and-trade [was] going to be right at the top of the agenda".[141]

85. In an effort to take expedient steps towards fulfilling its mandate, the new government made Ontario Regulation 386/18, which came into force on July 3, 2018. The Regulation immediately repealed the *Cap and Trade Regulation* and prohibited registered participants from purchasing, selling, trading or otherwise dealing with emission allowances.[142] Participants with Ontario CITSS

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[140] **C-104**, California Air Resources Board, "Market Notice: New Functionality in CITSS", 15 June 2018. *See also* **C-105**, ICE Futures U.S., "Notice: California Carbon Allowances Futures Contracts – Changes to Deliverable Allowances in the Compliance Instrument Tracking System Service", 18 June 2018; **C-103**, CA CITSS Help Desk, "Market Notice – New Functionality in CITSS", 15 June 2018.

[141] **R-54**, ipolitics, "Ford to recall Ontario legislature on July 11", 29 June 2018.

[142] **R-55**, *Prohibition Against the Purchase, Sale and Other Dealings with Emission Allowances and Credits*, O. Reg. 386/18, s. 1: "For the purposes of subsection 21 (3) of the Act, no registered participant shall, on and after the day this Regulation comes into force, purchase, sell, trade or otherwise deal with emission allowances and credits." and s. 2: "Ontario Regulation 144/16 is revoked." Regulation 386/18 was made by the Cabinet on June 29, 2018, and entered into force on July 3, 2018, on the day it was filed. *See also* **C-107**, Office of the Premier, "Premier Doug Ford Announces the

accounts received an email notification that same day confirming that: "all Ontario participants will be prevented from both transferring and receiving instruments (including emission allowances and credits) in their general account in CITSS."[143]

2. The Government Introduces Bill 4 Before the Ontario Legislative Assembly

86. On July 25, 2018, the government introduced Bill 4[144] to repeal the *Climate Change Act* and wind down Ontario's cap and trade program. Bill 4 set out the framework for the orderly wind-down of the program. First, it created a requirement for capped participants to report their GHG emissions from January 1 to July 3, 2018 and the retirement (by the Ministry) of emission allowances matching those emissions.[145] In addition, Bill 4 set out a detailed compensation process for eligible participants that had purchased emission allowances in excess of their actual emissions of GHGs.[146] Bill 4 also required the government to establish targets for reducing GHG emissions in Ontario, and for the Minister to elaborate a new climate change plan.[147] Consistent with Ontario's legislative processes, Bill 4 was required to pass three readings and a committee stage before it could receive Royal Assent and come into force.

87. On September 11, 2018, Ontario posted Bill 4 for public comments on the Environmental

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End of the Cap-and-Trade Carbon Tax Era in Ontario", 3 July 2018. In Ontario (and Canada generally), "cabinet" refers to the meeting of the ministers together as a group. The cabinet is in most matters the supreme executive authority. The cabinet formulates and carries out all executive policies, and it is responsible for the administration of all the departments of government. The Premier presides over the meetings of the cabinet. Where a statute requires that a decision be made by the "Governor in Council", the cabinet will make the decision, and send an "order" or "minute" of the decision to the Lieutenant Governor for signature (which by convention is automatically given). *See* **R-56**, Peter Hogg, Wade Wright, "Constitutional Law of Canada" (Carswell, 2021), ss. 9.5 and 9.6.

[143] **C-108**, Cap and Trade Help (MOECC), "Notice: Ontario's Cap and Trade Program", 3 July 2018.

[144] **R-57**, Bill 4, An Act respecting the preparation of a climate change plan, providing for the wind down of the cap and trade program and repealing the Climate Change Mitigation and Low-carbon Economy Act, 2016, 25 July 2018 ("Bill 4").

[145] **R-57**, Bill 4, ss. 6, 7.

[146] **R-57**, Bill 4, s. 8.

[147] **R-57**, Bill 4, s. 3, 4 and 5; *See* **C-111**, Ontario Government News Release, "Ontario Introduces Legislation to End Cap and Trade Carbon Tax Era in Ontario", 25 July 2018: "The proposed legislation will also include measures to help replace the cap-and-trade carbon tax with a better plan for achieving real environmental goals."

Registry.[148] Interested stakeholders had 30 days to comment on the bill. As Mr. Wood explains, the Ministry received 11,222 comments and it "reviewed, analyzed and summarized all of these comments, which touched upon themes such as transparency and accountability, need for an alternative program, economic impact, financial impacts of compensation approach and climate change plan."[149]

88. In addition to "substantial lobbying efforts" by KS&T,[150] Koch Industries also provided comments on Bill 4.[151] Koch Industries began by reiterating its opposition to the concept of cap and trade[152] before focussing on its dissatisfaction with the proposed compensation principles.[153] It argued that Bill 4 would "disadvantage entities that diligently met their 'mandatory participant' compliance obligations through multi-national corporate compliance entity that is registered as a 'market participant'."[154] Koch Industries proposed creating a separate class of participants who *would* be eligible for compensation: those that elected, despite the clear legislative regime, to structure their internal affairs by registering as market participants rather than compliance entities. Bill 4, Koch Industries submitted, would "exclude[] specific market participants based only on definitional classifications."[155]

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[148] *See* **C-12**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018, pp. 1, 10. The Claimants' Memorial refers to a case brought by Greenpeace Canada that was dismissed by a majority decision of an Ontario court. **R-58**, *Greenpeace Canada v. Minister of the Environment (Ontario)*, 2019 ONSC 5629, ¶¶ 88, 91, and 116. The validity and effectiveness of the *Cancellation Act* was not challenged in that proceeding. Instead, the applicant sought "an academic determination" that repeal of the Regulation 144/16 did not meet the public participation requirements of the *Environmental Bill of Rights*. *See* ¶ 91 per Myers, J.

[149] **RWS-1**, Wood – Witness Statement, ¶ 24; **C-12**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018, pp. 2-3.

[150] Claimants' Memorial, ¶¶ 229. Between July and September 2018, KS&T representatives met with various high-ranking Ontario officials, including the Minister of Infrastructure, the Minister of Finance, and the Chief of Staff to the Minister of the Environment, as well as the Premier's Principal Secretary, the Executive Director of Policy, and the Director of Stakeholder Relationships. Claimants' Memorial, ¶¶ 222-228.

[151] **RS-86**, Environmental Registry of Ontario, "Comment on Bill 4, Cap and Trade Cancellation Act", Comment ID 10437, 11 October 2018 ("Koch Comment on Bill 4").

[152] **RS-86**, Koch Comment on Bill 4, p. 1.

[153] **RS-86**, Koch Comment on Bill 4, p. 2.

[154] **RS-86**, Koch Comment on Bill 4, Cap and Trade Cancellation Act, p. 2.

[155] **RS-86**, Koch Comment on Bill 4, Cap and Trade Cancellation Act, p.1.

89. KS&T also wrote letters to the Attorney General of Ontario and to the Premier's Office, stating that "Koch supports the repeal of the cap and trade program and the carbon tax, but there are potentially unintended consequences in Bill 4, as it presently reads."[156] In its comments and correspondence, Koch asked that Ontario provide compensation to "any market participant related to and acting for, on behalf of, or in relation to a mandatory participant".[157] KS&T too advocated for a distinction between market participants on the basis that they were acting on behalf of a mandatory participant.[158] However, the cap and trade program established under the *Climate Change Act* contemplated no such category.

90. On November 15, 2018, the Ministry published a "decision summary" responding to concerns raised during the consultation period, including the non-eligibility of market participants for compensation.[159] Concerning this ineligibility of market participants, the Ministry explained that "[t]he compensation approach recognizes that regulated participants may have purchased allowances to comply with the regulation whereas market participants without a compliance obligation chose to take risks as market traders and speculators."[160] Moreover, it emphasized that the government received a strong mandate from the people of Ontario to cancel the cap and trade program.[161]

3. The *Cancellation Act* Comes into Force

91. As Bill 4 proceeded through the legislative and public consultation processes, several changes were made. These changes included: "ensuring that free allowances were deducted once (rather than

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[156] **C-114**, Letter from KS&T to the Attorney General of Ontario, 24 October 2018, p. 1; **C-115**, Letter from KS&T to the Premier's Office, 24 October 2018, p. 1.

[157] **RS-86**, Koch Comment on Bill 4, Cap and Trade Cancellation Act, p. 3; **C-114**, Letter from KS&T to the Attorney General of Ontario, 24 October 2018, p. 2; **C-115**, Letter from KS&T to the Premier's Office, 24 October 2018, p. 2.

[158] **C-114**, Letter from KS&T to the Attorney General of Ontario, 24 October 2018, p. 2; **C-115**, Letter from KS&T to the Premier's Office, 24 October 2018, p. 2. Premier Ford responded by to Koch Industries by letter, explaining that Ontario chose to replace the cap and trade program with a new approach to address the challenges of climate change. **C-116**, Letter from Premier Doug Ford to Koch Industries, 5 November 2018.

[159] **C-12**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018.

[160] **C-12**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018, p. 5. The Ontario Government also did not adopt a suggestion to require capped entities to purchase emission allowances because that would have imposed additional costs on participants in the cap and trade program, as Mr. Wood explains. **RWS-1**, Wood – Witness Statement, ¶ 21.

[161] **C-12**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018, p. 3.

twice) when calculating the amount of compensation", "removing duplication in regulation making authority", and "clarifying the regulation-making authority for prescribing amounts of compensation."[162] The final form of Bill 4 – the ***Cancellation Act*** – received Royal Assent on October 31, 2018.[163]

92. Key features of the *Cancellation Act* included (a) the retirement and cancellation of emission allowances,[164] (b) the compensation for cancelled emission allowances for eligible participants,[165] (c) the immunity of the Crown in respect of the winding down of cap and trade,[166] and (d) the establishment of a new made-in-Ontario environmental plan to fight climate change.[167]

a) Emission Allowances Are Retired or Cancelled Based on a Participant's Greenhouse Gas Emissions

93. As explained by Mr. Wood, the *Cancellation Act* provided that emission allowances held by capped participants would be matched with GHG emissions attributed to them as of July 3, 2018. Allowances that matched attributed emissions of GHG would be retired. The remaining allowances would be cancelled.[168] The *Cancellation Act* stated that attribution of GHG emissions to participants would be governed by regulations.[169] Regulation 390/18 created a new obligation for capped participants to submit reports by October 1, 2018 for their GHG emissions between January 1 and July 3, 2018.[170] Under the *Compensation Regulation*, the total amount of GHG emissions attributed to a participant would be the sum of (i) the participant's reported emissions for 2017 and (ii) the

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[162] **C-12**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018, p. 2.

[163] **R-59**, *Cancellation Act, 2018, S.O. 2018, c. 13* ("*Cancellation Act*").

[164] **R-59**, *Cancellation Act*, ss. 6, 7.

[165] **R-59**, *Cancellation Act*, s. 8.

[166] **R-59**, *Cancellation Act*, ss. 9, 10.

[167] **R-59**, *Cancellation Act*, ss. 3, 4, 5.

[168] **RWS-1**, Wood – Witness Statement, ¶¶ 19, 20 and 22.

[169] **R-59**, *Cancellation Act*, s. 2(1): "For the purposes of this Act, the amount of all greenhouse gas emissions attributed to a participant is the amount prescribed by the regulations or determined in accordance with the regulations."

[170] **R-60**, *Greenhouse Gas Emissions: Quantification, Reporting and Verification*, O. Reg. 390/18, ss. 10(3), 13(3). Previously, participants were required to submit their annual GHG emissions reports by June 1 of the following year (i.e. participants had to submit their reports for GHG emissions in 2017 by June 1, 2018). **RS-48**, Regulation 143/16, s. 24.

participant's reported emissions for the period from January 1, 2018 to July 3, 2018.[171] GHG emissions attributed to a participant were then used as the basis for retiring and cancelling cap and trade instruments.[172]

94. Under the *Cancellation Act*, "eligible instruments" meant those emission allowances or credits in the CITSS accounts of participants as of July 3, 2018 and "not classified with or assigned a vintage year of 2021."[173] Emission allowances were then retired in accordance with two scenarios, assessed as of July 3, 2018. First, if a participant held *fewer* emission allowances than necessary to match its GHG emissions from January 1, 2017 to July 3, 2018, all of its emission allowances were retired.[174] Second, if a participant held *more* emission allowances than necessary to match its GHG emissions, the number of instruments equivalent to that amount were retired and the remaining allowances were cancelled.[175] As described below, participants were eligible to receive compensation for cancelled emission allowances.[176]

b) The *Cancellation Act* Sets Out a Framework for Compensation

95. The *Cancellation Act* set out the framework for compensating certain categories of participants whose emission allowances were "cancelled", i.e. those participants who held purchased emission allowances in excess of their attributed emissions.[177]

96. No compensation was payable for cancelled emission allowances assigned a vintage year of

[171] **R-61**, *Compensation*, O. Reg. 9/19 ("Regulation 9/19"), s. 4(1).

[172] **RWS-1**, Wood – Witness Statement, ¶ 19.

[173] **R-59**, *Cancellation Act*, c. 13, ss. 1(1), 6(1).

[174] **R-59**, *Cancellation Act*, s. 6(2)(2).

[175] **R-59**, *Cancellation Act*, ss. 6(2)(1), 7(1).

[176] Under s. 71 of the *Climate Change Act*, auction funds had been recorded in the Greenhouse Gas Reduction Account (GGRA) and used only for purposes set out in the *Act*. **AW-4**, *Climate Change Act*, s. 71(1); *see also* **RWS-1**, Wood – Witness Statement, ¶ 31. Under the *Cancellation Act*, the GGRA was renamed as the Cap and Trade Wind Down Account. The remaining funds could only be used for authorized expenditures, including costs incurred in connection with the repeal of the *Climate Change Act*, compensation under s. 8 of the *Cancellation Act*, and costs in connection with certain initiatives that had previously been reviewed under the *Climate Change Act*. **AW-8**, *Cap and Trade Cancellation Act*, ss. 11(1),(2); *see also* **RWS-1**, Wood – Witness Statement, ¶ 32.

[177] **R-59**, *Cancellation Act*, ss. 7, 8.

2021 or for allowances distributed to participants free of charge.[178] In addition, the *Cancellation Act* stated that, "[u]nless otherwise provided by a regulation", no compensation was payable to the following categories of participants: (1) market participants; (2) electricity importers; (3) natural gas distributors; (4) operators of equipment related to the transmission, storage or transportation of natural gas; (5) suppliers of petroleum products; (6) operators of equipment for electricity transmission systems; and (7) electricity generators.[179]

97. These categories of participants were excluded from compensation for several reasons. While fuel suppliers and electricity importers had mandatory compliance obligations, they had been able to pass the cost of compliance to their customers.[180] Market participants had no compliance obligations[181] and chose to participate in the cap and trade program at their own risk. Ontario decided to offer compensation only to certain eligible capped participants that contributed to the goal of carbon abatement. As explained by Minister Phillips during the legislative debates pertaining to Bill 4, the *Cancellation Act* provided a "responsible and fair framework for compensation" which was built around whether an entity had compliance obligations to meet:

> Under the cap-and-trade program, capped participants were, by law, required to match allowances to the amount of greenhouse gases they emitted over a compliance period, for example 2017 to 2020. Our approach recognizes that regulated participants may have purchased allowances to comply with regulations, whereas market participants without a compliance obligation chose to take risks as market traders and speculators.[182]

98. In addition, the *Cancellation Act* set out the eligibility criteria for compensation in section 8 and the *Compensation Regulation* confirmed that only persons eligible under section 8 could apply

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[178] **R-59**, *Cancellation Act, 2018*, ss. 6(1)(b), 8(3), (4).

[179] **R-59**, *Cancellation Act*, *2018*, s. 8(5).

[180] **RWS-1**, Wood – Witness Statement, ¶ 25.

[181] **RWS-1**, Wood – Witness Statement, ¶ 25.

[182] **C-175**, Hansard Transcript, Legislative Assembly of Ontario, 31 July 2018, per Hon. Rod Phillips; *see also* per Belinda Karahalois: "As we work through the wind-down of the cap-and-trade carbon tax, the minister assures us that there will be a determination of potential compensation to ensure that Ontario taxpayers and consumers are protected, but such compensation will not be available for allowances where the costs associated with complying with this tax were passed on to consumers. That means that compensation would not be provided for allowances that were exported out of Ontario, for allowances allocated free of charge, or for allowances where the cost was recovered from consumers."

to obtain compensation.[183] The *Compensation Regulation* also set out the requirements of a valid application, which included submitting to the Minister: (i) verified reports concerning the participant's GHG emissions and (ii) a verification statement prepared by an accredited verification body in respect of each report.[184] Eligible participants had until February 14, 2019, to submit their applications for compensation in a form approved by the Minister.[185]

c) The *Cancellation Act* Includes a Crown Immunity Provision

99. Sections 69 and 70 of the *Climate Change* Act specified that there would be no right to compensation, no expropriation, and no amount payable by the Crown with respect to actions or inactions under the *Act*. Similarly, the *Cancellation Act* expressly limited compensation payable to the framework set out in section 8 of the *Act* and included a Crown immunity provision.

100. Section 9 of the *Cancellation Act* stated that there would be no compensation for participants following the wind-down of the cap and trade program, except as set out in section 8 of the *Act*:

> Except as set out in section 8, no person is entitled to any compensation or damages in respect of the value of cap and trade instruments retired or cancelled under this Act or for any other loss, including loss of revenues or loss of profits, related, directly or indirectly, to the enactment of this Act, the making or revocation of any regulation under this Act, the repeal of the *Climate Change Mitigation and Low-carbon Economy Act, 2016* or the making or revocation of any regulation under that Act.[186]

101. The *Cancellation Act* also included a Crown immunity provision. Section 10(1) of the *Cancellation Act* provides that "[n]o cause of action arises against the Crown […] as a direct or indirect result of" actions with respect to the *Cancellation Act* or the *Climate Change Act*, as well as "the retirement or cancellation of any cap and trade instrument"[187] or "any act or omission related to

[183] **R-61**, Regulation 9/19, s. 5: "A participant who is eligible to receive compensation under section 8 of the Act may apply to the Minister for compensation […]".

[184] **R-61**, Regulation 9/19, s. 5.

[185] **R-61**, Regulation 9/19, s. 6.

[186] **R-59**, *Cancellation Act, 2018*, s. 9.

[187] **R-59**, *Cancellation Act, 2018*, s. 10(1)(d).

the wind down of the cap and trade program"[188]. In addition, section 10(2) states that "[n]o proceeding, including but not limited to any proceeding for a remedy in contract, restitution, tort, misfeasance, bad faith, trust or fiduciary obligation, and any remedy under any statute, that is directly or indirectly based on or related to anything referred to in subsection (1) may be brought or maintained against the Crown […]".

d) The Government Adopts a New Environmental Plan

102. The *Cancellation Act* not only set out the framework for the winding down of Ontario's cap and trade program, but was also instrumental in the development of a new solution to the challenges posed by climate change.[189] The *Cancellation Act* required the Minister to prepare, with the approval of the Lieutenant Governor in Council, a climate change plan and to produce and share with the public regular reports in respect of the plan.[190]

103. On November 29, 2018 the Government of Ontario released its plan to "reduce greenhouse gas emissions and helping communities and families prepare for climate change".[191] The plan was open for a 60-day period of public consultation.[192] When introducing the plan, Minister Phillips stated that the Government of Ontario understood "the pressure Ontarians feel with rising costs of living as well as skyrocketing energy costs that have hurt our economy and our competitiveness", and that "a cap-and-trade program or carbon tax that seeks to punish people for heating their home or driving their cars remains unacceptable to the people of Ontario."[193]

104. The new plan included several elements for addressing the challenges posed by climate change. One element, "make polluters accountable", proposed that Ontario create and establish

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[188] **R-59**, *Cancellation Act, 2018*, s. 10(1)(e).

[189] *See* **C-111**, Ontario Government News Release, Ontario Introduces Legislation to End Cap and Trade Carbon Tax Era in Ontario, 25 July 2018: "The proposed legislation will also include measures to help replace the cap-and-trade carbon tax with a better plan for achieving real environmental goals."

[190] **R-59**, *Cancellation Act, 2018*, ss. 4(1) and 5(1).

[191] **R-62**, Ontario, Preserving and Protecting our Environment for Future Generations: A Made-in-Ontario Environment Plan, 29 November 2018, p. 2 ("2018 Environment Plan").

[192] **R-63**, Ontario, News Release, "Ontario Releases Plan to Protect the Environment", 29 November 2018.

[193] **R-62**, 2018 Environment Plan, p. 3.

emission performance standards to achieve greenhouse gas emissions reductions from large emitters.[194] An emissions performance standard (**EPS**) establishes emission levels that industrial facilities are required to meet and is tied to their level of output or production. As of January 1, 2022, each large industrial emitter is required to demonstrate compliance on a regular basis. This system is Ontario's alternative to the federal carbon pricing system. As explained by Mr. Wood, "It is meant to reward innovation amongst large industrial emitters in Ontario. Unlike the cap and trade program, the EPS does not impose a blanket cap on emissions in Ontario, but rather represents a tailored approach to reducing greenhouse gas emissions created by large industrial polluters in the province."[195]

4. KS&T Applies for Compensation Despite Its Ineligibility

105. On February 14, 2019, KS&T submitted an application for compensation.[196] One of the fields on the form asked the applicant to confirm that it was "eligible to apply for compensation under s.8 of the *Cap and Trade Cancellation Act*"."[197] KS&T – undisputedly registered as a "market participant" and thus ineligible for compensation[198] – nevertheless indicated that it fulfilled this criterion.[199] In its application for compensation, KS&T argued that it had registered to participate in the Ontario's cap and trade program in order to assist Koch-affiliated companies in California with meeting their compliance obligations, and that it should therefore not be treated as a market participant for the purposes of compensation.[200]

106. As set out in Section II.C.4, KS&T did not meet the eligibility criteria set out in the *Cancellation Act* and Compensation Regulation.[201] On March 4, 2019, Ontario sent a "Proposed

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[194] **R-62**, 2018 Environment Plan, pp. 25-26.

[195] **RWS-1**, Wood – Witness Statement, ¶ 35.

[196] **C-127**, KS&T Compensation Application Form, 14 February 2019.

[197] **C-127**, KS&T Compensation Application Form, 14 February 2019.

[198] **RWS-2**, Ramlal – Witness Statement, ¶ 38; **NR-13**, KS&T Participant Registration Form, [redacted] [redacted].

[199] **C-127**, KS&T Compensation Application Form, 14 February 2019.

[200] **C-127**, KS&T Compensation Application Form, 14 February 2019.

[201] **C-117**, Letter from Minister Rod Phillips to Koch Industries, 18 February 2019.

Determination" to KS&T, explaining that, in accordance with the *Cancellation Act* and the Compensation Regulation, KS&T was not eligible for compensation because it was registered in the Ontario cap and trade program as a "market participant".[202] In response, on March 11, 2019, KS&T asked the Ministry to reconsider and "compensate Koch for the full volume of allowances procured in the May 2018 WCI auction."[203] In support of this request, KS&T repeated its earlier assertion that it was "in effect, participating as a mandatory participant on behalf of its corporate affiliates".[204]

107. On March 14, 2019, Ontario issued its "Final Determination" explaining once again that, in accordance with the *Cancellation Act* and the Compensation Regulation, KS&T was not eligible for compensation because it was registered in the Ontario's cap and trade program as a market participant.[205] It is undisputed that KS&T was registered as a market participant in the Ontario cap and trade program and that the *Climate Change Act* did not provide for a separate category of market participants whose affiliates had compliance obligations.

III. THE CLAIMANTS HAVE FAILED TO ESTABLISH THE JURISDICTION OF THE TRIBUNAL

108. The Claimants' claims must be rejected for lack of subject-matter jurisdiction. The Claimants bear the burden of establishing the Tribunal's jurisdiction (**Section A**) under both the ICSID

[202] **C-128**, Letter from the Ministry of the Environment, Conservation and Parks to KS&T, 4 March 2019: "I have reviewed your application and determined in accordance with the provisions in the CTCA and the Regulation that Koch Supply & Trading, LP is not eligible to receive compensation. Koch Supply & Trading, LP was registered under the cap and trade program as a market participant within the meaning of the *Climate Change Mitigation and Low-carbon Economy Act, 2016*. Subsection 8(5) of the CTCA lists the types of participants that are not eligible to receive compensation. In particular, subparagraph 1 of subsection 8(5) specifically states that entities that were registered as a market participant under the cap and trade program are not eligible to receive compensation."

[203] **C-130**, Letter from KS&T to Ministry of the Environment, Conservation and Parks, 11 March 2019, p. 2.

[204] **C-130**, Letter from KS&T to Ministry of the Environment, Conservation and Parks, 11 March 2019, p. 1.

[205] **C-10**, Letter from the Ministry of the Environment, Conservation and Parks to KS&T, 14 March 2019: "It has been determined after considering these comments and in accordance with the provisions of the *Cap and Trade Cancellation Act, 2018* (CTCA) and the Regulation that Koch Supply & Trading, LP is not eligible to receive compensation. Koch Supply & Trading, LP was registered under the Cap and Trade program as a market participant within the meaning of the *Climate Change Mitigation and Low-carbon Economy Act, 2016*. Subsection 8(5) of the CTCA lists the types of participants that are not eligible to receive compensation. In particular, subparagraph 1 of subsection 8(5) specifically states that entities that were registered as a market participant under the Cap and Trade program are not eligible to receive compensation."

Convention and the NAFTA[206] (**Section B**). The Claimants have fallen far short, as Canada explains in **Section C** (ICSID Convention) and **Section D** (NAFTA). Canada also shows that the Tribunal lacks personal jurisdiction over Koch Industries under NAFTA Article 1116(1) (**Section E**).

A. The Claimants Bear the Burden of Proving that the Tribunal Has Jurisdiction

109. It is "an accepted principle of international law that the claimant in an arbitration bears the legal burden of showing that the tribunal has jurisdiction to consider its claim."[207] The *Perenco v. Ecuador* tribunal noted that "[t]he burden of proof to establish the facts supporting its claim to standing lies with the Claimant."[208] If a jurisdictional objection is raised by the respondent, the onus is on the claimant to show that jurisdictional requirements have been satisfied.[209] If there is any ambiguity as to whether or not a claimant has met its burden, the tribunal should decline jurisdiction.[210]

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[206] **CL-2**, *North American Free Trade Agreement*, 17 December 1994, (1993) 32 I.L.M. 289, 605 ("NAFTA").

[207] **RL-1**, *Sergei Viktorovich Pugachev v. The Russian Federation* (UNCITRAL) Award on Jurisdiction, 18 June 2020 ("*Pugachev – Award on Jurisdiction*"), ¶ 248. *See also* **CL-45**, *Bayindir Insaat Turizm Ticaret Ve Sanayi AS v. Islamic Republic of Pakistan* (ICSID Case No. ARB/03/29) Decision on Jurisdiction, 14 November 2005 ("*Bayindir – Decision on Jurisdiction*"), ¶¶ 190 and 192: "In accordance with accepted international (and general national) practice, a party bears the burden of proving the facts it asserts. In *Impregilo*, the tribunal took it for granted that the Claimant had to satisfy 'the burden of proof required at the jurisdictional phase' and make 'the prima facie showing of Treaty breaches required by ICSID Tribunals'. […] In the Tribunal's understanding, […] Bayindir has the burden of demonstrating that its claims fall within the Tribunal's jurisdiction."

[208] **RL-2**, *Perenco Ecuador Limited v. Republic of Ecuador and Empresa Estatal Petróleos del Ecuador* (ICSID Case No. ARB/08/6) Decision on Jurisdiction, 30 June 2011 ("*Perenco – Decision on Remaining Issues of Jurisdiction and on Liability*"*)*, ¶ 98. *See also* **RL-3**, *Vito G. Gallo v. The Government of Canada* (UNCITRAL) Award, 15 September 2011, ¶ 277: "[T]he maxim 'who asserts must prove', or *actori incumbit probatio*, applies also in the jurisdictional phase of this investment arbitration: a claimant bears the burden of proving that he has standing and the tribunal has jurisdiction to hear the claims submitted. If jurisdiction rests on the existence of certain facts, these must be proven at the jurisdictional stage – only the alleged violations of the treaty affording jurisdiction (in this case the NAFTA) can be accepted pro tem."

[209] **RL-4**, *Tulip Real Estate Investment and Development Netherlands B.V. v. Republic of Turkey* (ICSID Case No. ARB/11/28) Decision on Bifurcated Jurisdictional Issue, 5 March 2013, ¶ 48: "As a party bears the burden of proving the facts it asserts, it is for Claimant to satisfy the burden of proof required at the jurisdictional phase." *See also* **RL-5**, *National Gas S.A.E. v. Arab Republic of Egypt* (ICSID Case No. ARB/11/7) Award, 3 April 2014, ¶ 118; **RL-6**, *Spence International Investments, LLC, Berkowitz, et al. and others) v. Republic of Costa Rica* (ICSID Case No. UNCT/13/2) Interim Award (Corrected), 30 May 2017, ¶ 239.

[210] **RL-7**, *ICS Inspection and Control Services Limited (U.K.) v. The Argentine Republic* (UNCITRAL) Award on Jurisdiction, 10 February 2012, ¶ 280: "The burden of proof for the issue of consent falls squarely on a given claimant who invokes it against a given respondent. Where a claimant fails to prove consent with sufficient certainty, jurisdiction will be declined."

110. Pursuant to NAFTA Article 1122(1), each NAFTA Party consents to arbitration only "in accordance with the procedures set out in this Agreement." As explained by the tribunal in *Methanex*:

> 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.[211]

111. The Claimants bear the burden to demonstrate that that this dispute falls within the scope of the ICSID Convention and NAFTA Chapter Eleven. They have failed to do so.

B. The Claimants Must Establish Jurisdiction Under Both the ICSID Convention and NAFTA Chapter Eleven

112. Canada and the Claimants agree that this Tribunal's jurisdiction must be established under both Article 25 of the ICSID Convention and NAFTA Chapter Eleven.[212] Amongst other things, the

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[211] **RL-8**, *Methanex Corporation v. United States of America* (UNCITRAL) Partial Award, 7 August 2002 ("*Methanex – Partial Award*"), ¶ 120. *See also* **CL-52**, *William Ralph Clayton, William Richard Clayton, Douglas Clayton, Daniel Clayton and Bilcon of Delaware, Inc. v. Canada* (UNCITRAL) Award on Jurisdiction and Liability, 17 March 2015, ¶ 229: referring to Art. 1116(2) and 1117(2): "The heightened protection given to investors from other NAFTA Parties under Chapter Eleven of the Agreement must be interpreted and applied in a manner that respects the limits that the NAFTA Parties put in place as integral aspects of their consent." *See also* **RL-1**, *Pugachev – Award on Jurisdiction*, ¶ 252: "[The claimant] must proffer evidence to establish the facts that support his claims with respect to jurisdiction. This implies, *inter alia*, submitting appropriate means of evidence to prove compliance with each of the Treaty's requirements."

[212] Claimants' Memorial, ¶ 1. *See* **RL-9**, Christoph Schreuer, "The ICSID Convention: A Commentary", 2nd ed (Cambridge University Press, 2009) ("Schreuer: The ICSID Convention: A Commentary"), Art. 25, ¶ 124. This is also known as the "double keyhole" approach or "double barreled" test. *See also* **RL-10**, *Aguas del Tunari, S.A., v. Republic of Bolivia* (ICSID Case No. ARB/02/3) Decision on Respondent's Objections to Jurisdiction, 21 October 2005 ("*Aguas – Decision on Respondent's Objections to Jurisdiction*"), ¶ 278: "The state parties to the BIT can seek to encompass all manner of disputes. But in attempting to place disputes under their BIT before ICSID, an institution regulated by a separate instrument, the scope of the disputes which may be submitted is necessarily limited to those disputes that pass through the jurisdictional keyhole defined by Article 25."; **RL-11**, *Venezuela Holdings B.V. and others v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB/07/27) Decision on Jurisdiction, 10 June 2010, ¶ 156: "The Tribunal observes that Article 25 fixes the 'outer limits' of ICSID jurisdiction and that parties can consent to that jurisdiction only within those limits."; **RL-12**, *Toto Costruzioni Generali S.p.A. v. Lebanese Republic* (ICSID Case No. ARB/07/12) Decision on Jurisdiction, 11 September 2009, ¶¶ 66: "[F]or this Tribunal to have jurisdiction, it is not sufficient that the dispute arises out of an investment as per the meaning of 'investment' given by the parties in the Treaty, but also as per the meaning of 'investment' under the ICSID Convention."; **RL-10**, *Aguas – Decision on Respondent's Objections to Jurisdiction*, ¶ 278: "[T]he scope of disputes which may be submitted [under the ICSID Convention] is necessarily limited to those disputes that pass through the jurisdictional keyhole defined by Article 25."; **RL-22**, *TSA Spectrum de Argentina S.A. v. Argentine Republic* (ICSID Case No. ARB/05/5) Award, 19 December 2008, ¶ 134: "Article 25 of the ICSID

Claimants must establish that the impugned measures relate to the Claimants' alleged "investment" in the territory of Canada and that the present dispute arises directly out of that "investment".

113. Article 25(1) of the ICSID Convention provides that:

> The jurisdiction of the Centre shall extend to *any legal dispute arising directly out of an investment*, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.[213]

114. In a number of well-known cases, tribunals have articulated "objective criteria" for the definition of the term "investment" that flow from the object and purpose of the ICSID Convention.[214] These criteria cannot be set aside by a consent given in another legal instrument, such as a bilateral investment treaty (**BIT**).[215]

115. The tribunal in *Joy Mining v. Egypt* considered that:

> The fact that the Convention has not defined the term investment does not mean, however, that anything consented to by the parties might qualify as an investment under the Convention. The Convention itself, in resorting to the concept of investment in connection with jurisdiction, establishes a framework to this effect: jurisdiction cannot be based on something different or entirely unrelated. In other words, it means that there is a limit to the freedom with which the parties may define an investment if they wish to engage the jurisdiction of ICSID tribunals.
>
> The parties to a dispute cannot by contract or treaty define as investment, for the purpose of ICSID jurisdiction, something which does not satisfy the *objective requirements* of Article 25 of the Convention. Otherwise Article 25 and its reliance on the concept of investment, even if not specifically defined, would be turned into

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Convention defines the ambit of ICSID's jurisdiction. In other words, it defines the extent, hence also the objective limits, of this jurisdiction (including the jurisdiction of tribunals established therein) which cannot be extended or derogated from even by agreement of the Parties."

[213] **RL-13**, ICSID Convention, Regulations and Rules, ICSID, D.C.: International Centre for Settlement of Investment Disputes, 2003, Art. 25(1) (emphasis added).

[214] *See* **RL-14**, *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic* (ICSID Case No. ARB/13/8) Award, 9 April 2015 ("*Postova Banka – Award*"), ¶ 353.

[215] *See* **RL-14** *Postova Banka – Award*, ¶ 353.

a meaningless provision.[216]

116. The Claimants must establish both that that the present dispute arises directly out of an "investment" within the meaning of Article 25 of the ICSID Convention and that the impugned measures related to the Claimants' "investment" in the territory of Canada within the meaning of NAFTA Chapter Eleven.

C. The Claimants' Activities Do Not Constitute an "Investment" Within the Meaning of Article 25 of the ICSID Convention

117. The parties agree that for there to be an "investment" under the ICSID Convention, the criteria articulated in *Salini v. Morocco* must be met, notably (1) contribution of money or assets; (2) of a certain duration; (3) an element of risk; and (4) a contribution to the economic development of the host State.[217] The Claimants have failed to establish that they meet the requirements of an "investment" under Article 25 of the ICSID Convention.

1. The Claimants Have Not Made a Contribution of Money or Assets

118. In order to qualify as an "investment", there must be "a contribution of money or other assets of economic value".[218] As the *Postova Banka v. Greece* tribunal explained, the contribution must be to an economic venture, which is distinct from a sale that does not qualify as an "investment": "[i]f an 'objective' test is applied, in the absence of *a contribution to an economic venture*, there could be

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[216] **CL-41**, *Joy Mining Machinery Limited v. The Arab Republic of Egypt* (ICSID Case No. ARB/03/11) Award on Jurisdiction, 6 August 2004, ¶¶ 49-50 (emphasis added). *See also* **CL-39**, *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco [I]* (ICSID Case No. ARB/00/4) Decision on Jurisdiction, 23 July 2001 ("*Salini – Decision on Jurisdiction*"), ¶ 44; **CL-40**, *Jan de Nul N.V. and Dredging International N.V. v. Arab Republic of Egypt* (ICSID Case No. ARB/04/13) Decision on Jurisdiction, 16 June 2006 ("*Jan de Nul – Decision on Jurisdiction*"), ¶ 90; **RL-15**, *Patrick Mitchell v. Democratic Republic of Congo* (ICSID Case No. ARB/99/7) Decision on the Application for Annulment of the Award, 1 November 2006, ¶ 31; **RL-16**, *Ioannis Kardassopoulos v. The Republic of Georgia* (ICSID Case No. ARB/05/18) Decision on Jurisdiction, 6 July 2007, ¶ 113; **RL-17**, *El Paso Energy International Company v. Argentine Republic* (ICSID Case No. ARB/03/15) Award, 31 October 2011 ("*El Paso – Award*"), ¶ 142; **CL-47**, *Phoenix Action, Ltd. v. The Czech Republic* (ICSID Case No. ARB/06/5) Award, 15 April 2009, ¶ 96; **RL-18**, *Vladislav Kim and others v. Republic of Uzbekistan* (ICSID Case No. ARB/13/6) Decision on Jurisdiction, 8 March 2017, ¶ 242. **RL-19**, *Koch Minerals Sarl and Koch Nitrogen International Sarl v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB/11/19) Award, 30 October 2017 ("*Koch Minerals – Award*"), ¶ 6.50.

[217] Claimants' Memorial, ¶ 330 citing **CL-39**, *Salini – Decision on Jurisdiction*, ¶ 52.

[218] *See, e.g.,* **CL-46**, *Saipem S.p.A. v. People's Republic of Bangladesh* (ICSID Case No. ARB/05/07) Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007 ("*Saipem – Decision*"), ¶ 99.

no investment. An investment, in the economic sense, is linked with a process of creation of value, which distinguishes it clearly from a sale".[219] The tribunal further noted that "[i]n a sale there is also a contribution of goods or services by the seller and a contribution of money by the buyer, but this is different from the contribution to an economic venture required in order to find an investment."[220]

119. The Claimants argue that they have committed funds in Ontario by acquiring emission allowances at auction and participating in Ontario's program as a market participant.[221] KS&T also characterizes its "business strategy" of buying "wholesale" in Ontario for resale in the "retail" market as committing capital to Ontario.[222] In reality, KS&T's strategy of buying emission allowances in Ontario for resale in California, without any local presence or personnel in Ontario, contributed nothing of value to an economic venture in Ontario.

120. KS&T, a Delaware entity, had no subsidiary, office, or personnel in Ontario. The two individuals responsible for KS&T's Ontario CITSS account were Mr. Paul Brown and Mr. Sam Power. Mr. Porter was based in Wichita, Kansas.[223] Mr. Paul Brown was not even an employee of KS&T.[224] Mr. Graeme Martin, who "was primarily responsible for building relationships with potential customers and counterparties in the Ontario cap and trade market", was based in Houston, Texas.[225]

121. KS&T participated in the Ontario cap and trade program as a market participant. Its sole economic "contribution" was the purchase of emission allowances when it was successful at bidding in auctions. KS&T's characterization of its role as "vital" to the program is unsupported. KS&T was not required to register in the Ontario cap and trade program, nor did the system require its

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[219] **RL-14**, *Postova Banka – Award*, ¶ 361.

[220] **RL-14**, *Postova Banka – Award*, FN 506.

[221] Claimants' Memorial, ¶ 331, alleging that the Claimants "have committed in excess of USD 84 million in investing in Ontario's Cap and Trade Program, in addition to its vital contributions to the effective functioning of the Program as a market participant."

[222] Claimants' Memorial, ¶ 126.

[223] **RWS-2**, Ramlal – Witness Statement, ¶ 41; **NR-13**, KS&T Participant Registration Form, [redacted] s. 4.0.

[224] Claimants' Memorial, ¶ 132; **CWS-3**, Brown - Witness Statement, ¶ 7.

[225] **CWS-2**, Martin – Witness Statement, ¶ 6.

participation to function and accomplish the policy goal of reduction in GHG emissions.[226] KS&T's participation in the secondary market in Ontario amounted to a total of ███ ███.[227] The Claimants failed to explain how ███ were "linked with a process of creation of value" in Ontario.[228] Any sale or purchase of emission allowances between KS&T and an Ontario-registered participant simply meant that the buyer acquired a number of limited authorizations to emit GHGs without penalty and, in exchange, the seller received money.

122. In sum, the Claimants have failed to demonstrate that they made a contribution to an economic venture in Canada that would qualify as an "investment". KS&T paid money to acquire emission allowances at auction, which were bought by KS&T through its Ontario CITSS accounts ███.[229] There is no evidence of contribution by KS&T to compliance obligations of related entities in Ontario.[230]

2. The Claimants Have Not Met the "Certain Duration" Requirement

123. The Claimants argue that duration "is a very flexible term" that "could be anything from a couple of months to many years", and that they "hav[e] spent several years investing in Ontario's Cap and Trade Program from 2016 to 2018."[231]. Some tribunals and commenters have indicated that a duration of two to five years is required.[232] Here, there is no need to set a specific minimum duration:

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[226] **RER-2**, Litz – Expert Report, ¶ 27.

[227] *See above*, ¶¶ 52, 66.

[228] *See* **RL-14**, *Postova Banka – Award*, ¶ 361 and FN 506.

[229] On ███ KS&T transferred the ███ of its Ontario CITSS account to its California CITSS account. **RWS-2**, Ramlal – Witness Statement, ¶ 52 and Attachment 1, ███. In ███, KS&T again transferred the ███ of its Ontario CITSS account to its California account. **RWS-2**, Ramlal – Witness Statement, ¶ 54 and Attachment 1, ███.

[230] **RWS-2**, Wood – Witness Statement, ¶ 13.

[231] Claimants' Memorial, ¶ 332.

[232] **CL-40**, *Jan de Nul – Decision on Jurisdiction*, ¶ 93: "In response to a specific question by the Tribunal at the hearing on jurisdiction […], both parties expressed the opinion that an operation may be characterized as an investment if it lasts at least two years."; **CL-49**, *KT Asia – Award*, ¶¶ 208: "Cases have held that projects with a minimum duration between two and five years satisfied the duration element. Like other tribunals, this one considers that '[d]uration is to be analysed in light of all the circumstances, and of the investor's overall commitment';" and ¶ 214: pointing out that the time from the acquisition of the shares until the request for arbitration "would *only be 16 months, which is a very short time* if one remembers the five years tentatively put forward in the course of the elaboration of the ICSID Convention." (emphasis

KS&T's participation in Ontario's cap and trade program fails to meet the duration requirement based on KS&T's stated intent and the nature of the transaction at issue.

124. KS&T acquired emission allowances with the intention of transferring them to California as soon as possible for resale in that jurisdiction. Indeed, KS&T moved [redacted] emission allowances from its Ontario CITSS account to its California CITSS account [redacted] such transfers became permitted on January 1, 2018.[233] Following the February 2018 auction, KS&T again moved [redacted] emission allowances from its Ontario CITSS account to its California CITSS account.[234] KS&T also intended to transfer [redacted] emission allowances from the May 15, 2018 auction to California for sale in the near term.[235] Moreover, the purchase of a item for resale is inherently limited in time.[236]

3. The Claimants Have Not Undertaken an Investment Risk

125. The Claimants argue that "an element of risk is inherent in any long-term investment"[237] and that they "exposed themselves to financial risk in order to develop KS&T as a profitable enterprise in Ontario over the long-term, including participating in auctions and on the secondary market, while

added); **RL-9**, Schreuer: The ICSID Convention: A Commentary, Art. 25, ¶ 162. *See, e.g.*, **CL-39**, *Salini – Decision on Jurisdiction*, ¶ 54: "The transaction, therefore, complies with the minimal length of time upheld by the doctrine, which is from 2 to 5 years."

[233] **RWS-2**, Ramlal – Witness Statement, ¶ 52 and Attachment 1, [redacted]

[234] **RWS-2**, Ramlal – Witness Statement, ¶ 54 and Attachment 1, [redacted]

[235] Claimants' Memorial, ¶¶ 164-165, 496: "KS&T had planned to use at least [redacted] of the carbon allowances it purchased in the May 2018 joint auction to meet its existing contractual obligations [redacted] **C-127**, KS&T Compensation Application Form, 14 February 2019; **C-73**, [redacted] *See also* **CL-49**, *KT Asia – Award*, ¶ 213: "[I]n the Tribunal's view the transfer of the ownership of shares in a company to KT Asia on an intended short-term basis in order to then sell it on to a third party does not support the finding that KT Asia had any intention to hold an investment in BTA Bank for any material time."

[236] *See* **CL-45**, *Bayindir – Decision on Jurisdiction*, ¶ 132. *See also* **CL-49**, *KT Asia Investment Group B.V. v. Republic of Kazakhstan* (ICSID Case No. ARB/09/8) Award, 17 October 2013 ("*KT Asia – Award*"), ¶ 207: "An allocation of resources cannot be deemed an investment unless it is made for a certain duration. The element of duration is inherent in the meaning of an investment."

[237] **CL-39**, *Salini – Decision on Jurisdiction*, ¶ 56: "A construction that stretches out over many years, for which the total cost cannot be established with certainty in advance, creates an obvious risk for the Contractor"; **CL-45**, *Bayindir – Decision on Jurisdiction*, ¶ 136: "Besides the inherent risk in long-term contracts, the Tribunal considers that the very existence of a defect liability period of one year and of a maintenance period of four years against payment, creates an obvious risk for Bayindir."; **CL-46**, *Saipem – Decision*, ¶ 109: "In the present case, the undisputed stopping of the works […] and the necessity to renegotiate the completion date constitute examples of inherent risks in long-term contracts".

seeking to develop business and turn a profit."[238] The Claimants however fail to establish that KS&T was establishing an economic venture in Ontario over the long-term and that it undertook any risk in relation to that objective.

126. The *Postova Banka v. Greece* tribunal explained that, "any economic transaction […] entails some element of risk. Risk is inherent in life and *cannot per se qualify what is an investment*."[239] The tribunal noted in particular that:

> [C]ommercial and sovereign risks are distinct from operational risk. The distinction here would be between a risk inherent in the investment operation in its surrounding – meaning that the profits are not ascertained but depend on the success or failure of the economic venture concerned – and all the other commercial and sovereign risks.[240]

127. KS&T bore a commercial risk: it bought emission allowances at auction, betting that it could resell them at a higher price in another jurisdiction. It also accepted the risks inherent in Ontario's cap and trade program, which contemplated changes to the program without compensation. KS&T cannot now complain that its inability to complete a cross-border sale, and its ineligibility for compensation, contained any "investment" risk related to the objective of developing an economic venture in Ontario.

4. The Claimants Have Not Contributed to the Host State's Economic Development

128. In order to qualify as an "investment", a project "should be significant to the State's

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[238] Claimants' Memorial, ¶ 333.

[239] **RL-14**, *Postova Banka – Award*, ¶ 367 (emphasis added). *See also* **RL-20**, *Romak S.A. (Switzerland) v. The Republic of Uzbekistan* (UNCITRAL) Award, 26 November 2009, ¶¶ 229-230: "All economic activity entails a certain degree of risk. As such, all contracts – including contracts that do not constitute an investment – carry the risk of non-performance. However, this kind of risk is pure commercial, counterparty risk, or, otherwise stated, the risk of doing business generally. It is therefore not an element that is useful for the purpose of distinguishing between an investment and a commercial transaction. An 'investment risk' entails a different kind of *alea*, a situation in which the investor cannot be sure of a return on his investment, and may not know the amount he will end up spending, even if all relevant counterparties discharge their contractual obligations. Where there is 'risk' of this sort, the investor simply cannot predict the outcome of the transaction."

[240] **RL-14**, *Postova Banka – Award*, ¶ 370.

development."[241] The Claimants argue that they have "contributed substantially to Canada's economic development" because "investments like KS&T's raised a total of CAD 2.9 billion for Ontario."[242] This is a gross exaggeration by the Claimants. The relevant amount – the sum that Ontario received as proceeds from KS&T's purchase of emission allowances at the May 2018 auction – is less than USD [redacted][243]

129. In addition, the mere fact that KS&T purchased emission allowance in Ontario does not mean that KS&T made a contribution to the economic development of Ontario. Traders are not necessarily investors. As the tribunal in *Global Trading v. Ukraine* noted with respect to a contract for the cross-border sale of goods, "[t]he fact that the trade in these particular goods was *seen to further the policy priorities* of the purchasing State *does not bring about a qualitative change in the economic benefit* that all legitimate trade brings in its train."[244]

130. The Claimants have not met their burden of satisfying the requirements of Article 25 of the ICSID Convention. As a result, this Tribunal does not have jurisdiction *ratione materiae* and the Claimants' claim must be dismissed.

D. The Claimants Do Not Hold Protected "Investments" Under Article 1101 and Article 1139 of the NAFTA

131. Article 1101 sets out the "scope and coverage" of NAFTA Chapter Eleven. In order to establish the subject-matter jurisdiction of the Tribunal, the Claimants must prove that the dispute satisfies all the elements of Article 1101: "This Chapter applies to *measures adopted or maintained* by a Party relating to: […] (b) *investments* of investors of another Party *in the territory of the*

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[241] **CL-45**, *Bayindir – Decision on Jurisdiction*, ¶ 137: "Lastly, relying on the preamble of the ICSID Convention, ICSID tribunals generally consider that, to qualify as an investment, the project must represent a significant contribution to the host State's development. In other words, investment should be significant to the State's development."

[242] Claimants' Memorial, ¶ 334.

[243] In the May 2018 auction, KS&T acquired [redacted] emission allowances at the auction settlement price of USD 14.65 per allowance. Of those emission allowances, [redacted] had been created by Ontario and were transferred to KS&T's Ontario CITSS account from Ontario. By calculation, the total received in relation to those emission allowances was USD [redacted] *See* **RWS-2**, Ramlal – Witness Statement, ¶¶ 48, 57 and Attachment 1, [redacted]

[244] **RL-21**, *Global Trading Resource Corp. and Globex International, Inc. v. Ukraine* (ICSID Case No. ARB/09/11) Award, 1 December 2010, ¶ 56 (emphasis added).

Party".[245]

132. NAFTA Article 1139 defines the term "investment". Unlike other investment treaties containing an open-ended, illustrative list of covered investments, NAFTA Article 1139 contains an exhaustive enumeration of investments that are protected.[246] Article 1139 includes "a sophisticated and precise definition of protected investments" and "lists eight categories of 'interests' which are considered as investments, and two categories which are excluded."[247] Article 1139 makes clear that trade and non-investment assets, such as "claims to money that arise solely from: commercial contracts for the sale of goods or services […] and the extension of credit in connection with a commercial transaction […] and any other claims to money that do not involve the kinds of interests set in subparagraphs (a) through (h)", are specifically excluded from the scope of protected "investments" under NAFTA.[248]

133. The Claimants have failed to establish that they hold any "investments" within the subject-matter jurisdiction of the Tribunal. **Section 1** explains that emission allowances are not "property" under municipal law, and therefore fall outside the scope of Article 1139(g). **Section 2** demonstrates that KS&T did not hold qualifying "interests" arising out of the "commitment of capital or other

[245] **CL-2**, NAFTA, Art. 1101(b) (emphasis added). NAFTA Article 201 defines "measure" as including "any law, regulation, procedure, requirement or practice". The Claimants appear to challenge a public statement of Mr. Ford on June 15, 2018, prior to his swearing-in as Premier, as a "measure". Claimants' Request for Arbitration, 7 December 2020 ("Claimants' RFA"), ¶ 75(a). Such an announcement is not a "measure". Mr. Ford was not yet in power; and in addition, statements of future intent fall outside the scope of NAFTA Articles 201 and 1101. *See generally* **RL-23**, Meg Kinnear, Andrea Kay Bjorklund, et al., "Investment Disputes under NAFTA: An Annotated Guide to NAFTA Chapter 11, Supplement No. 1", (Kluwer Law International; Kluwer Law International 2006) ("Kinnear: Investment Disputes under NAFTA"), p. 1101-33: "The words 'adopted or maintained' suggest that the measures at issue in a claim under Chapter 11 must be or have been in some way in force. Arguably, the intention to create a measure is not sufficient, otherwise the parties would have included the concept of 'proposed measures,' as they did elsewhere in the agreement.".

[246] **CL-20**, *Grand River Enterprises Six Nations, Ltd., et.al. v. United States of America* (UNCITRAL) Award, 12 January 2011, ¶ 82: "NAFTA's Article 1139 is neither broad nor open-textured. It prescribes an exclusive list of elements or activities that constitute an investment for purposes of NAFTA."

[247] **RL-24**, *Lion Mexico Consolidated L.P. v. United Mexican States* (ICSID Case No. ARB(AF)/15/2) Decision on Jurisdiction, 30 July 2018 ("*Lion – Decision on Jurisdiction*"), ¶ 182. *See also* **CL-56**, *Mondev International Ltd. v. United States of America* (ICSID Case No. ARB(AF)/99/2) Award, 11 October 2002 ("*Mondev – Award*"), ¶ 79: "The Tribunal notes that Chapter 11 specifically addresses issues of standing and scope of application through a series of detailed provisions, most notably the definitions of "enterprise", "investment", "investment of an investor of a Party" and "investor of a Party" in Article 1139. These terms are used with care throughout Chapter Eleven.

[248] **CL-2**, NAFTA, Art. 1139(i), (j).

resources in the territory" of Canada. Finally, Koch Industries' allegation that a U.S. enterprise is an "investment" in Canada under Article 1139(a) is absurd and must be rejected, as must its invocation interests that are irrelevant to this claim under Article 1139(e) and (h), as discussed in **Section 3**.

1. The Emission Allowances Held by KS&T Were Not "Property" Under NAFTA Article 1139(g)

134. The Claimants have made only a perfunctory assertion that KS&T held intangible property rights in emission allowances under NAFTA 1139(g)[249], bypassing any analysis or explanation of the relevant domestic law on property. The emission allowances do not qualify as an "investment" as defined in Article 1139(g) because they are not "real estate or other property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes".

135. "Property" is not defined in the NAFTA. As a result, a tribunal examining whether there is a protected investment pursuant to Article 1139(g) must look to what constitutes "property" under Ontario law (**Section (a)**). As set out in the accompanying expert report of Professor Larissa Katz, the emission allowances are not "property" under Ontario law **(Section (b)**). Professor Katz's conclusion is consistent with the broader environmental policy context in which the emission allowances were created (**Section (c)**).

a) The Existence of Property Rights under Article 1139(g) is Determined with Reference to the Municipal Law of the Host State

136. Absent a definition in the NAFTA, in assessing whether the emission allowances are a protected "investment" under Article 1139(g), the Tribunal must first look to what constitutes "property" under the relevant municipal law.[250] Such a determination requires a case-by-case inquiry,

[249] Claimants' Memorial, ¶ 323(c).

[250] **CL-10**, *Emmis International Holding, B.V., Emmis Radio Operating, B.V. and MEM Magyar Electronic Media Kereskedelmi és Szolgàltatò v. Hungary* (ICSID Case No. ARB/12/2) Award, 16 April 2014 ("*Emmis – Award*"), ¶ 162: "Public international law does not create property rights. Rather, it accords certain protections to property rights created according to municipal law."; **RL-25**, Zachary Douglas, "Property, Investment and the Scope of Investment Protection Obligations", in Z. Douglas, J. Pauwelyn, J. Vinuales, The Foundations of International Investment Law: Bringing Theory into Practice (Oxford University Press, 2013) ("Douglas: Property, Investment and the Scope of Investment Protection Obligations"), ¶ 1.150: "International law is concerned with the modalities of the exercise of sovereign power; it does not purport to create, define or regulate private rights over any type of property, whether intangible or tangible."; **RL-26**, Muthucumaraswamy Sornarajah, "The International Law on Foreign Investment", 3rd ed. (Cambridge University Press, 2010) ("M. Sornarajah: The International Law on Foreign Investment"), p. 383, note 67: "There is no indication of a

involving an examination of the nature and extent of rights conferred under the State's domestic law.[251] This principle has been repeatedly affirmed by international tribunals.[252] Whether emission allowances can constitute an alleged "investment" under NAFTA Article 1139(g) is contingent upon their existence as property rights under Ontario law.

b) Emission Allowances Are Not Property Rights Under Ontario Law

137. Property law is a subject of provincial jurisdiction in Canada.[253] Ontario is a common law jurisdiction where the sources of law include legislation and prior case law.[254] In deciding questions regarding the existence of property rights, courts in Ontario will first look to whether a property right is defined by Ontario legislation. In the absence of a specific legislative declaration found in an Ontario statute that the emission allowances constitute property rights in Ontario, courts in Ontario would apply the common law to determine this question.[255]

138. Under the common law principle of *stare decisis*, judges in Ontario follow precedents of other judges in higher courts in the same province and the Supreme Court of Canada when treating the same legal question.[256] The question of whether emission allowances are "property" is a novel legal question that has yet to be considered by Ontario courts.[257]

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theory of property in international law itself. International law does not create property in an individual. It relies upon municipal law for the recognition of property rights."

[251] **RL-27**, Campbell McLachlan, Laurence Shore & Matthew Weiniger, "International Investment Arbitration: Substantive Principles" (Oxford University Press, 2007) ("McLachlan: Substantive Principles"), ¶ 8.64. "…it is for the host State law to define the nature and extent of property rights that a foreign investor can acquire."

[252] **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 231; **CL-10**, *Emmis – Award*, ¶¶ 161-162: to "determine whether an investor/claimant holds property or asserts capable of constituting an investment it is necessary in the first place to refer to host State law."; **RL-130**, *Cairn Energy PLC and Cairn UK Holdings Limited (CUHL) v. Republic of India* (UNCITRAL) Award, 21 December 2020, ¶ 649: "While an international treaty is by definition international law and its interpretation is governed by international law, it is not the only law relevant to the Tribunal's inquiry. As Professor Jan Paulsson has stated, "[a]n international treaty may provide for the protection of contracts, property, or other private-law rights, but international law does not define such rights; one must look to national law."

[253] **R-64**, *The Constitution Act, 1867*, s. 92(13) (excerpt).

[254] **R-65**, Government of Canada, "Where our Legal System Comes From".

[255] **RER-1**, Expert Report of Professor Larissa Katz, 17 February 2022 ("Katz - Expert Report"), ¶ 16.

[256] **RL-28**, J. Sebastian Winny, "Stare Decisis in Ontario Law", 35 ADVOC. Q. 68 (2008), pp. 68-69.

[257] **RER-1**, Katz - Expert Report, ¶ 16.

139. In her report, Professor Katz explains the methodology that an Ontario court would take to assess whether emission allowances are property rights in Ontario, based on the approach that the courts have taken with other novel property arguments.[258] Applying this methodology, Professor Katz concludes that emission allowances lack hallmark core characteristics of common law property rights in Ontario, including "exclusive control and use" (**section (i)**) and "stability" (**section (ii)**), among others.[259] In addition, as addressed below, characteristics such as value and tradeability – and reference to "commercial realities" – are not determinative of whether an interest is "property" under Ontario law (**section (iii)**).[260] Absent express legislative declaration, statutorily created interests such as emission allowances are not "property" if they lack the core characteristics required of property rights at Ontario common law.[261] Professor Katz concludes that the emission allowances do not demonstrate the "core common law characteristics of property rights" and therefore are not considered property rights in Ontario.[262]

(i) Exclusive control and use

140. Under Ontario common law, the property right holder must have exclusive control and use of the subject matter of the property right.[263] This right allows a property holder alone to determine how a "thing" is used, absent the interference of any other party. The Ontario Court of Appeal in *Bouckhuyt* held that: "The notion of 'property' imports the right to exclude others from the enjoyment

[258] **RER-1**, Katz - Expert Report, *see* Section 5.

[259] **RER-1**, Katz - Expert Report, ¶¶ 27-29, 32, 73. Professor Katz identifies exclusive control and use, certainty of subject matter, seperability, stability, locability, and contingency of value and tradability as those rights that bear on the question of whether environmental emission allowances count as property rights in Ontario. Based on her analysis of these characteristics, emission allowances would not count as property at Ontario law. Canada discusses "exclusive control and use" and "stability" in particular here.

[260] **R-66**, *Saulnier v Royal Bank of Canada*, [2008] 3 S.C.R. 166, 2008 SCC 58, ¶¶ 41-42

[261] The relevant common law is the common law in Ontario. This is because while common law jurisdictions share the core features of property at law, there is no consensus across common law jurisdictions about what new interests count as property rights. Professor Katz notes that: "Canadian courts tend to be more reluctant to expand the category of traditional property rights than courts may be in other common law jurisdictions." **RER-1**, Katz - Expert Report, ¶ 19.

[262] **RER-1**, Katz - Expert Report, ¶¶ 16, 83.

[263] **RER-1**, Katz - Expert Report, Section 5.2.

of, interference with or appropriation of a specific legal right."[264]

141. In *Bouckhuyt*, the Court of Appeal confirmed that the ability to exclude others from the enjoyment of, interference with or appropriation of a specific legal right, is a necessary incident of property.[265] Professor Katz states that "property rights are fundamentally *rights* that give the owner […] exclusive control over a thing or domain of human activity, protected against interference by others, including government."[266] When a party cannot prevent the government from withholding or revoking an interest, the party cannot "exclude" the government from controlling that interest, and thus it lacks the necessary core characteristic of exclusive control and use required of property in Ontario.

142. Professor Katz notes that "[e]mission allowances do not confer an ability to exclude others from interfering with a defined domain of activity, or to direct the activity of others in respect of a domain of activity."[267] Under section 27 of the *Climate Change Act,* both the Minister and the Director retained control to remove emission allowances in certain circumstances without being required to provide notice to registered participants.[268] Moreover, only registered participants could participate in auctions and account holders were restricted to trading with other registered or authorized participants. These factors are indicia of a restricted market, "tending to weaken the exclusive control even over the tradability of emission allowances as compared with other property-like intangibles."[269] Professor Katz further explains that "[i]n light of the statutory reservation of Ministerial powers under the Act and s. 70 of the Act (clarifying that the exercise of these powers

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[264] **R- 67**, *National Trust Co. v Bouckhuyt*, [1987] 23 O.A.C 40 (CA), ¶ 74. In **R-68**, *Del Giudice v. Thompson* 2021 ONSC 2206, ¶ 175, the court acknowledged the right to control as a key feature of intangible assets that count as property at common law.

[265] **R-69**, *Tucows.Com Co. v Lojas Renner S.A.*, 2011 ONCA 548, ¶ 63.

[266] **RER-1**, Katz - Expert Report, ¶ 28 (emphasis in original).

[267] **RER-1**, Katz - Expert Report, ¶ 67.

[268] **RER-1**, Katz - Expert Report, ¶ 68. **R-6**, *Climate Change Act*, ss. 27(1): "The Minister may, in accordance with the regulations, remove emission allowances and credits from a registered participant's cap and trade accounts in the circumstances specified in this Act and in such circumstances as may be prescribed.", and s. 27(3): "The Minister or the Director is not required to notify the registered participant before removing emission allowances and credits from the participant's cap and trade accounts, and the consent of the registered participant is not required."

[269] **RER-1**, Katz - Expert Report, ¶ 68.

would not amount to expropriation), the power to trade emission allowances is not itself a right to exclusive control over a domain of activity."[270]

143. Given the above, Professor Katz concludes that emission allowances within the cap and trade system lacked the requisite right of exclusive control necessary to count as property under the common law of Ontario.[271] This conclusion is bolstered by the fact that in undertaking such an analysis, Canadian courts adopt a cautious and constrained approach to the recognition of an interest as a property right, in particular in the context of government-individual relations.[272]

(ii) Stability

144. Stability is a core characteristic indicating the proprietary character of an interest. Under Ontario common law, property rights are not merely privileges at the discretion of another party; rather, they are stable enduring rights that can be enforced against others.[273] As Professor Katz explains, "[a] property right is stable to the extent that its existence does not depend on the discretion or choices of another."[274] Property rights are stable, durable rights whose existence does not depend solely on governmental policy choices.

145. Professor Katz explains that the control that government inherently retained over the cap and trade program itself and over climate policy more generally undermines a view of emission allowances as a stable, durable interest that is enforceable as of right against government.[275] Indeed, she states that the absence of fetters on policy choices affecting the very existence of emission allowances indicates that these interests lacked stability, a key characteristic of property rights.[276]

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[270] **RER-1**, Katz - Expert Report, ¶ 68.

[271] **RER-1**, Katz - Expert Report, Section 6.6.2.

[272] *See* **RER-1**, Katz - Expert Report, s. 5.9.

[273] **RER-1**, Katz - Expert Report, ¶ 32.

[274] **RER-1**, Katz - Expert Report, ¶ 30.

[275] **RER-1**, Katz - Expert Report, ¶ 73: "In *Foster,* the lack of stability that rendered an interest non-proprietary was captured as follows: 'It appears that the characterization of such a licence depends on the extent to which the licence holder can be said to have been granted a vested right on the one hand; or a privilege wholly dependent on the discretion of the issuing Ministry or regulatory body on the other hand.'" *See* **R-70**, *Foster, Re*, [1992] CarswellOnt 637, ¶ 5.

[276] *See* **RER-1**, Katz - Expert Report, ¶ 73.

That is not surprising, as emission allowances were designed, first and foremost, to be a flexible policy mechanism for each jurisdiction to reduce carbon emissions, not to create property rights.[277]

146. Professor Katz notes that section 70 of the *Climate Change Act*, "conveys that emission allowances were not constituted as *choses in action* that would resist or constrain policy choices of the government taken within the Cap-and-Trade program."[278] Under this provision, it is explicitly stated that no compensation is owed "in respect of any action taken by the Minister or Director under this Act […], including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts."[279] Ontario's legislation thus expressly limited the rights conferred with an emission allowance. This provision demonstrates that there was no legislative intent to imbue these interests with a proprietary nature, in line with the broader environmental policy regarding cap and trade.[280]

(iii) Contingency of value and tradability

147. The Claimants allege that the emission allowances held by KS&T were "tradable property rights, both as commodities and under futures contracts and were capital assets."[281] In support of this statement, the Claimants cite to *Armstrong* a UK case concerning emission allowances in the European Union Emissions Trading System ("ETS").[282] In that case, the UK court concluded that European Union allowances were "property" because they were a transferable exemption which had a value.[283] The Claimants' reliance on *Armstrong* is unavailing not only because it concerns a different regime, the ETS, but also because under Ontario law value and tradability are not themselves determinative of property rights.

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[277] **RER-2**, Litz - Expert Report, ¶ 51.

[278] **RER-1**, Katz - Expert Report, ¶ 73.

[279] **R-6**, *Climate Change Act*, s. 70; *see* **R-71**, *Manrell v Canada* [2003] FCA 128, ¶ 25, "it is implicit in this notion of 'property' that 'property' must have or entail some exclusive right to make a claim against someone else."

[280] **RER-1**, Katz - Expert Report, ¶ 59.

[281] Claimants' Memorial, ¶ 323(c).

[282] Claimants' Memorial, ¶ 323(c).

[283] **R-72**, *Armstrong DLW GmbH v Winnington Networks Ltd*, [2012] EWHC 10 (Ch), ¶ 58.

148. In Canada, the fact that something is tradable and has commercial value does not mean that it constitutes property. In a decision binding on all Canadian jurisdictions, Justice Binnie, writing for the Supreme Court of Canada in the case of *Saulnier v. RBC*, emphasized that "many things that have commercial value do not constitute property."[284] This approach is a rejection of the "commercial realities" view of property.[285]

c) The Broader Context Supports the Conclusion that the Emission Allowances Did Not Confer Property Rights

149. The conclusion that emission allowances did not confer property rights is consistent with the fundamental policy objectives of the WCI model of cap and trade.[286] The nature of emission allowances was described by the WCI Design Recommendations in 2008: "Emission allowances are *not considered property rights* but are a limited authorization to emit."[287] The WCI Design for the WCI Regional Program 2010 confirmed that: "The program authority or a participating Partner jurisdiction shall retain the right to terminate or limit such authorization"[288] and that a "compliance instrument under the Partner jurisdiction's Cap-and-Trade Program *does not constitute a property right for any purpose*."[289]

150. The fact that emission allowances in Ontario's cap and trade program were not property is not unique. Under the relevant California regulation, compliance instruments were expressly not property: "[a] compliance instrument issued by the Executive Officer does not constitute property or a property right."[290] In addition, under other North American cap and trade programs, allowances are

[284] **R-66**, *Saulnier v. Royal Bank of Canada*, [2008] 3 S.C.R. 166, 2008 SCC 58, ¶ 42: "There is no necessary connection between proprietary status and commercial value."

[285] **RER-1**, Katz - Expert Report, ¶ 19.

[286] **RER-1**, Katz - Expert Report, Section 6.4.

[287] **R-5**, 2008 WCI Recommendations, FN 28 (emphasis added).

[288] **C-15**, 2010 WCI Design Document, p. DD-20, ¶ 4.4.6.

[289] **C-15**, 2010 WCI Design Document, p. DD-21, ¶ 4.4.7 (emphasis added).

[290] **R-73**, California Code of Regulations, "California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms 17", CCR, §95820(c): "A compliance instrument issued by the Executive Officer does not constitute property or a property right."

not property.[291] For example, under the RGGI, a cooperative effort among ten U.S. States, "a CO_2 allowance under the CO_2 Budget Trading Program does not constitute a property right."[292]

151. To imbue such compliance instruments proprietary status would restrict the ability of States to regulate or modify environmental policies. A reduction in the availability of emission allowances within a cap and trade system is contemplated by their very design.[293] This is consistent with Professor Katz's explanation that the context in which an interest is being construed is a significant factor in guiding the treatment of an interest as property. Professor Katz states that, "to construe a statutorily created interest as property rights fetters discretion to regulate in the public interest and so derogates from public rights, which courts will presume the legislature not to have intended absent clearly expressed contrary intention."[294] Where recognizing statutorily created interests as property would "derogate from government discretion to regulate in the public interest", common law principles favour a non-proprietary construction.[295]

2. KS&T Did Not Hold "Interests Arising from the Commitment of Capital or other Resources in the Territory of a Party to Economic Activity in Such Territory" Under NAFTA Article 1139(h)

152. The Claimant KS&T asserts that it had investments in Canada under Article 1139(h), pointing to the purchase price of emission allowances it acquired in Ontario auctions.[296] Article 1139(h) provides that:

> **investment** means: […]
>
> (h) interests arising from the commitment of capital or other resources in the territory of a Party to economic activity in such territory, such as under

[291] **RER-2**, Litz - Expert Report, ¶¶ 49, 51.

[292] **R-9**, The Regional Greenhouse Gas Initiative, "Model Rule", s. XX-1.5(c)(9).

[293] **R-5**, 2008 WCI Recommendations, p. 27, ss. 1.7.1, and 1.7.2.

[294] **RER-1**, Katz - Expert Report, ¶ 49.

[295] **RER-1**, Katz - Expert Report, ¶ 49.

[296] Claimants' Memorial, ¶ 323. The Claimant Koch Industries does not assert subject-matter jurisdiction on the basis of Article 1139(h). *See* Claimants' Memorial, ¶ 322.

> (i) contracts involving the presence of an investor's property in the territory of the Party, including turnkey or construction contracts, or concessions, or
>
> (ii) contracts where remuneration depends substantially on the production, revenues or profits of an enterprise;

153. For an alleged investment to fall under Article 1139(h), the Claimants must establish that KS&T made a "commitment" of capital or other resources "in the territory" of Ontario in furtherance of "economic activity in" Ontario. In **section (a)**, Canada explains that the Claimants have failed to satisfy the requirements of the *chapeau* of Article 1139(h). Far from being a "commitment" of capital, KS&T's acquisition of emission allowances was a purchase and sale transaction, which is excluded from protection under Article 1139(h). Article 1139(h)(i) and (ii) further illustrate that KS&T's alleged investment falls outside the scope of an "investment" under Article 1139(h), as addressed in **section (b)**.

a) The Purchase Price of the Emission Allowances Was Not a "Commitment of Capital" "in the Territory" of Ontario

154. To qualify as an investment under NAFTA Article 1139(h), a commitment of capital or resources must "exhibit certain features so as to give rise to 'interests'".[297] The *chapeau* of Article 1139(h) states that a protected "interest" can only arise: "[f]rom the *commitment* of capital or other resources *in the territory* of a Party *to economic activity in such territory*" (emphasis added). The interpretation of (h) is assisted by Articles 1139 (i) and (j), which clarify what an "investment *does not* mean":

> (i) claims to money that arise solely from
>
> > (i) commercial contracts for the sale of goods or services by a national or enterprise in the territory of a Party to an enterprise in the territory of another Party, or
> >
> > (ii) the extension of credit in connection with a commercial transaction, such as trade financing, other than a loan covered by subparagraph (d);
>
> or

[297] **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 182. *See also* **RL-23**, Kinnear: Investment Disputes under NAFTA, pp. 1139-30.

> (j) any other claims to money, that do not involve the kinds of interests set out in subparagraphs (a) through (h)

155. Read in its context,[298] Article 1139(h) requires a commitment of capital that amounts to something more than a claim to money arising from a purchase and sale transaction.

156. This conclusion has been confirmed by NAFTA tribunals. As the tribunal explained in *Apotex Inc. v. United States*, "NAFTA Article 1139(h)'s focus on interests arising from the commitment of capital in the host State to economic activity in such territory excludes simple cross-border trade interests. Something more permanent is necessary."[299] Similarly, in *Canadian Cattlemen*, where Canadian beef farmers were negatively affected by a U.S. border closure, the tribunal declined jurisdiction on the basis that "mere cross-border trade interests" are not protected and that "something more permanent" is required in order to "rise to the level of an investment" under NAFTA.[300]

157. The Claimants allege that the monies KS&T used to buy emission allowances through its Ontario CITSS account in 2017 and 2018 constitute an "investment" under Article 1139(h).[301] KS&T's suggestion that the purchase price of the emission allowances acquired at the 2017 auctions and the February 2018 joint auction constitutes an "investment" in Ontario is absurd, given that it transferred those allowances to California for resale and use in that jurisdiction. Canada will instead address the alleged "investment" for which the Claimants' seek compensation in this arbitration, which is linked to the purchase price of the emission allowances in KS&T's Ontario CITSS account

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[298] **RL-29**, *Vienna Convention on the Law of Treaties*, 23 May 1969 (entered into force 27 January 1980) 1155 U.N.T.S. 331("*Vienna Convention on the Law of Treaties*"), Art. 31(1): "A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

[299] **RL-30**, *Apotex Inc. v. United States of America* (ICSID Case No. UNCT/10/2) Award on Jurisdiction and Admissibility, 14 June 2013 ("*Apotex – Jurisdiction Award*"), ¶ 233.

[300] **RL-31**, *Canadian Cattlemen for Fair Trade v. United States of America*, (UNCITRAL) Award on Jurisdiction, 28 January 2008 ("*Cattlemen – Award*"), ¶ 144; *see also* **RL-32**, *Bayview Irrigation District v Mexico* (ICSID Case No ARB(AF)/05/1) Award, 19 June 2007 ("*Bayview – Award*"), ¶ 104.

[301] Claimants' Memorial, ¶ 323(b): "KS&T […] held interests arising out of the commitment of capital and other resources in Canada, including: […] "commitment of capital through the purchases of carbon allowances from public auctions through KS&T's Ontario CITSS accounts. Over a two year period, KS&T invested a cumulative total of CAD 26,255,340 in 2017 and USD 64,126,490.95 in 2018 through the purchase of 5,841,583 carbon allowances from Ontario auctions." Of course, in the February 2018 joint auction Ontario only received payment for the portion of emission allowances that it had contributed to the auction.

as a result of the May 2018 auction.[302]

158. According to statements made by KS&T in 2019, it acquired the emission allowances in the May 2018 auction for the purpose of selling them to Flint Hills Resources (**FHR**), a U.S. company with compliance obligations in California.[303] The Claimants have confirmed that KS&T purchased emission allowances in Ontario in order to "sell them on to FHR"[304] in California. KS&T's purchase of emission allowances in Ontario in the May 2018 for resale in California is nothing more than the first in series of transactions leading to a cross-border sale. The Claimants have not identified any "interests" arising from the purchase of the emission allowances such as to elevate it beyond a mere expenditure of funds.[305]

b) Subparagraphs (h)(i) and (h)(ii) Further Illustrate that the Purchase Price of the Emission Allowances is Not a Protected "Interest"

159. Subparagraphs (h)(i) and (ii) illustrate which types of "interests arising out of the commitment of capital or resources" are protected under NAFTA Article 1139(h).[306] The purchase price of emission allowances bears no similarity to either Article 1139(h)(i) or (ii).

160. The common feature between both subparagraphs (h)(i) and (ii) is that they refer to "contracts". Moreover, subparagraphs (h)(i) and (h)(ii) both require additional features for "commitments of capital or resources" to be protected under NAFTA; the former "impl[ies] the presence of an investor's property in the host state", while the latter involves "remuneration [that]

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[302] KS&T also alleges that its "investment" under NAFTA Article 1139(h) "included KS&T's broader carbon trading business, and the efforts on the part of KS&T to build an enterprise of trading in Ontario emission allowances over the course of several years as part of a sustained, long-term business plan." Claimants' Memorial, ¶ 323(a). There no evidence that KS&T had a subsidiary in Ontario, an office in Ontario, an address in Ontario, or personnel in Ontario. This assertion is also contradicted by the Claimants' statements predating this NAFTA claim, in which they argued that KS&T was, in effect, a mandatory participant in the Ontario program, and not a market participant at all. *See* **C-127**, KS&T Compensation Application Form, 14 February 2019: KS&T was "technically registered as a market participant" but actually "purchased allowances for its mandatory compliance affiliates."

[303] **C-127**, KS&T Compensation Application Form, 14 February 2019.

[304] Claimants' Memorial, ¶ 165.

[305] If the Tribunal finds otherwise, the "investment" must be limited to the amount received by Ontario from KS&T as a result of the May 2018 auction, being USD [redacted]

[306] **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 207.

depends substantially on the production, revenues or profits of an enterprise located in the host state."[307] They both implicate substantial investments and long-term commitment of capital contributing to the economic development of the host state.

161. More specifically, subparagraph (h)(i) only covers contracts involving "the presence of an investor's property in the territory" of the host State. Examples of the types of contracts covered under subparagraph (h)(i) are included in the provision itself, i.e. "turnkey contracts, construction contracts and concessions".[308] Tribunals considering subparagraph (h)(i) have found that "interests" held through a limited partnership formed in the host State and arising from contractual rights to develop large parcels of property in the host State qualified for protection under Article 1139; [309] but "short-term, fixed-term loans" that did not imply the presence of the investor in the territory of the host State did not.[310] Therefore, the mere commitment of funds relating to a contract, if such commitment is not in relation to an investor's property in the territory of the host State and bears no relationship with contracts such as turnkey or construction contracts or concessions, is not protected under NAFTA Article 1139(h).

162. Subparagraph (h)(ii), in turn, "refers to contracts where the investor commits capital, provided that the remuneration depends substantially on the production, revenues or profits of an enterprise located in the host state."[311] Article 1139(h)(ii) forms part of the first group of interests protected under NAFTA Article 1139 and refers to "situations where the foreign investor owns or finances 'enterprises' located in the host state".[312] Therefore, subparagraph (h)(ii) must be understood as specifically covering "contracts with variable remuneration" provided they relate to the "production,

[307] **RL-24**, *Lion – Decision on Jurisdiction*, ¶¶ 198, 199.

[308] **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 198.

[309] **CL-56**, *Mondev – Award*, ¶ 80.

[310] The loans "[did] not imply the presence of an investor's property in the host state, and [had] no relationship with turnkey contracts, construction contracts, and concessions'"; they also lacked any "additional, defining feature" specifically accounted for in subparagraphs (h)(i) and (h)(ii). **RL-24**, *Lion – Decision on Jurisdiction*, ¶¶ 198, 207.

[311] **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 199.

[312] **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 185. KS&T does not own or control an enterprise in Canada.

revenues or profits of *an enterprise located in the host state*".[313]

163. The Claimants do not address how KS&T's alleged investment accords with the illustrative examples of interests protected under subparagraphs (h)(i) and (ii). The emission allowances are not contracts at all, let alone "contracts relating to the presence of an investor's property in the territory of the host State such as "turnkey or construction contracts or concessions" as set out in subparagraph (h)(i). Nor does the purchase of emission allowances involve a "situation[] where the foreign investor owns or finances 'enterprises' located in the host state"[314], as contemplated by subparagraph (h)(ii).

164. Having failed to demonstrate that it held "interests" arising from the commitment of capital or resources in "the territory of [Ontario]" that contributed to the "economic activity in such territory", KS&T cannot claim that it had a protected investment within the meaning of NAFTA Article 1139(h). KS&T's dealings in the emission allowances were more akin to cross-border trade or sales, which are not protected investments under the NAFTA.[315]

3. Koch Industries Does Not Hold Protected "Investments" Under Article 1101 and Article 1139

165. The Claimant Koch Industries is the indirect parent of KS&T. Both are U.S. enterprises. Koch Industries alleges that it has the following qualifying "investments" under NAFTA Article 1139: (1) its shareholding in KS&T, under Article 1139(a); (2) its shareholding in Invista, under Article 1139(a); (3) other unidentified "interests in enterprises" under Article 1139(e); and (4) real estate and other property (its Canadian subsidiaries Invista and Georgia Pacific), under Article 1139(g). Not one of these alleged "investments" is sufficient to establish subject-matter jurisdiction in this dispute.

a) Koch Industries' Ownership of KS&T, a U.S. Entity, is Not an "Investment" in Canada Under Article 1139(a)

166. Article 1139(a) provides that "investment means (a) an enterprise". The "enterprise" referred to in Article 1139(a) must necessarily be an enterprise of the host State, not of the purported investor's

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[313] **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 207 (emphasis added).

[314] **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 185.

[315] **RL-30**, *Apotex – Jurisdiction Award*, ¶¶ 207-208, 221, 224, 233.

home State. Article 1101(1)(b) confirms this conclusion, establishing that NAFTA Chapter Eleven applies to "measures adopted or maintained by a Party relating to […] investments of investors of another Party in the territory of the Party."[316] This principle is not controversial and has been reiterated by NAFTA tribunals.[317] In order to hold an "investment" in Canada under Article 1139(a), Koch Industries would need to establish that it owns or controls a relevant "enterprise" in the territory of Canada.

167. KS&T is a partnership organized under the laws of Delaware.[318] As such, KS&T is an enterprise of the United States, and Koch Industries' ownership or control of KS&T cannot be an "investment" in Canada under Article 1139(a) and Article 1101. Therefore, it falls outside the scope of an "investment" capable of supporting subject-matter jurisdiction.

b) Koch Industries' Ownership of a Canadian Enterprise That is Not in Dispute Is Not an "Investment" Under Article 1139(a)

168. Koch Industries also points to its shareholding in Invista, a Canadian entity. However, in order to ground subject-matter jurisdiction under Article 1101(1)(b) and Article 1139(a), the "enterprise" must also be the alleged "investment" in dispute. That is, an enterprise cannot serve as the basis for jurisdiction over a dispute regarding *another* enterprise or investment. In the context of a NAFTA dispute, the measure, alleged breach and alleged damages must all relate to the same alleged

[316] NAFTA, Article 1101(1)(b). *See also* NAFTA Article 1139: "investment of an investor of a Party" means "an investment owned or controlled directly or indirectly by an investor of such Party".

[317] **RL-32**, *Bayview – Award*, ¶ 105, "It is clear that the words "territory of the Party" in that phrase do not refer to the territory of the Party of whom the investors are nationals. It requires investment in the territory of another NAFTA Party –the Party that has adopted or maintained the measures challenged. In short, in order to be an "investor" under Article 1139 one must make an investment in the territory of another NAFTA State, not in one's own."; **RL-31**, *Cattlemen – Award*, ¶126 "Returning to Article 1101(1) in light of these definitions provides the first crystallization of the answer. From the fact that Article 1101(b) and (c), which are conjunctively linked with 1101(a), explicitly limit Chapter Eleven's coverage to investments in the territory of the Party whose measure is at issue, it is apparent that the foreign investment, and the investors who engage in such investment activities, are the concern of Chapter Eleven. In other words, 'investors' are inextricably linked to 'investments,' which Article 1101 limits to 'foreign investments,' – that is to say, investments of a party in the territory of another Party whose measure is at issue."

[318] Claimants' Memorial, ¶ 5.

investment.[319] But the Claimants claim no breach or damages with respect to Invista.[320] Koch Industries' alleged investment in Invista is irrelevant to the claim put forward by the Claimants, and has no bearing on whether the Tribunal has jurisdiction *ratione materiae* over this dispute.

c) Unidentified Interests in Unidentified Enterprises Are Not "Investments" Under NAFTA 1139(e)

169. The Claimant argues that Koch Industries holds "interests in enterprises entitling Koch to the income or profits of these enterprises" and that these are protected investments under Article 1139(e).[321] However, the Claimant does not identify any particular "interests" or "enterprises", instead merely citing to the definition of Article 1139(e) itself. A NAFTA tribunal cannot simply assume jurisdiction over an unidentified alleged "investment."

d) Koch Industries Does Not Hold Identifiable Real Estate or Other Property as a Protected "Investment" Under NAFTA 1139(g)

170. The Claimants allege that Koch Industries holds "a range of other bricks-and-mortar investments in Ontario, as well as intangible investments" sufficient to satisfy the requirements of Article 1139(g), stating that "[t]hese include, but are not limited to, Koch subsidiaries INVISTA and Georgia Pacific".[322] As set out above, unidentified investments cannot found the Tribunal's jurisdiction, nor can alleged investments that are irrelevant to the claims at issue. That Koch Industries indirectly owns real estate in Canada – because it owns Canadian companies that themselves own real estate in Canada – is irrelevant unless that real estate is itself the subject of the investment dispute. There is no basis on which to conclude that the Tribunal has subject-matter jurisdiction over the dispute as a result of Koch Industries' holding real estate or other property under

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[319] *See* **RL-131**, *Westmoreland Mining Holdings LLC v. Government of Canada* (ICSID Case No. UNCT/20/3), *Final Award*, 31 January 2022, ¶ 200.

[320] [redacted] **R-74**, [redacted]

[321] Claimants' Memorial, ¶ 322(b).

[322] Claimants' Memorial, FN 412.

Article 1139(g).[323]

171. Koch Industries has no protected "investments" under NAFTA Article 1139, and as such, this Tribunal lacks jurisdiction over its claims.

E. Koch Industries Lacks Standing Under NAFTA Article 1116 Because It Has Not Pled Any Cognizable Loss or Damage

172. Under Article 1116(1), an investor may only submit a claim to arbitration if that investor has suffered loss or damage as a result of the alleged breach of Section A of the NAFTA. Where a claimant cannot have incurred loss or damage "by reason of, or arising out of" the alleged breach, the tribunal does not have jurisdiction.[324]

173. The Claimants make no allegation of damage to Koch Industries' shareholding in KS&T or Invista.[325] The Claimants do not allege any damage to the unidentified enterprises or intangibles, nor do they allege any damage in relation to "bricks-and-mortar" enterprises. The Claimants seek damages in relation to emission allowances held by KS&T, on the basis that "there has been an expropriation of its investments and/or an Article 1105 breach which has resulted in those

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[323] The Claimants have abandoned the argument that Koch Industries indirectly held KS&T's emission allowances under the cap and trade program, as initially alleged in the Request for Arbitration, *see* Claimants' RFA, ¶ 18.

[324] *See* **CL-89**, *Methanex Corporation v. United States of America* (UNCITRAL) Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005 ("*Methanex – Final Award*"), Part II, Ch. F, ¶ 26: "The Tribunal construes Articles 1116 and 1117 as requiring a claim of loss or damage that originates in the measure adopted or maintained by the NAFTA Party."); *Westmoreland Mining Holdings LLC v. Government of Canada* (ICSID Case No. UNCT/20/3), *Final Award*, 31 January 2022; s*ee also* **RL-33**, *Saluka Investments B.V. (The Netherlands) v. The Czech Republic* (UNCITRAL) Partial Award, 17 March 2006 ("*Saluka – Partial Award*"), ¶ 244: "[I]n accordance with the Treaty, [the Tribunal's] jurisdiction is limited to claims brought by the Claimant, Saluka, in respect of damage suffered by itself [...]" **RL-34**, *Pope & Talbot v. Government of Canada*, (UNCITRAL) Seventh Submission of the United States of America, 6 November 2001 ("*Pope & Talbot – Seventh Submission of the United States*"), ¶¶ 2, 5-6, 9, **RL-35**, *Vento Motorcycles, Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/17/3) United States Articles 1128 Submission, 23 August 2019, ¶ 40, **RL-36**, *Legacy Vulcan, LLC v. United Mexican States*, (ICSID Case No. ARB/19/1) Non-Disputing Party Submission of the Government of Canada Pursuant to NAFTA Article 1128, 7 June 2021, ¶ 27; **RL-37**, *Legacy Vulcan, LLC v. United Mexican States*, (ICSID Case No. ARB/19/1) Submission of the United States of America, 7 June 2021, ¶ 19.

[325] *See* **R-34**, *Pope & Talbot – Seventh Submission of the United States*, ¶ 6: "Examples of direct losses sustained by an investor in its capacity as an investor that would give rise to a claim under Article 1116 are, for example, losses suffered as a result of an investor's stockholder shares having been expropriated or losses sustained as a result of the investor having been denied its right to vote its shares in a company incorporated in the territory of another NAFTA Party." In any event, Koch Industries' shareholding in KS&T is irrelevant for these purposes because KS&T is a U.S. entity.

investments being rendered worthless."[326]

174. The Tribunal lacks personal jurisdiction over Koch Industries because it has failed to plead that it incurred any cognizable loss or damage by reason of, or arising out of, the alleged breaches of Articles 1105 and 1110.

IV. THE CLAIMANTS HAVE FAILED TO ESTABLISH A VIOLATION OF NAFTA CHAPTER ELEVEN

A. The Claimants Have Not Established a Breach of Article 1105

1. Summary of Canada's Position

175. The Claimants argue that Ontario breached NAFTA Article 1105 by "abruptly and arbitrarily cancell[ing] the Cap and Trade Program, and cancell[ing] all carbon allowances" as well as by "provid[ing] for compensation in an arbitrary and discriminatory manner, and expressly den[ying] participants in the Cap and Trade Program access to justice."[327] The Claimants allege that these actions "are manifestly arbitrary and discriminatory, include an express denial of justice, and violate the Claimants' legitimate expectations".[328] On the contrary, Ontario's policy decisions with respect to the cap and trade program and its wind-down were made in pursuit of legitimate policy goals, and do not rise to the high threshold required to establish a violation of Article 1105.

176. The Claimants propose an overly broad and legally unfounded interpretation of NAFTA Article 1105 (**section 2**). The scope of NAFTA Article 1105 is limited to the protection of aliens from treatment in violation of the minimum standard of treatment under customary international law (**a**). The Claimants bear the burden of establishing that this standard includes the specific protections they allege (**b**). The Claimants fail to establish that NAFTA Article 1105 includes the protection of an investor's legitimate expectations (**c**).

177. In any event, the Claimants have not shown that Ontario's actions breached NAFTA Article 1105 (**section 3**). First (**a**), Ontario's decision to wind down the cap and trade program was not

[326] Claimants' Memorial, ¶ 513.

[327] Claimants' Memorial, ¶ 351.

[328] Claimants' Memorial, ¶ 349.

"sudden" or "abrupt", but was instead a clear campaign promise of the party that won the June 2018 provincial election. Once in power, the new government adopted Regulation 386 under the *Climate Change Act* and then followed the normal legislative process in developing and implementing Bill 4, which became the *Cancellation Act*.

178. Second (**b**), Ontario's decisions with respect to wind down and compensation were taken in good faith and for legitimate policy reasons, and were not manifestly arbitrary. The compensation scheme adopted by the government as part of the wind-down of the cap and trade program was grounded in policy-based distinctions between participants in the program, including whether an entity had compliance obligations or not. It is not for a NAFTA Chapter Eleven tribunal to label *bona fide* public policy choices as manifestly arbitrary and contrary to the minimum standard of treatment under customary international law.

179. Third (**c**), Article 1105 does not protect an investor's legitimate expectations, and in any event the evidence shows that Ontario did not make specific commitments to the Claimants to induce an alleged investment. Ontario never promised that it would refrain from cancelling the cap and trade program or that, in the event of cancellation, all participants would be compensated. To the contrary, participants in the cap and trade program knew that "no compensation" would be available. In addition, the Harmonization Agreement was incapable of supporting any legitimate expectations, including with regard to how and when a party could withdraw.

180. Fourth (**d**), Ontario did not commit a denial of justice by enacting section 10 of the *Cancellation Act*. Crown immunity provisions are valid and constitutional in Canada. Section 10 allowed for Ontario to efficiently and orderly wind down the cap and trade program, and it rather applied to all participants in the cap and trade program equally, foreign and domestic. The Crown immunity provision of the *Cancellation Act* does not rise to the level that is required to amount to a denial of justice as defined in customary international law.

2. The Claimants' Overly Broad Interpretation of NAFTA Article 1105 Must be Rejected

a) Article 1105 Guarantees Treatment In Accordance With the Minimum Standard of Treatment of Aliens Under Customary International Law

181. NAFTA Article 1105 stipulates that "[e]ach Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security".

182. On July 31, 2001, the Free Trade Commission (**FTC**) adopted a binding interpretation of Article 1105(1):

> Minimum Standard of Treatment in Accordance with International Law
>
> (1) Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.
>
> (2) The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.
>
> (3) A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).[329]

183. Under NAFTA Article 1132(1), an interpretation issued by the FTC is binding on arbitral tribunals. In order to establish a violation of NAFTA Article 1105, an investor must demonstrate that Canada violated a rule of customary international law regarding the treatment of aliens.[330] An arbitral tribunal may not "simply adopt its own idiosyncratic standard of what is 'fair' or 'equitable', without reference to established sources of law."[331]

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[329] **RL-38**, NAFTA Free Trade Commission, Notes of Interpretation of Certain Chapter 11 Provisions, 31 July 2001.

[330] **CL-68**, *Loewen Group, Inc. and Raymond L. Loewen v. United States of America* (ICSID Case No. ARB(AF)/98/3) Award (23 June 2003) ("*Loewen – Award*"), ¶ 128: "'fair and equitable treatment' and 'full protection and security' are not free-standing obligations. They constitute obligations only to the extent that they are recognized by customary international law."

[331] **CL-56**, *Mondev – Award*, ¶ 119.

184. The threshold to establish a violation of this standard is high.[332] There will be no violation of the minimum standard of treatment unless the conduct of the State "is sufficiently egregious and shocking […] so as to fall below accepted international standards."[333] For the conduct of the State to fall below the minimum standard of treatment of aliens, an act must be "a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination, or a manifest lack of reasons" to fall below accepted international standards.[334] The tribunal in *Perenco Ecuador Limited v. Republic of Ecuador* confirmed that the use of the words "arbitrary", "grossly", "manifest" and "complete" serves a purpose and makes clear that only State actions that raise to a certain threshold of seriousness will breach international law.[335]

b) The Claimants Bear the Burden of Establishing that Article 1105 Includes the Protections They Allege

185. A claimant bears the burden of proving that Article 1105 includes the protections it alleges.[336] A claimant must either rely on a recognized rule of customary law or prove the emergence of a new rule under customary international law that prohibits a particular State act or omission. Where a rule of customary international law has not been satisfactorily established, a tribunal may not assume this

[332] **CL-17**, *International Thunderbird Gaming Corporation v. United Mexican States* (UNCITRAL) Award, 26 January 2006 ("*Thunderbird – Award*"), ¶ 194; **CL-18**, *Glamis Gold – Award*, ¶¶ 616-617, 627.

[333] **CL-18**, *Glamis Gold – Award*, ¶ 627.

[334] **CL-18**, *Glamis Gold – Award*, ¶ 616.

[335] **RL-2**, *Perenco – Decision on Remaining Issues of Jurisdiction and on Liability*, ¶ 559: "'The inclusion of such words as 'arbitrary,' the use of the adjectival modifiers 'grossly' in relation to 'unfair, just or idiosyncratic,' and 'manifest' in relation to a failure of natural justice and 'complete' in relation to a lack of transparency and candour implies a search for 'something more' that distinguishes an act in violation of international law from the perceived unfairness occasioned by many governmental actions that do not rise to a breach of international law." In *Perenco*, the tribunal concluded that the applicable standard was an "autonomous" fair and equitable treatment standard. Despite applying this "autonomous" standard, which is of no relevance in a NAFTA case, the tribunal nonetheless concluded that something more than a "perceived unfairness" was necessary to amount to a breach international law.

[336] *See* **RL-39**, *Case Concerning Rights of Nationals of the United States of America in Morocco (France v. United States)*, [1952] I.C.J. Rep. 176, p. 200 citing *The Asylum Case* (*Colombia v. Peru*), [1950] I.C.J. Rep. 266, pp. 276- 277: "The Party which relies on custom of this kind must prove that this custom is established in such a manner that it has become binding on the other Party."; **CL-18**, *Glamis Gold – Award*, ¶ 601: " If, as Claimant argues, the customary international law minimum standard of treatment has indeed moved to require something less than the "egregious," "outrageous," or "shocking" standard as elucidated in *Neer*, then the burden of establishing what the standard now requires is upon Claimant."

task and should rather "hold that the Claimant fails to establish the particular standard asserted."[337]

186. To demonstrate the existence of a new customary rule, a claimant must prove both the existence of a State practice and *opinio juris*, indicating that this practice was adopted by States because it constitutes accepted law.[338] This requires evidence of the consistency and generality of a practice amongst States and the belief by States that the practice is legally binding on them under international law.[339] An investor cannot resort to decisions from arbitral tribunals to prove the existence of a customary rule, without relying on actual evidence of State practice. As held by the NAFTA tribunal in *Glamis Gold*, arbitral awards "do not constitute State practice and thus cannot create or prove customary international law" but can only "serve as illustrations of customary international law if they involve an examination of customary international law".[340]

c) Article 1105 Does Not Include the Broad Protections the Claimants Allege

(i) Article 1105 Does Not Allow a Tribunal to Second-Guess Government Policy Decisions

187. The Claimants' case is based on an argument that this Tribunal should second-guess the Government of Ontario's decision to wind-down the cap and trade program and should substitute its own policy rationale for Ontario's actions *ex post facto*. However, NAFTA Article 1105 is an objective standard and not an invitation for claimants to question the legitimacy of States'

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[337] **CL-54**, *Cargill – Award*, ¶ 273. *See also* **CL-57**, *ADF – Award*, ¶ 185: "The investor, of course, in the end has the burden of sustaining its charge of inconsistency with Article 1105(1). That burden has not been discharged here and hence, as a strict technical matter, the Respondent does not have to prove that the current customary international law concerning standards of treatment consists only of discrete, specific rules applicable to limited contexts."

[338] **CL-18**, *Glamis Gold v. United States of America* (UNCITRAL) Award, 8 June 2009 ("*Glamis Gold – Award*"), ¶¶ 600-603; **CL-57**, *ADF Group Inc. v. United States of America* (ICSID Case No. ARB(AF)/00/1) Award, 9 January 2003 ("*ADF – Award*"), ¶¶ 184-185.

[339] **RL-40**, *Case Concerning Military and Paramilitary Activities in and Against Nicaragua (Nicaragua v. United States of America)*, [1986] I.C.J. Rep. 14, ¶ 207: "In considering the instances of the conduct …the Court has to emphasize that, as was observed in the *North Sea Continental Shelf* cases, for a new customary rule to be formed, not only must the acts concerned 'amount to settled practice', but they must be accompanied by the *opinio juris sive necessitates*. Either the States taking such action or the other States in a position to react to it must have behaved so that their conduct is 'evidence of a belief that this is practice is rendered obligatory by the existence of a rule of law requiring it.'"). *See also* **RL-41**, James Crawford, "Brownlie's Principles of International Law", 9th ed. (Oxford: Oxford University Press, 2018) (Crawford: Brownlie's Principles of International Law"), pp. 21-22.

[340] **CL-18**, *Glamis Gold – Award*, ¶ 605.

decisions.[341] International law generally recognizes a high level of deference to States with respect to their domestic policy choices and how they choose to regulate matters within their borders.[342]

188. Tribunals have confirmed that their role is not to second-guess States' policy choices and to substitute themselves for the States.[343] As a corollary, and in light of the deference accorded to States, Article 1105 cannot be read as a broad protection against any measure that an investor views as unfair. Nor can it serve as a basis for reviewing the sufficiency of the policy rationale underlying States' choices on how to regulate and manage their affairs.[344]

189. The Claimants cannot simply label Ontario's actions as "unreasonable", "political" or "arbitrary" in order to invite the Tribunal to second-guess Ontario's policy decisions. Absent a clear demonstration that a measure meets very high threshold to establish a violation of Article 1105, it cannot be considered manifestly arbitrary as understood under the minimum standard of treatment under customary international law.

(ii) Article 1105 Does Not Protect Against Changes in the Regulatory Environment

190. The minimum standard of treatment under NAFTA Article 1105 also does not guarantee to foreign investors that host States will "maintain a stable legal and business environment."[345] Indeed, the standard of treatment does not shield investors from any regulatory changes nor to ensure that

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[341] **CL-67**, *Chemtura Corporation (formerly Crompton Corporation) v. Government of Canada*, Award, 2 August 2010 ("*Chemtura – Award*"), ¶ 134; **CL-18**, *Glamis Gold – Award*, ¶ 779; **CL-56**, *Mondev – Award*, ¶ 120.

[342] *See for example*, **RL-33**, *Saluka – Partial Award*, ¶ 305; **RL-42**, *Gemplus, S.A., SLP, S.A., and Gemplus Industrial, S.A. de C.V. v. The United Mexican States* (ICSID Case No. ARB(AF)/04/3 & ARB(AF)/04/4) Award, 16 June 2010 ("*Gemplus – Award*"), s.6, ¶ 26; **CL-115**, *Crystallex International Corporation v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB(AF)/11/2) Award, 4 April 2016 ("*Crystallex – Award*"), ¶ 583; **RL-17**, *El Paso – Award*, ¶ 342; **CL-58**, *Eco – Decision on Jurisdiction, Liability and Directions on Quantum*, ¶ 750.

[343] **CL-67**, *Chemtura – Award*, ¶ 134; **RL-33**, *Saluka – Partial Award*, ¶ 337: "It is clearly not for this Tribunal to second-guess the Czech Government's privatisation policies."; **RL-43**, *Invesmart, B.V. v. Czech Republic* (UNCITRAL) Award, 26 June 2009 ("*Invesmart – Award*"), ¶ 501: "Numerous tribunals have held that when testing regulatory decisions against international law standards, the regulators' right and duty to regulate must not be subjected to undue second-guessing by international tribunals. Tribunals need not be satisfied that they would have made precisely the same decision as the regulator in order for them to uphold such decisions.".

[344] **RL-33**, *Saluka – Partial Award*, ¶ 305; **RL-42**, *Gemplus – Award*, 16 June 2010, ¶¶ 6-26.

[345] **RL-44,** *Mobil – Decision on Liability and on Principles of Quantum*, ¶ 153.

"the circumstances prevailing at the time the investment is made remain totally unchanged."[346]

191. On the contrary, States have the right to, and often do, change their laws.[347] As confirmed by the *Mobil* tribunal, nothing in NAFTA Article 1105 can be read as preventing a State from regulating, even it affects foreign investors and imposes additional burdens on them.[348] The Claimants ignore the well-established principle that States can "chang[e] the regulatory environment to take account of new policies and needs, even if some of those changes may have far-reaching consequences and effects, and even if they impose significant additional burdens on an investor."[349] Plainly put, "Article 1105 is not, and was never intended to amount to, a guarantee against regulatory change, or to reflect a requirement that an investor is entitled to expect no material changes to the regulatory framework within which an investment is made."[350]

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[346] **RL-33**, *Saluka – Partial Award*, ¶ 305.

[347] **RL-45**, Patrick Dumberry, "The Protection of Investor's Legitimate Expectations and the Fair and Equitable Treatment Standard under NAFTA Article 1105" 31:1, Journal of International Arbitration, 47 ("Dumberry: The Protection of Investor's Legitimate Expectations"), pp. 69-70, citing **RL-46**, *Parkerings-Compagniet AS v. Republic of Lithuania* (ICSID Case No. ARB/05/8) Award, 11 September 2007 ("*Parkerings – Award*"), ¶ 332.

[348] **RL-44**, *Mobil – Decision on Liability and on Principles of Quantum*, ¶ 153: "Article 1105 is not, and was never intended to amount to, a guarantee against regulatory change, or to reflect a requirement that an investor is entitled to expect no material changes to the regulatory framework within which an investment is made. Governments change, policies changes and rules change. These are facts of life with which investors and all legal and natural persons have to live with. What the foreign investor is entitled to under Article 1105 is that any changes are consistent with the requirements of customary international law on fair and equitable treatment. Those standards are set at, as we have noted above, at a level which protects against egregious behaviour."

[349] **RL-44**, *Mobil Investments Canada Inc. v Canada* (ICSID Case No ARB(AF)/07/4) Decision on Liability and on Principles of Quantum, 22 May 2012 ("*Mobil – Decision on Liability and on Principles of Quantum*"), ¶ 153.

[350] **RL-44**, *Mobil – Decision on Liability and on Principles of Quantum*, ¶ 153. Tribunals in a non-NAFTA context have also recognized that even an autonomous "fair and equitable treatment" standard does not confer a broad protection to foreign investors against regulatory changes in the host State. **RL-47**, *Charanne and Construction Investments v. Spain* (SCC Case No. V 062/2012) Final Award [Unofficial English Translation], 21 January 2016, ¶ 510: "[I]n the absence of a specific commitment toward stability, an investor cannot have a legitimate expectation that a regulatory framework such as that at issue in this arbitration is to not be modified at any time to adapt to the needs of the market and to the public interest"; **RL-48**, *Philip Morris Brand Sàrl, Philip Morris Products S.A.* and *Abal Hermanos S.A. v. Oriental Republic of Uruguay* (ICSID Case No. ARB/10/7) Award, 8 July 2016, ¶ 422: "It is common ground in the decisions of more recent investment tribunals that the requirements of legitimate expectations and legal stability as manifestations of the FET standard do not affect the State's rights to exercise its sovereign authority to legislate and to adapt its legal system to changing circumstances."; **RL-17**, *El Paso – Award*, ¶ 367: "it is inconceivable that any State would accept that, because it has entered into BITs, it can no longer modify pieces of legislation which might have a negative impact on foreign investors, in order to deal with modified economic conditions and must guarantee absolute legal stability"; **RL-49**, *Blusun S.A., JeanPierre Lecorcier and Michael Stein v. Italian Republic* (ICSID Case No. ARB/14/3) Award, 27 December 2016, ¶ 367: "[T]ribunals have so far declined to sanctify laws as promises"; **RL-46**, *Parkerings – Award*, ¶ 332: "A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement,

(iii) Article 1105 Does Not Protect an Investor's Legitimate Expectations

192. NAFTA tribunals have confirmed that a State's failure to comply with an investor's legitimate expectations will not, in itself, constitute a breach of the minimum standard of treatment. At most, legitimate expectations are "a factor to be taken into account by a tribunal when assessing an allegation of breach of another element of the standard."[351] This is not contested by the Claimants, who indicate in their Memorial that "whether a responding State has violated an investor's legitimate expectations will be a 'relevant factor' in assessing whether a measure amounts to a breach of the fair and equitable treatment standard."[352]

193. The Claimants nonetheless argue that "Canada has violated […] Article 1105(1) of the NAFTA with respect to its treatment of the Claimants and their investments" because its "actions […] violate *the Claimants' legitimate expectations.*"[353]

194. NAFTA Article 1105 does not contain an autonomous fair and equitable obligation, and the protection of investors' legitimate expectations is not a recognized rule under customary international law.[354] Since the Claimants do not even attempt to present evidence sustaining an argument that legitimate expectations are indeed protected under customary international law, this argument must fail. Moreover, even tribunals that have recognized that an investor's legitimate expectations may be a "relevant factor" to consider have narrowly qualified this concept.[355] For instance, in *Glamis Gold*,

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in the form of a stabilisation clause or otherwise, there is nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment. As a matter of fact, any businessman or investor knows that laws will evolve over time".

[351] **RL-45**, Dumberry: The Protection of Investor's Legitimate Expectations, p. 49, referring to **RL-44**, *Mobil – Decision on Liability and on Principles of Quantum*, ¶ 152; **CL-12,** *Waste Management, Inc. v. Mexico* (ICSID No. ARB(AF)/00/3) Award, 30 April 2004 ("*Waste Management – Award*"), ¶ 98.

[352] Claimants' Memorial, ¶ 348.

[353] Claimants' Memorial, ¶ 349 (emphasis added).

[354] **RL-45**, Dumberry: The Protection of Investor's Legitimate Expectations, p. 60: "there is little support for the assertion that there exists under customary international law any obligation for host states to protect investors' legitimate expectations."

[355] **RL-45**, Dumberry: The Protection of Investor's Legitimate Expectations, p. 49: legitimate expectations cannot "be solely based on the host state's existing domestic legislation at the time of the investment", but rather must "be based on specific commitments made by the host state to have purposely induced its investments."

which concerned a project to develop an open-pit gold mine in California, the tribunal held that "a violation of Article 1105 based on the unsettling of reasonable, investment-backed expectations, requires as a threshold circumstances, at least a quasi-contractual relationship between the State and the investor, whereby the State has purposely and specifically induced the investment."[356] The tribunal also indicated that such assurances from the State given to the investor, in order to induce its investment, would have had to be "definitive, unambiguous and repeated".[357] Finally, the tribunal confirmed that the fact that new legislation was passed to impose mandatory backfilling of open-pit mines, contrary to the claimant's expectations, was not relevant since "a claimant cannot have a legitimate expectation that the host country will not pass legislation that will affect it."[358]

195. Therefore, even if this Tribunal was to consider the Claimants' legitimate expectations as a "relevant factor" in determining whether there has been a violation of another element of the minimum standard of treatment, these legitimate expectations must be based on specific assurances given by Ontario to them in order to induce an investment. As explained below, nothing of the sort has been alleged by the Claimants and their claim must therefore fail.

(iv) Denial of Justice Under Article 1105 Requires a High Level of Severity and the Exhaustion of Local Remedies

196. The protection of foreign investors against denial of justice forms part of the minimum standard of treatment under customary international law found in NAFTA Article 1105. A finding of a denial of justice therefore requires a "high threshold of severity" and "only the gravest cases will be considered in breach of Article 1105,"[359] such as in the case of discriminatory treatment of a foreign litigant that amounts to "manifest injustice".[360] In the context of State immunity provisions, the right

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[356] **CL-18**, *Glamis Gold – Award*, ¶ 766.

[357] **CL-18**, *Glamis Gold – Award*, ¶ 802.

[358] **CL-18**, *Glamis Gold – Award*, ¶ 813. *See also* **RL-44**, *Mobil – Decision on Liability and on Principles of Quantum*, ¶ 152.

[359] **RL-51**, Patrick Dumberry, The Fair and Equitable Treatment Standard: A Guide To NAFTA Case Law on Article 1105. (Kluwer Law International, 2013) ("Dumberry: A Guide to NAFTA Case Law on Article 1105"), p. 33.

[360] **CL-68**, *Loewen – Award*, ¶ 135. The concept of "denial of justice" is usually confined to a particular category of "deficiencies on the part of the host state, principally concerning the administration of justice". **RL-41.** Crawford: Brownlie's Principles of International Law, pp. 602-603.

to access courts is not absolute, but rather may be subject to limitations.[361] These limitations are permitted "by implication since the right of access by its very nature calls for regulation by the State."[362]

197. For instance, in *Mondev* the tribunal confirmed that domestic laws limiting State liability do not necessarily amount to a denial of justice. That case dealt in part with a statutory provision conferring immunity to the Boston Redevelopment Authority ("BRA") for intentional torts under the *Massachusetts Tort Claims Act*.[363] The tribunal explained that one important question was "the rationale for the BRA's immunity."[364] With respect to the facts of the case and the statutory immunity conferred to the BRA for tortious interference with contractual relations, the tribunal concluded that it did not amount to a denial of justice since "reasons can well be imagined why a legislature might decide to immunize a regulatory authority, mandated to deal with commercial redevelopment plans, from potential liability for tortious interference."[365] The tribunal found that statutory immunity from liability was justified because allowing claims for tortious interference could result in "a distraction to the work of the Authority."[366] It added that "the extent to which a State decides to immunize regulatory authorities from suit for interference with contractual relations is a matter for the competent organs of the State to decide."[367]

198. In addition, the exhaustion of local remedies is a condition precedent to a finding of denial of

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[361] **RL-52**, Jan Paulsson, "Denial of Justice in International Law" (Cambridge University Press, 2005), p. 140. One approach to assessing the severity of an alleged denial of justice in the case of a sovereign immunity clause is to examine whether the limitation on access to a court is in furtherance of a legitimate aim and whether the means employed are proportionate to that aim. **RL-53**, Andrea K. Bjorklund, "Reconciling State Sovereignty and Investor Protection in Denial of Justice Claims", 45:4 Virginia Journal of International Law 809, pp. 864, 878-879.

[362] **R-75**, *McElhinney v. Ireland*, 21 November 2001, (2001) 34 EHRR 322, ¶ 34, cited by **RL-52**, Jan Paulsson, "Denial of Justice in International Law" (Cambridge University Press, 2005), pp. 140-141.

[363] **CL-56**, *Mondev – Award*, ¶ 139.

[364] **CL-56**, *Mondev – Award*, ¶ 145.

[365] **CL-56**, *Mondev – Award*, ¶ 153.

[366] **CL-56**, *Mondev – Award*, ¶ 153.

[367] **CL-56**, *Mondev – Award*, ¶ 154.

justice by a State,[368] including under the NAFTA.[369] For instance, in *Loewen*, the tribunal concluded that the United States did not commit a denial of justice against Mr. Loewen even if "the conduct of the trial by the trial judge was so flawed that it constituted a miscarriage of justice amounting to a manifest injustice."[370] The tribunal reached this conclusion because Mr. Loewen had not exhausted all local remedies by failing to apply to the US Supreme Court to appeal the Mississippi decision.[371]

199. It clarified that this requirement should be understood as an "obligation to exhaust remedies which are effective and adequate and are reasonably available to the complainant in the circumstances in which it is situated."[372] The tribunal concluded that the exhaustion of local remedies is essential in order to "afford the State the opportunity of redressing through its legal system the inchoate breach of international law occasioned by the lower court decision."[373]

3. The Claimants Have Failed to Establish a Violation of Article 1105

a) Ontario's Decision to Wind Down the Cap and Trade Program Was Not Abrupt and Followed a Legitimate Democratic Process

200. The Claimants allege that Ontario's decision to cancel the cap and trade program was "abrupt" and "sudden" and the result of a political decision; in doing so they suggest the measure was manifestly arbitrary and therefore in breach of NAFTA Article 1105.[374] The Claimants' arguments are incorrect and rely on mischaracterizations of the facts.

201. Even before the start of the electoral campaign on May 8, 2018,[375] the leader of the

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[368] **RL-54**, Chittharanjan F. Amerasinghe, "Local Remedies in International Law" (Cambridge University Press, 2nd ed. 2004), p. 100.

[369] **RL-51**, Dumberry: A Guide to NAFTA Case Law on Article 1105, p. 33.

[370] **CL-68**, *Loewen – Award*, ¶ 54.

[371] **CL-68**, *Loewen – Award*, ¶ 217.

[372] **CL-68**, *Loewen – Award*, ¶ 168.

[373] **CL-68**, *Loewen – Award*, ¶ 156.

[374] Claimants' Memorial, ¶¶ 357, 359.

[375] The Lieutenant Governor of Ontario accepted Premier Kathleen Wynne's advice to sign a Proclamation dissolving the 41st Parliament of the Province of Ontario on May 8th 2018. **R-30**, Ontario Newsroom, Ontario Election on June 7, 2018, 8 May 2018.

Progressive Conservative Party of Ontario, Mr. Doug Ford, made it clear that he would cancel the cap and trade program if elected. In a declaration made on April 23, 2018, Mr. Ford confirmed his intention of cancelling the program[376] and repeated this promise several times, making it one of the central themes of his campaign.[377] Mr. Ford stated that he was opposed to the cap and trade program because it was driving gas prices up, which in turn "increase[d] the cost of transporting everyday items such as food products […] as well as […] other goods and services" and affected to a greater extent "[l]ower income individuals and families."[378] The Party's platform called for "protect[ing] our environment without making life unaffordable for families", and in particular included a promise to "dismantle Cap-and-Trade" and "withdraw from the Western Climate Initiative".[379]

202. Once in power, in order to proceed with the orderly wind-down of the cap and trade program, Ontario followed a principled approach that treated every category of participant fairly and in a non-arbitrary manner. First, on July 3, 2018, Regulation 386/18 came into force and stipulated that "no registered participant shall, on and after the day this Regulation comes into force, purchase, sell, trade or otherwise deal with emission allowances and credits." This effectively meant that no participant in the Ontario cap and trade program, including KS&T, could transfer emission allowances held in an Ontario CITSS account.

203. Second, on July 25, 2018, Bill 4 was introduced into the Ontario Legislature.[380] In addition to the legislative process which consisted of three readings and a committee stage, Bill 4 was also posted on the Environmental Registry for public comment on September 11, 2018.[381] Stakeholders had thirty

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[376] **R-34**, PC Party of Ontario, Doug Ford Will Fight a Carbon Tax and Scrap Kathleen Wynne's Cap and Trade' Slush Fund, 23 April 2018.

[377] **R-77**, Ontario PC Party, "Statement from Ontario PC Leader Doug Ford on the Carbon Tax", 25 April 2018; **R-35**, Ontario PC Party, "Doug Ford's Plan for the People Will Put More Money in the Pockets of Ontario Parents", 28 April 2018; **R-78**, Ontario PC Party, "Doug Ford will Cut Gas Taxes by Ten Cents Per Litre", 16 May 2018; **R-79**, Ontario PC Party, Doug Ford Formally Commits to Reducing Taxes for Ontario Families, 24 May 2018; **R-80**, Ontario PC Party, "NDP Will Increase Gas & Hydro Bills, Ontario PCs Will Reduce Them", 30 May 2018.

[378] **R-78**, Ontario PC Party, "Doug Ford will Cut Gas Taxes by Ten Cents Per Litre", 16 May 2018, p. 1.

[379] **R- 32**, PC Party of Ontario, "People's Guarantee", p. 25.

[380] **R-57**, Bill 4.

[381] **R-57**, Bill 4; **C-12**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018, pp. 1, 10.

days to comment and over 10 000 comments were received in relation to Bill 4. The MECP reviewed, analyzed and summarized these comments, including the comments received from Koch Industries.[382] On October 31, 2018, the Cancellation Act received Royal Assent.

204. The Claimants cannot credibly argue that Ontario's decision to wind down the cap and trade programt was "sudden", "unexpected" or "abrupt", or that it was manifestly arbitrary.

b) Ontario's Policy Choices to Replace the Cap and Trade Program Were Made in Good Faith and in Pursuit of Legitimate Policy Objectives

205. Contrary to the Claimants' allegations, Ontario's actions with respect to the winding down of the cap and trade program were made in good faith and for legitimate policy reasons, including that the existing program imposed economically inefficient burdens on Ontarians. The compensation scheme was also designed based on legitimate policy reasons, and was neither arbitrary nor discriminatory. As explained by Mr. Wood in his witness statement, Ontario provided compensation for participants that had compliance obligations and were required to participate in the cap and trade program.[383] Participants including fuel suppliers, natural gas distributors and electricity importers as well as market participants were excluded from compensation. The decision to exclude certain categories of participants from compensation was based on rational policy aims informed by the regulatory purpose of cap and trade system, and not on discriminatory grounds.

206. The Claimants also argue that Ontario acted in bad faith with respect to the Harmonization Agreement.[384] The Claimants' characterization of Ontario's obligations and supposed "bad faith" is baseless. The Harmonization Agreement recognized each Party's sovereignty and was non-binding. Indeed, the Preamble stated that nothing in the Agreement could be interpreted as to "restrict, limit or otherwise prevail over […] each Party's sovereign right and authority to adopt, maintain, modify, repeal or revoke any of their respective program regulations or enabling legislation."[385] There is no basis on which to allege that Ontario acted in "bad faith" with respect to the Harmonization

[382] **R-57**, Bill 4; **C-12**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018; **RWS-1**, Wood – Witness Statement, ¶¶ 26-27.

[383] **RWS-1**, Wood – Witness Statement, ¶ 22.

[384] Claimants' Memorial, ¶ 363.

[385] **R-25**, Harmonization Agreement, Preamble.

Agreement.

c) Ontario Did Not Frustrate Any Legitimate Expectations Held by the Claimants

207. The Claimants argue that Ontario created legitimate expectations because it "promoted the role of market participants in Cap and Trade" and because of the "Ontario government's repeated and specific encouragement of participation of market participants in the market."[386] They further allege that "[a]ll of these actions created an expectation that Ontario understood, valued and respected the role market participants like KS&T played in ensuring the success of the Cap and Trade Program."[387]

208. However, the evidence clearly shows that Ontario did not "chase" KS&T or any other market participant to encourage them to participate in the cap and trade program.[388] Ontario published guidance materials[389] and held several information sessions ahead of the launch of the cap and trade program to help all interested stakeholders register in time. Various formalities had to be met in order for interested participants to take part in the first auction.[390] Holding information sessions for anyone potentially interested in participating in the cap and trade program does not amount to specific assurances given by the host State.

209. In addition, when KS&T registered as a market participant in Ontario, it knew it was a highly

[386] Claimants' Memorial, ¶ 392.

[387] Claimants' Memorial, ¶ 393.

[388] Claimants' Memorial, ¶ 111.

[389] *See, e.g.,* **C-30**, Ontario Government, "What you need to know about Ontario's carbon market using a cap and trade program, including how it works and who is required to participate", 2 June 2016, updated 8 June 2021: "Even if your company doesn't have emissions to report, you can still participate in the auction as a market participant. Market participants can include individuals, not-for-profit organizations and companies without compliance obligations."; **C-31**, Ontario Government, "Cap and Trade CITSS Registration", 15 July 2016, updated 12 July 2021: "Capped and Market Participants of the Ontario cap and trade program are required to open CITSS."; **C-32**, Ontario Government, "Cap and Trade: Register and Participate in CITSS", 20 July 2016, updated 2019: "Market participants can apply any time for CITSS registration."; **C-35**, Ontario Government, "Cap and Trade: Auction of Allowances", 31 October 2016: "You must be registered and approved in the Compliance Instrument Tracking System Service (CITSS) […] as a mandatory, voluntary or market participant of Ontario's cap and trade program before you can participate in an auction."

[390] *See, e.g.,* **C-34**, Email from MOECC, "Ontario Cap and Trade Registration Deadline", 30 September 2016: "Dear Ontario cap and trade program stakeholder: […]".

regulated and uncertain program. KS&T was on notice that "no right to compensation" and "no right to payment" existed before it decided to participate in the program. KS&T could not have had any expectations that it could be compensated in relation to the emission allowances it bid for through its Ontario CITSS account.[391]

210. More generally, the operation of cap and trade programs has always been uncertain. Political opposition in Canada and elsewhere, as well as States' decision in recent years to leave regional initiatives (*e.g.* New Jersey withdrew from RGGI) show the uncertainty surrounding the cap and trade programs.[392] Finally, starting at the end of 2017, there were clear indications that the cap and trade program in Ontario could be terminated.[393] Considering the risks and political uncertainty associated with the cap and trade program in Ontario, KS&T cannot credibly argue it had legitimate expectations in relation to the cap and trade program when it decided to participate in the May 2018 auction.[394]

211. Finally, the Claimants argue that a statement made by the Premier-Designate that once in office, the new government "[would] provide clear rules for the orderly wind down of the cap-and-trade program", created legitimate expectations that KS&T would receive compensation.[395] The phrase "orderly wind down" is not a promise or assurance that every participant will be compensated; it does not even address the question of compensation. Moreover, these statements were made after any alleged investment from KS&T.

212. Therefore, even if legitimate expectations are considered as a "relevant factor", the Claimants have failed to demonstrate that any assurances were given to them by Ontario to induce an investment.

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[391] **R-6**, *Climate Change Act*, ss. 70(1), (2).

[392] **RER-2**, Litz - Expert Report, ¶¶ 119, 122, 145; **CER-1**, Expert Report of Dr. Robert Stavins, 5 October 2021 ("Stavins Report"), ¶ 33.

[393] *See* Section II.B.1 and Section IV.A.3(a).

[394] Nor could the Harmonization Agreement have created any legitimate expectations for the Claimants. The Harmonization Agreement did not even create binding obligations amongst the three Parties. The objective of the Agreement was for the Parties to "work jointly and collaboratively toward the harmonization and integration of the Parties' greenhouse gas emissions reporting programs and cap-and-trade programs for reducing greenhouse gas emissions." **R-25**, Harmonization Agreement, Art. 1. The Harmonization Agreement certainly did not create any rights for third parties, such as participants in the cap and trade program, including KS&T. And, as discussed above, the Harmonization Agreement did not impose any conditions on a Party's withdrawal.

[395] Claimants' Memorial, ¶¶ 397, 398.

The Claimants cannot sustain the argument that their legitimate expectations were violated.

d) The Claimants Have Not Established a Denial of Justice

213. The requirement for a foreign investor to exhaust local remedies before it can bring a denial of justice claim against a host state is well-established. Failure to comply with this requirement precludes a finding that a State has committed a denial of justice. Here, the Claimants could have challenged the wind-down of the program and the enactment of the *Cancellation Act* in domestic court, as have other market participants[396], but they chose not to exhaust local remedies before bringing a claim under NAFTA Article 1105. Their denial of justice claim should therefore be rejected.

214. In addition, as noted above, under NAFTA Article 1105 only situations which "shock or surprise" and give rise "to justified concerns as to the judicial propriety of the outcome", will be considered a denial of justice.[397] Section 10(1) of the *Cancellation Act* provides that "[n]o cause of action arises against the Crown" as a result of the repeal of the *Climate Change Act*, the retirement of cap and trade instruments, or any acts or emissions relating to "the wind down of the cap and trade program".[398] As a corollary, section 10(2) provides that no proceedings "may be brought or maintained against the Crown" in relation to such causes of action.[399]

215. Section 10 of the *Cancellation Act* is, on its face and unless found otherwise by Canadian courts, constitutional and valid. While the fact that it is *prima facie* constitutional and valid in Canada is not determinative for this Tribunal, it should nonetheless inform the Tribunal's analysis as to whether section 10 rises to a level that it constitutes a denial of justice under international law.

216. Crown immunity provisions have historically been considered valid and constitutional in Canada for several reasons. The first is that Parliament is sovereign: the legislature can do as it sees

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[396] **R-81**, SMV Energy Solutions, Notice of class proceeding including a claim for damages pursuant to s. 18(1) of the Crown Liability and Proceedings Act, December 16, 2020; **R-82**, *SMV Energy Solutions v. Ontario*, ONSC, Amended Statement of Claim, 28 July 2021.

[397] **CL-56**, *Mondev – Award*, ¶ 127; *see also* **CL-68**, *Loewen – Award*, ¶ 132.

[398] *Cancellation Act*, s.10, "No cause of auction".

[399] *Cancellation Act*, s.10, "No cause of auction".

fit and adopt any statute within constitutional boundaries. Courts can only review the constitutionality of statutes, not their reasonableness nor whether a statute is desirable. This was recognized by the Supreme Court of Canada in *Reference re Resolution to Amend the Constitution*, where it explained that the idea that Parliament is sovereign and free from judicial intervention was recognized as early as 1689.[400] In *Wells v. Newfoundland*, the Supreme Court of Canada affirmed the power of Parliament and provincial legislatures to adopt any statute, within constitutional boundaries, without being subject to review by courts: "legislative decision making is not subject to any known duty of fairness. Legislatures are subject to constitutional requirements for valid law-making, but within their constitutional boundaries, they can do as they see fit. The wisdom and value of legislative decisions are subject only to review by the electorate."[401]

217. The second reason is that historically, at common law, the Crown was entirely immune from private lawsuits and no cause of action could be asserted against it.[402] As stated by the Supreme Court of Canada, "both Parliament and the provincial legislatures have gradually placed limits on this immunity in order to draw the legal position of the Crown and its servants closer to that of other Canadian litigants."[403] Statutes allowing lawsuits against the Crown were mostly enacted following the Second World War.[404] However, "the Crown is not in exactly the same legal position as ordinary

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[400] **R-83**, *Reference re Resolution to Amend the Constitution*, [1981] 1 S.C.R. 753, 28 September 1981, p. 785 ("It would be incompatible with the self-regulating — "inherent" is as apt a word — authority of Houses of Parliament to deny their capacity to pass any kind of resolution. Reference may appropriately be made to art. 9 of the *Bill of Rights* of 1689, undoubtedly in force as part of the law of Canada, which provides that "Proceedings in Parliament ought not to be impeached or questioned in any Court or Place out of Parliament").

[401] **R-84**, *Wells v. Newfoundland*, [1999] 3 S.C.R. 199, 15 September 1999, ¶ 59; Relying in part on these decisions, the Supreme Court of Canada also explained in *Authorson v. Canada (Attorney General)*, a case that recognized the constitutionality of a provision that insulated the Crown from any cause of action arising from the breach of a statute, that "[l]ong-standing parliamentary tradition makes it clear that the only procedure due any citizen of Canada is that proposed legislation receive three readings in the Senate and House of Commons and that it receive Royal Assent. Once that process is completed, *legislation within Parliament's competence is unassailable*." It also clarified that "Court interference with the legislative process is not an interpretation of an already enacted law." **R-85**, *Authorson v. Canada (Attorney General),* [2003] 2 S.C.R. 40, 17 July 2003, ¶¶ 37, 40. (emphasis added).

[402] **R-87**, *Just v. British Columbia*, [1989] 2 S.C.R. 1228, [1989] S.C.J. No. 121, 7 December 1989, p. 1239

[403] **R-86**, *Canada (Attorney General) v. Thouin*, 2017 SCC 46, [2017] 2 S.C.R. 184, 28 September 2017, ¶ 1.

[404] **R-86**, *Canada (Attorney General) v. Thouin*, 2017 SCC 46, [2017] 2 S.C.R. 184, 28 September 2017, ¶ 23: "In about 1950, Parliament, drawing on the *Crown Proceedings Act, 1947* (U.K.), 10 & 11 Geo. 6, c. 44, that had been enacted in the United Kingdom, began to impose limits on the scope of the common law Crown immunity. In 1953, it passed

litigants, since it still retains certain residual privileges and immunities […]."[405] These residual privileges and immunities include notably Crown immunity from discovery in proceedings in which it is not a party to, Crown immunity for true policy decisions based on upon social, political or economic factors, and Crown immunity conferred by statute which removes any cause of action arising from the breach of a statute or other tortious liability.[406]

218. Section 10 of the *Cancellation Act* is also in furtherance of a legitimate aim, is non-discriminatory, and is in keeping with the associated regulatory regime. In *Mondev*, the tribunal confirmed that statutory immunity provisions will be justified under certain circumstances, including where allowing liability claims could result in "a distraction to the work of the [Government]."[407] The Crown immunity provision in the *Act* applies equally to all categories of participants – mandatory, voluntary and market participants – as well as to foreign and domestic entities. Finally, section 10 is in line with sections 69 and 70 of the *Climate Change* Act, which had already put participants on notice that certain proceedings against the Crown would not be authorised and that they had no right to compensation or to any payment as set out in that *Act*.[408]

219. In sum, the Claimants have failed to meet the "high threshold of severity" for a finding that a host State committed a denial of justice. Their claim of a violation of NAFTA Article 1105 based on an alleged denial of justice should be dismissed.

B. The Claimants Have Failed to Establish a Breach of Article 1110

1. Summary of Canada's Position

220. The Claimants allege that Canada has indirectly expropriated the Claimants' investments[409]

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the *Crown Liability Act*, S.C. 1952-53, c. 30 (Morley, at p. 1-41; Hogg, Monahan and Wright, at p. 9), which had the effect of expanding Crown liability and thus bringing the Crown's legal position closer to that of ordinary litigants."

[405] **R-86**, *Canada (Attorney General) v. Thouin*, 2017 SCC 46, [2017] 2 S.C.R. 184, 28 September 2017, ¶ 23.

[406] **R-87**, *Just v. British Columbia*, [1989] 2 S.C.R. 1228, [1989] S.C.J. No. 121, 7 December 1989, p. 1239; **R-86**, *Canada (Attorney General) v. Thouin*, 2017 SCC 46, [2017] 2 S.C.R. 184, 28 September 2017, ¶ 43.

[407] **CL-56**, *Mondev – Award*, ¶ 153.

[408] *Climate Change Act*, ss. 69, 70.

[409] The Claimants' allegations with respect to Article 1110 do not concern any alleged "investments" of Koch Industries. Their arguments on expropriation are limited to "the carbon allowances held in KS&T's Ontario CITSS account as of 15

through the Premier-Designate's announcement (on June 15, 2018) and Regulation 386/18 (on July 3, 2018).[410] The Claimants also posit an "alternative case" that the emission allowances were directly expropriated through the enactment of the *Cancellation Act* (on October 31, 2018).[411] These allegations are unfounded and must be rejected.

221. As explained in **Section 2**, NAFTA Chapter Eleven incorporates customary international law rules on expropriation, and NAFTA Parties have reaffirmed the principles applicable to expropriation claims in later treaties.

222. In **Section 3**, Canada explains that the Claimants have failed to demonstrate the existence of any investment capable of being expropriated. The emission allowances that KS&T held in its Ontario CITSS account did not confer property rights under Ontario law and hence are not capable of being expropriated. Moreover, KS&T's alleged "carbon trading business in Ontario",[412] "business model in Ontario"[413], and "ability to trade more broadly in the carbon market in Ontario"[414] did not themselves constitute property rights.

223. Because KS&T held no property rights capable of being expropriated, the analysis under NAFTA Article 1110 should end there. However, even if the Tribunal finds that KS&T held property rights capable of being expropriated, the claim for breach of Article 1110 must fail for the reasons set out in **Section 4**.

224. First (**a**), Ontario did not interfere with the Claimants' alleged distinct, reasonable investment-backed expectations.[415] The 2016 legislation that created Ontario's cap and trade system was clear:

June 2018" and KS&T's alleged "carbon trading business in Ontario". *See* Claimants' Memorial, ¶¶ 401-402, 408-411, 418, 420-421.

[410] Claimants' Memorial, ¶ 401. It is unclear whether the Claimants' argument is that these two events, taken together, constitute "an" expropriation, or whether the two events are presented as alternatives.

[411] Claimants' Memorial, ¶ 460.

[412] Claimants' Memorial, ¶¶ 323(a), 402, 409, 491. In their arguments on valuation, the Claimants also refer to KS&T's alleged "Ontario emission trading business". *See* Claimants' Memorial, pp. iii, 145 and ¶ 490.

[413] Claimants' Memorial, ¶¶ 201, 409.

[414] Claimants' Memorial, ¶ 418.

[415] *See* Claimants' Memorial, ¶¶ 410-411.

no compensation would be payable for anything done or not done under the *Climate Change Act* and regulations and no such action would constitute an expropriation. The Claimants cannot credibly claim that KS&T had an expectation that it would be compensated if Ontario chose to pursue a different environmental policy.

225. Second (**b**), nothing Ontario did on June 15, 2018 substantially deprived the Claimants of the economic value of their alleged property rights in Ontario.

226. Third (**c**), Ontario's measures represent a valid exercise of the Ontario government's police powers. Ontario's measures were non-discriminatory and were designed and applied to protect a legitimate public welfare objective: to replace the cap and trade program with a new environmental policy intended to address challenges posed by climate change in a more economically efficient way.

227. Fourth (**d**), there was no State-sanctioned compulsory transfer of property from the Claimants to either the government or a State-mandated third party. Ontario did not "take" any of the Claimants' alleged investments and did not receive any benefit from the effect of Regulation 386/18 on the emission allowances held in KS&T's Ontario CITSS account.

2. NAFTA Article 1110(1) Incorporates Customary International Law Rules on Expropriation

228. NAFTA Article 1110(1) provides:

> No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ("expropriation"), except:
>
> (a) for a public purpose;
>
> (b) on a non-discriminatory basis;
>
> (c) in accordance with due process of law and Article 1105(1); and
>
> (d) on payment of compensation in accordance with paragraphs 2 through 6.

229. NAFTA does not define "expropriation", but NAFTA tribunals and the NAFTA Parties have

interpreted Article 1110(1) as incorporating customary international law rules.[416] Article 1110 covers both direct and indirect expropriations. It is also clearly established that the scope of Article 1110 is not broadened by the phrase "measure tantamount to nationalization or expropriation".[417]

230. NAFTA tribunals have generally applied a three-step analysis to determine whether a Party's measures have breached the standards of Article 1110(1).[418] First, the Tribunal must identify the investment that is capable of being expropriated. Second, the Tribunal must determine whether that investment has been expropriated. Third, if the Tribunal finds that there was an expropriation,[419] it must determine whether it was lawful under the conditions set out in Article 1110(1)(a) through (d)).

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[416] **CL-18**, *Glamis Gold, Ltd. v. The United States of America* (UNCITRAL) Award, 8 June 2009 ("*Glamis Gold – Award*"), ¶ 354: "The inclusion in Article 1110 of the term 'expropriation' incorporates by reference the customary international law regarding that subject"; **CL-79**, *Archer Daniels Midland Company v. The United Mexican States* (ICSID Case No. ARB(AF)/04/05) Award, 21 November 2007 ("*ADM – Award*"), ¶ 237: "The key terms in Article 1110 – 'nationalization,' 'expropriation,' and 'measures tantamount thereto' – are not defined in the NAFTA. The interpretation of these terms requires an analysis of the applicable rules of international law, in accordance with Article 1131 of the NAFTA."; **CL-12**, *Waste Management – Award*, ¶ 177: referring to "the international law of expropriation as reflected in Article 1110". *See also* the positions of the NAFTA Parties on this issue: **RL-55**, *Metalclad Corporation v. The United Mexican States*, (ICSID Case No. ARB(AF)/97/1) Submission of the Government of the United States of America, 9 November 1999, ¶ 10: "The United States Government believes that it was the intent of the Parties that Article 1110(1) reflect customary international law as to the categories of expropriation."; **RL-56**, *Mondev International Ltd. v. United States of America* (ICSID Case No. ARB(AF)/99/2), Second Submission of Canada pursuant to NAFTA Article 1128, 7 July 2001, ¶¶ 64-65: defining "expropriation" in Article 1110 with reference to international law; **RL-57**, *Methanex Corporation v. The United States of America* (UNCITRAL) Mexico Fourth Submission pursuant to NAFTA Article 1128, 30 January 2004, ¶ 13: "Article 1110, which must be interpreted in accordance with the applicable rules of customary international law, incorporates the principle that States generally are not liable to compensate aliens for economic loss resulting from non-discriminatory regulatory measures taken to protect the public interest, including human health."

[417] **CL-18**, *Glamis Gold Ltd. v. United States of America* (UNCITRAL) Final Award, 8 June 2009 ("*Glamis Gold – Award*"), ¶ 355: "'Tantamount' means equivalent and thus the concept should not encompass *more* than direct expropriation; it merely differs from direct expropriation which effects a physical taking of property in that no actual transfer of ownership rights occurs." (emphasis in original).

[418] *See for example* **CL-67**, *Chemtura – Award*, ¶¶ 242 and 257; **CL-69**, *Joshua Dean Nelson v. United Mexican States* (ICSID Case No. UNCT/17/1) Final Award, 5 June 2020 ("*Nelson – Award*"), ¶ 222: "To determine the existence of an unlawful expropriation in breach of NAFTA Article 1110(1), the Tribunal will follow a three-prong test that consists in asking: '(i) whether there is an investment capable of being expropriated, (ii) whether that investment has in fact been expropriated, and (iii) whether the conditions set [forth] in Article 1110(1)(a)-(d) have been satisfied.'"

[419] **CL-88**, *Fireman's Fund Insurance Company v. United Mexican States* (ICSID Case No. ARB(AF)/02/01) Award, 17 July 2006, ¶ 174: "Paragraphs (a) through (d) do not bear on the question as whether an expropriation has occurred. Rather, the conditions contained in paragraphs (a) through (d) specify the parameters as to when a State would not be liable under Article 1110."; **RL-58**, *Corn Products International Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/04/01) Decision on Responsibility, 15 January 2008, ¶ 89: "[I]t is important not to confuse the question whether there has been an expropriation with that of whether the four criteria in paragraphs (a) to (d) of Article 1110 have been satisfied. Those paragraphs come into play only if it has been decided that there has been an expropriation, or a measure tantamount to an expropriation, but the absence of one or more of them is not in itself indicative of expropriation."

The burden of proving the existence of an investment capable of being expropriated[420] and the substantial deprivation of that investment[421] rests with the party alleging the expropriation.[422]

231. The NAFTA Parties' understanding of what constitutes an expropriation under Article 1110 is also reflected in the CUSMA, a treaty to which all three NAFTA Parties are party. CUSMA Annex 14-B (Expropriation) and similar provisions in other treaties entered into by NAFTA Parties[423] confirm what the NAFTA Parties mean and have always meant by the term "expropriation".[424] They "do not change the nature of the substantive obligations that existed under […] prior agreements; instead, they merely elucidate, for the benefit of tribunals charged with interpreting the treaty, the

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[420] **CL-10**, *Emmis – Award*, ¶ 173: "[T]he Claimants bear the burden of proving that they owned an investment capable of expropriation."

[421] **CL-129**, *Middle East Cement Shipping and Handling Co. v. Arab Republic of Egypt* (ICSID Case No. ARB/99/6) Award, 12 April 2002, ¶¶ 89-90; **RL-59**, *Link-Trading Joint Stock Company v. Republic of Moldova* (UNCITRAL) Final Award, 18 April 2002, ¶ 87; **RL-60**, *Tokios Tokelés v. Ukraine* (ICSID Case No. ARB/02/18) Award, 26 July 2007, ¶¶ 121-122.

[422] Once the State has brought *prima facie* evidence of a legitimate exercise of police powers, the burden falls to the claimant to establish that the exercise was not legitimate: **RL-61**, *Les Laboratoires Servier, S.A.A., Biofarma, S.A.S., Arts et Techniques du Progres S.A.S. v. Republic of Poland* (UNCITRAL) Final Award, 14 February 2012, ¶¶ 583.

[423] *See* **RL-62**, Comprehensive and Progressive Agreement for Trans-Pacific Partnership ("CPTPP"), Annex 9-B: Expropriation (both Canada and Mexico are party to the CPTPP); **RL-63**, Treaty between the Government of the United States of America and the Government of the Republic of Rwanda Concerning the Encouragement and Reciprocal Protection of Investment, (2008), in force 1 January 2012, Annex B: Expropriation; **RL-64**, United States – Panama Trade Promotion Agreement, (2007), in force 31 October 2012, Chapter Ten, Annex 10-B Expropriation; **RL-65**, United States – Colombia Trade Promotion Agreement, (2006), in force 15 May 2012, Chapter Ten, Annex 10-B Expropriation. *See also* **RL-66**, The Agreement Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment, (2012), Annex B: Expropriation; **RL-67**, Canada's 2021 Foreign Investment Promotion and Protection Agreement (FIPA) Model, (2021), Art. 9(2), (3) and (4).

[424] *See* **CL-18**, *Glamis Gold – Award*, ¶ 356: the tribunal referred to the Annex of the United States model treaty to decide whether the impugned measure was expropriatory. *See* **RL-68**, *Methanex Corporation v. United States of America* (UNCITRAL) Amended Statement of Defence of Respondent United States of America, 5 December 2003, ¶ 405, FN 636; **RL-69**, *Glamis Gold, Ltd. v. United States of America* (UNCITRAL) Counter-Memorial of the United States of America, 19 September 2006, pp. 159-160, FN 740; **RL-70**, *Grand River Enterprises v. United States of America* (UNCITRAL) Counter-Memorial of the United States of America, 22 December 2008, p. 147, FN 524; **CL-62**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL), Government of Canada, Rejoinder Memorial, 6 November 2015, ¶ 9: "[T]he lack of such an annex in the NAFTA is irrelevant. These annexes merely explain what the NAFTA Parties mean and have always meant by the term 'indirect expropriation', as affirmed by other submissions."; **CL-87**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL) Government of Canada, Counter-Memorial, 20 January 2015, ¶ 475: "[W]hile the NAFTA does not contain the same annex, the factors laid out in these recent interpretative texts provide useful guidance to assess whether there has been an indirect expropriation in this case."; **RL-71**, *Odyssey Marine Exploration, Inc. v. United Mexican States* (ICSID Case No. UNCT/20/1) Non-Disputing Party Submission of the Government of Canada pursuant to NAFTA Article 1128, 2 November 2021, ¶¶ 28, 31 and FN 39, 45.

Parties' intent in agreeing to those obligations."[425] Therefore, the Tribunal may rely on these annexes in interpreting NAFTA Article 1110.[426]

232. In CUSMA Annex 14-B (Expropriation), the Parties "confirm[ed] their shared understanding" that "[a]n action or a series of actions by a Party cannot constitute an expropriation unless it interferes with a tangible or intangible property right[427] or property interest in an investment."[428] The Parties share the understanding that "[n]on-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations, except in rare circumstances."[429]

3. The Claimants' Expropriation Claim Fails Because There Was No "Investment" Capable of Expropriation

233. The first step in analysing whether there has been a breach of Article 1110 is to identify the specific investment alleged to have been expropriated[430] and determine whether there is a valid property right capable of being expropriated.[431] The Claimants entirely ignore this critical threshold

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[425] **RL-72**, Andrea J. Menaker, "Benefiting From Experience: Developments in the United States' Most Recent Investment Agreements" (2006), 12:1 U.C. Davis J. Int'l L. Pol'y 121, p. 122: Ms. Menaker is former Chief of the NAFTA Arbitration Division in the Office of the Legal Adviser for the U.S. Department of State; **RL-73**, Andrew Newcombe, "Canada's New Model Foreign Investment Protection Agreement", August 2004, pp. 5-6.

[426] See **RL-29**, *Vienna Convention on the Law of Treaties,* Article 31(3)(c): "There shall be taken into account, together with the context […] any relevant rules of international law applicable in the relations between the parties."

[427] **RL-74**, Canada United States Mexico Agreement ("CUSMA"), Annex 14-B: Expropriation, FN 18: "For greater certainty, the existence of a property right is determined with reference to a Party's law."

[428] **RL-74**, CUSMA, Annex 14-B: Expropriation, ¶ 1.

[429] **RL-74**, CUSMA, Annex 14-B: Expropriation, ¶ 3(b).

[430] **RL-75**, *Generation Ukraine v. Ukraine* (ICSID Case No. ARB/00/9) Award, 16 September 2003 ("*Generation – Award*"), ¶ 6.2: "Since expropriation concerns interference in rights in property, it is important to be meticulous in identifying the rights duly held by the Claimant at the particular moment when allegedly expropriatory acts occurred."; **RL-76**, *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v Islamic Republic of Pakistan* (ICSID Case No. ARB/03/29) Award, 27 August 2009 ("*Bayindir – Award*"), ¶ 442: "The first step in assessing the existence of an expropriation is to identify the assets allegedly expropriated."

[431] **RL-75**, *Generation – Award*, ¶ 8.8: "[T]here cannot be an expropriation unless the complainant demonstrates the existence of proprietary rights in the first place."; **CL-67**, *Chemtura – Award*, ¶ 258: "The first issue is whether the Claimant had an investment in Canada capable of being expropriated."; **CL-115**, *Crystallex – Award*, ¶ 659: "The Tribunal starts its analysis on expropriation with the threshold question as to whether the Claimant had rights capable of being expropriated."; **RL-77**, *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. Hungary* (ICSID Case No. ARB/12/2) Decision on Respondent's

question. This failure is fatal to the Claimants' expropriation claim.

234. Neither the emission allowances held in KS&T's Ontario CITSS account, nor KS&T's alleged "carbon trading business", "business model", or "ability to trade […] in the carbon market in Ontario" constitute investments capable of being expropriated.[432] It follows that Ontario could not have "expropriated" them within the meaning of NAFTA Article 1110.

a) The Enquiry into Whether There is an Investment Capable of Being Expropriated Is Independent from the Question of Whether There is an Investment under Article 1139

235. The concept of "expropriation", which is limited in customary international law to property capable of being expropriated, is not broadened by the definition of the term "investment" in NAFTA Article 1139.[433] Any party alleging a violation of Article 1110(1) must therefore demonstrate the existence of an "investment capable of being expropriated", independently of whether the claimant's

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Application for Bifurcation, 13 June 2013 ("*Emmis – Decision on Bifurcation*"), ¶ 43: "[T]he Tribunal would need to determine the nature and incidents of the rights held by Claimants that may be considered as investments capable of enjoying the protection of international law against expropriation before deciding whether Respondent's conduct had in fact caused any such expropriation."; **CL-10**, *Emmis – Award*, ¶ 159: "In view of the fact that the only cause of action within the Tribunal's jurisdiction is that of expropriation, Claimants must have held a property right of which they have been deprived. This follows from the ordinary meaning of the term."); **RL-78**, *Infinito Gold Ltd. v. Republic of Costa Rica* (ICSID Case No. ARB/14/5) Award, 3 June 2021 ("*Infinito – Award*"), ¶¶ 705-706: "[T]he Tribunal must first determine whether the Claimant […] held rights capable of being expropriated. If no valid rights exist under domestic law, there can be no expropriation."; **RL-79**, Rosalyn Higgins, "The Taking of Property by the State: Recent Developments in International Law", 176 R.C.A.D.I. 259 (1982), p. 272: "[O]nly *property* deprivation will give rise to compensation." (emphasis in original); **RL-80**, Rudolf Dolzer, "Indirect Expropriation of Alien Property", (1986) 1 ICSID Review – Foreign Investment Law Journal 41, (1986), p. 41: "Once it is established in an expropriation case that the object in question amounts to 'property,' the second logical step concerns the identification of 'expropriation.'"

[432] The Claimants have not argued that Ontario expropriated any of Koch Industries' alleged investments. *See* Claimants' Memorial, ¶¶ 322, 401-402, 408-411, 418, 420-421.

[433] **RL-81**, *Accession Mezzanine et al. v. Hungary* (ICSID Case No. ARB/12/3) Award, 17 April 2015 ("*Accession Mezzanine – Award*"), ¶ 75: "[T]he question of whether a protected investment […] is capable of being expropriated must be answered by reference to Article 6 ['Expropriation'] of the BIT and the general international law on expropriation."; **CL-19**, *Merrill & Ring – Award*, ¶ 139: "The first question the Tribunal must decide is whether the Investor's claim concerning expropriation relates to an investment as defined under the NAFTA treaty. NAFTA Chapter Eleven contains a broad definition of 'investment' as Article 1139 makes quite evident. […] However, the Tribunal is mindful that the protection of contractual rights [against expropriation] under international law has traditionally been understood within certain limits[.]"

investment is an "investment" within the meaning of Article 1139.[434]

236. In *European Media Ventures v. Czech Republic*, the tribunal clearly distinguished the question of whether an investment satisfies the jurisdictional conditions imposed by a treaty from that of whether an investment is capable of being expropriated:

> We wish to make clear […] that we consider the questions (a) whether the contractual rights on which the Claimant relies constitute an investment within Article 1 of the Treaty; (b) whether those rights are capable of expropriation under Article 3; and (c) whether they were in fact expropriated, to be *three entirely separate questions*.[435]

237. Therefore, even if the Tribunal were to find that KS&T has made an "investment" within the meaning of NAFTA Article 1139, the Tribunal must also consider whether each such "investment" is capable of being expropriated.

b) Domestic Law Determines the Property Rights Protected by NAFTA Article 1110(1)

238. International law does not create property rights.[436] Therefore, when faced with a claim of

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[434] **RL-82**, *European Media Ventures SA v. Czech Republic* (UNCITRAL) Partial Award on Liability, 8 July 2009 ("*European Media Ventures – Partial Award on Liability*"), ¶ 63: "There is no inconsistency in holding that rights to performance under a contract with a private party constitute an investment but not one which is capable of being expropriated."; **RL-77**, *Emmis – Decision on Bifurcation*, ¶ 43: "[I]t is of fundamental importance that the Tribunal identify precisely whether, and if so which investments of Claimants are capable of giving rise to their expropriation claim."; **RL-83**, *Accession Mezzanine et al. v. Hungary* (ICSID Case No. ARB/12/3) Decision on Respondent's Notice of Jurisdictional Objections and Request for Bifurcation, 8 August 2013, ¶ 39(2)(a): "The Tribunal is required to identify whether and which investments of Claimants may properly give rise to an expropriation claim[.]"; **RL-84**, UNCTAD Series on International Investment Agreements II, "Expropriation: A Sequel", (2012), p. 131: "Broad interpretation of the scope of economic interests capable of being expropriated may deviate from the original intention of the contracting States, clash with domestic tradition and complicate the process of valuation."

[435] **RL-82**, *European Media Ventures – Partial Award on Liability*, ¶ 41, FN 4 (emphasis added).

[436] **RL-26**, M. Sornarajah: The International Law on Foreign Investment, p. 383, note 67: "There is no indication of a theory of property in international law itself. International law does not create property in an individual. It relies upon municipal law for the recognition of property rights."; **RL-84**, UNCTAD Series on International Investment Agreements II, "Expropriation: A Sequel" (2012), p. 22: "Whether or not specified in the treaty, it is implicit that any investment susceptible to being expropriated must be a right or asset duly constituted, defined, formed and recognized under the laws of the host State that is granting the protection under the IIA […]. This is due to the fact that international law of expropriation is only concerned with the protection of property rights or other economic interests and does not regulate their process of creation."; **RL-25**, Douglas: Property, Investment and the Scope of Investment Protection Obligations, ¶ 1.150: "International law is concerned with the modalities of the exercise of sovereign power; it does not purport to create, define or regulate private rights over any type of property, whether intangible or tangible"; **RL-85**, John G. Sprankling,

expropriation, a NAFTA tribunal must first undertake a *renvoi* to the domestic law of the Party in question in order to determine the existence, nature, and scope of the property interests that the claimants allege were taken.[437] International arbitral tribunals have affirmed this principle.[438] If there is no property right at domestic law, then there is nothing that can be taken.[439] Similarly, any conditions and limitations inherent to an asserted property right may bear on whether there has been a taking of that property.[440]

c) Only Vested Property Rights Are Capable of Being Expropriated

239. NAFTA tribunals have maintained that an investment capable of being expropriated excludes a potential property right or one that is conditional, in that it may or may not materialize depending

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"The International Law of Property", (Oxford University Press, 2014), p. 3: "International law protects rights that arise under municipal law through uniform rules which safeguard […] foreign investments."

[437] **RL-86**, Andrew Newcombe & Lluis Paradell, "Law and Practice of Investment Treaties: Standards of Treatment" (2009) ("Newcombe: Law and Practise of Investment Treaties"), p. 351, ¶ 7.19: "The rights associated with any investment are normally determined by local law."; **RL-87**, Monique Sasson, "Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law", 2nd ed. (Kluwer Law International, 2017), p. 147: "International law classifies or identifies the property rights that fall under its umbrella of protection; municipal law governs the substantive aspects, including the existence and validity of a property right."; **RL-27**, McLachlan: Substantive Principles, ¶ 8.64: "The property rights that are the subject of protection under the international law of expropriation are created by the host State law. Thus, it is for the host State to define the nature and extent of property rights that a foreign investor can acquire."

[438] **CL-10**, *Emmis – Award*, ¶ 162: "In order to determine whether an investor/claimant holds property or assets capable of constituting an investment it is necessary in the first place to refer to host State law. Public international law does not create property rights."; **RL-88**, *EnCana Corporation v. Republic of Ecuador* (UNCITRAL) Award, 3 February 2006 ("*Encana – Award*"), ¶ 184: "[F]or there to have been an expropriation of an investment or return (in a situation involving legal rights or claims as distinct from the seizure of physical assets) the rights affected must exist under the law which creates them, in this case, the law of Ecuador."; **RL-89**, *Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal S.A. v. Argentina* (ICSID Case No. ARB/03/19) Decision on Liability, 30 July 2010 ("*Suez – Decision on Liability*"), ¶ 151; **RL-81**, *Accession Mezzanine – Award*, ¶ 75; **CL-106**, *Vestey Group Ltd v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB/06/4) Award, 15 April 2016, ¶ 257; **RL-24**, *Lion – Decision on Jurisdiction*, ¶ 231; **CL-69**, *Nelson – Award*, ¶¶ 228: "Claimant has the burden to prove that, under Mexican law, Tele Facil had the rights that Claimant considers were expropriated." and ¶ 280: "Claimant cannot claim that a right it does not have under Mexican law is capable of being expropriated."

[439] **RL-78**, *Infinito – Award*, ¶ 705: "If no valid rights exist under domestic law, there can be no expropriation."; **RL-50**, *Robert Azinian v. Mexico* (ICSID Case No ARB(AF)/97/2) Award, 1 November 1999, ¶ 100: "For if there is no complaint against a determination by a competent court that a contract governed by Mexican law was invalid under Mexican law, there is by definition no contract to be expropriated."; **RL-86**, Newcombe: Law and Practise of Investment Treaties, p. 351, ¶ 7.19: "Conceptually, property can only be expropriated if it exists. If a right was never acquired or has been otherwise extinguished under local law, it cannot be expropriated."

[440] **RL-76**, *Bayindir – Award*, ¶ 458: "[T]he fact that Bayindir was expelled is obviously not enough. As rightly pointed out by the Respondent, if the expulsion was lawful under the Contract, then there would be no taking of or interference with Bayindir's rights."

on a future event.[441] The Claimants agree that a "finding of indirect expropriation […] turns on whether the governmental measures have deprived the owner of substantially all of the benefits of its *vested rights*."[442]

240. The tribunal in *Feldman* adopted this approach in its analysis of the investor's claim under Article 1110. That tribunal stated that although the impugned measure prevented the claimant from exporting cigarettes, it was unclear whether the investor had ever possessed a vested right to export cigarettes, so it found that there was no expropriation.[443] Similarly, the *Thunderbird v. Mexico* tribunal explained that there can be no expropriation of an investment giving rise to compensation "where it can be established that the investor or investment never enjoyed a vested right in the business activity that was subsequently prohibited."[444]

241. The arbitral awards rendered under other investment treaties are to the same effect. For instance, the *Generation Ukraine v. Ukraine* tribunal stated that "[t]here cannot be an expropriation of something to which the Claimant never had a legitimate claim."[445] The *Emmis v. Hungary* tribunal similarly concluded that it "follows from the basic notion that an expropriation clause seeks to protect an investor from deprivation of his property that the property right or asset must have vested (directly or indirectly) in the claimant for him to seek redress."[446]

242. As explained below, because KS&T's "business model" and "ability to trade in emission

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[441] *See* **RL-90**, *Marvin Roy Feldman Karpa v. United Mexican States* (ICSID Case No ARB(AF)/99/1) Award, 16 December 2002 ("*Feldman – Award*"), ¶¶ 118 and 152; **RL-91**, *Eureko B.V. v. Poland* (UNCITRAL) Partial Award, 19 August 2005, ¶ 151; **CL-17**, *Thunderbird – Award*, ¶ 208; **CL-19**, *Merrill & Ring – Award*, ¶ 142; **CL-10**, *Emmis – Award*, ¶ 168; **RL-92**, *Eskosol S.p.A. in liquidazione v. Italian Republic* (ICSID Case No. ARB/15/50) Award, 4 September 2020, ¶¶ 470: "[A] finding of expropriation must be premised on a showing that 'Claimants must have held a property right of which they have been deprived.' The property right or asset in question 'must have vested (directly or indirectly) in the claimant for him to seek redress.'" and ¶ 472: "[A]bsent any *established right* that was abrogated by Government interference, the fact that Government conduct may have impacted a company business plan does not itself amount to expropriation, even if the end result ultimately is that the company was unable to survive financially." (emphasis in original).

[442] Claimants' Memorial, ¶ 405 (emphasis added).

[443] **RL-90**, *Feldman – Award*, ¶ 152.

[444] **CL-17**, *Thunderbird – Award*, ¶ 208.

[445] **RL-75**, *Generation – Award*, ¶ 22.1.

[446] **CL-10**, *Emmis – Award*, ¶ 168.

allowances" were not vested property rights, they were not capable of being expropriated within the meaning of NAFTA Article 1110.

d) KS&T Has Failed to Prove that It Held a Valid Property Right Capable of Being Expropriated

243. The Claimants' expropriation claim fails because there was no valid property right capable of being expropriated. The Claimants did not even attempt to prove otherwise.

244. The Claimants' allegations of expropriation focus on the emission allowances held in KS&T's Ontario CITSS account in June 2018.[447] These emission allowances, acquired at the May 2018 joint auction, were deposited into KS&T's Ontario CITSS account by each of the three participating jurisdictions.[448] As explained above and in the expert report of Professor Katz, an emission allowance is not a "property right" but rather a limited authorization to emit one tonne of GHG, serving as an immunity against penalty for non-compliance with the regulatory framework.[449] Therefore, emission allowances are not property rights capable of being expropriated.

245. This understanding of the rights at issue is further confirmed in sections 70(1) and (2) of the *Climate Change Act* which provide that "no person is entitled to be compensated for any loss or damages, including loss of revenues, loss of profit or loss of expected earnings" arising from actions relating to emission allowances and that "[n]othing done or not done in accordance with this Act or the regulations constitutes an expropriation or injurious affection for the purposes of the Expropriations Act or otherwise at law."[450] The Claimants ignore the fact that the legislation which

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[447] *See, e.g.*, Claimants' Memorial, ¶¶ 401-402, 418, 420.

[448] **RWS-2**, Ramlal - Witness Statement, ¶¶ 48, 57 and Attachment 1, transfers No. 126873, 127005, 127118, 127250, and 127362.

[449] *See* Section III.D.1 above; **RER-1**, Katz - Expert Report, ¶¶ 60-65; **RER-2**, Litz - Expert Report, ¶¶ 46-51. The *Cancellation Act* "cancelled" or "retired" not only those emission allowances that were issued by Ontario and held in Ontario CITSS accounts as of July 3, 2018, but also emission allowances that were issued by California and Quebec and held in Ontario CITS accounts. **R-59**, *Cancellation Act*, ss. 1(1)("cap and trade instrument") and 1(2); **R-7**, Regulation 144/16, s. 10.1. The Claimants fail to explain how Ontario could "expropriate" their alleged rights created by California law when California law expressly stated that emission allowances do not constitute property rights. **R-73**, California Code of Regulations, "California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms 17", CCR, §95820(c): "A compliance instrument issued by the Executive Officer does not constitute property or a property right."

[450] **R-6**, *Climate Change Act*, ss. 70(1), (2).

created the emission allowances they purchased contained these explicit limitations.

246. In addition, the Claimants have failed to identify any property rights in Canada in connection with KS&T's alleged "business".[451] As a market participant without compliance obligations, KS&T chose to submit itself to the regulatory regime, established under the *Climate Change Act* and the *Cap and Trade Regulation*, and all of KS&T's activities in Ontario were subject to that regulatory regime. KS&T could have had no expectation, let alone a property right, that its alleged "business model" would ever be viable or that Ontario's system would remain linked with that of California. Ontario cannot expropriate rights that the Claimants never had in the first place.

247. In sum, because KS&T held no property rights capable of being expropriated, no further analysis under NAFTA Article 1110 is required. For the sake of completeness, Canada explains that the claim would fail regardless because it fails to meet the international law requirements for there to have been either a direct or indirect expropriation.

4. The Claimants Have Not Established That Ontario Expropriated Any of Their Alleged Property Rights

a) Ontario's Measures Did Not Interfere with the Claimants' Distinct, Reasonable Investment-Backed Expectations

248. NAFTA tribunals have considered claimants' distinct investment-backed expectations as a relevant factor in determining whether there has been an indirect expropriation.[452] Any such expectations must be considered in light of, *inter alia*, "the regulatory regime in place at the time of investment".[453]

249. Article 1110 does not eliminate the normal commercial risks of a foreign investor, or place on a NAFTA Party the burden of compensating for the failure of a business plan that was not prudent

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[451] *See* Claimants' Memorial, ¶ 402 ("carbon trading business"), Claimants' Memorial, ¶ 418 ("ability to trade more broadly in the carbon market"), Claimants' Memorial, ¶ 409 ("business model").

[452] **CL-18**, *Glamis Gold – Award*, ¶ 356 and FN 704.

[453] **RL-93**, Jack Coe, Jr., and Noah Rubins, "Regulatory Expropriation and the Tecmed Case: Context and Contributions", in Todd Weiler, Ed., "International Investment Law and Arbitration: Leading Cases From The ICSID, NAFTA, Bilateral Treaties And Customary International Law", (2005) p. 624.

in the circumstances.[454] This is particularly true in a situation where KS&T, a sophisticated entity doing business in various jurisdictions around the globe, made a bet on an inherently speculative activity: trading emission allowances in a highly regulated market subject to regulatory change.

250. In *Nelson v. Mexico*, the tribunal concluded that the claimant's enterprise "had, at best, a business opportunity, a bet based on its own interpretations and speculations, that was proven wrong", and the claimant thus could not ask the tribunal to hold the respondent liable for the enterprise "having failed on a bet supported on assumptions and speculations that were proven incorrect."[455] Similarly, the tribunal in *Olguin v. Paraguay* stated that Paraguay's conduct in relation to the operations of a financial institution was "not overly sound" and "careless", and noted "serious shortcomings in the Paraguayan legal system and in the functioning of various State agencies."[456] However, the tribunal concluded that it was "not reasonable" for the claimant to seek compensation for a speculative investment:

> What is evident is that Mr. Olguín, an accomplished businessman, with a track record as an entrepreneur going back many years and experience acquired in the business world in various countries, was not unaware of the situation in Paraguay. He had his reasons (which this Tribunal makes no attempt to judge) for investing in that country, but it is not reasonable for him to seek compensation for the losses he suffered on making a speculative, or at best, a not very prudent, investment.[457]

251. NAFTA Chapter Eleven does not guarantee that the regulatory regime governing an investment will not change. Indeed, as the tribunal in *Feldman v. Mexico* concluded:

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[454] **CL-12**, *Waste Management – Award*, ¶¶ 160: "It is not the function of Article 1110 to compensate for failed business ventures, absent arbitrary intervention by the State amounting to a virtual taking or sterilising of the enterprise", and ¶ 177: "[I]t is not the function of the international law of expropriation as reflected in Article 1110 to eliminate the normal commercial risks of a foreign investor, or to place on Mexico the burden of compensating for the failure of a business plan which was, in the circumstances, founded on too narrow a client base and dependent for its success on unsustainable assumptions about customer uptake and contractual performance."; **CL-88**, *Fireman's Fund – Award*, ¶¶ 184, 218: "The NAFTA, like other free trade agreements and bilateral investment treaties, does not provide insurance against the kinds of risks that FFIC assumed […]"

[455] **CL-69**, *Nelson – Award*, ¶ 281.

[456] **RL-94**, *Eudoro Armando Olguín v. Republic of Paraguay* (ICSID Case No. ARB/98/5) Award, 6 July 2001 ("*Olguin – Award*"), ¶ 65(b).

[457] **RL-94**, *Olguin – Award*, ¶ 65(b).

> [T]he Tribunal is aware that not every business problem experienced by a foreign investor is an indirect or creeping expropriation under Article 1110, or a denial of due process or fair and equitable treatment under Article 1110(1)(c). […] [N]ot all government regulatory activity that makes it difficult or impossible for an investor to carry out a particular business, change in the law or change in the application of existing laws that makes it uneconomical to continue a particular business, is an expropriation under Article 1110. Governments, in their exercise of regulatory power, frequently change their laws and regulations in response to changing economic circumstances or changing political, economic or social considerations. Those changes may well make certain activities less profitable or even uneconomic to continue.[458]

252. The reasonableness of the Claimants' expectations necessarily depends on the regulatory climate existing at the time the alleged property right was acquired in the particular sector in which the investment was allegedly made. The *Methanex* tribunal, which rejected the claimant's expropriation claim in its entirety, emphasized that the claimant voluntary entered a highly regulated market in the absence of any commitment from the host State that the regulatory regime would remain unchanged.[459]

253. KS&T, an entity that did not have compliance obligations in Ontario, voluntarily registered in Ontario's cap and trade program without any commitment from Ontario that the program would last indefinitely, that KS&T's alleged business model would ever be viable, that KS&T would be successful in transferring allowances between its Ontario and California CITSS accounts, or that KS&T would receive any compensation from Ontario in the event the province decided to replace its cap and trade program, which created the emission allowances, with a different regulatory regime.

[458] **RL-90**, *Feldman – Award*, ¶ 112, citing **RL-50**, *Azinian – Award*, ¶ 83. *See also* **RL-27**, McLachlan: Substantive Principles, ¶ 8.128: "Arbitral tribunals have repeatedly emphasised that not every business problem experienced by a foreign investor is an expropriation; it is a fact of commercial life that individuals may be disappointed in their dealings with public authorities".

[459] **CL-89**, *Methanex – Final Award*, Part IV, Chapter D, ¶¶ 9-10: "Methanex entered a political economy in which it was widely known, if not notorious, that governmental environmental and health protection institutions at the federal and state level, operating under the vigilant eyes of the media, interested corporations, nongovernmental organizations and a politically active electorate, continuously monitored the use and impact of chemical compounds and commonly prohibited or restricted the use of some of those compounds for environmental and/or health reasons. Indeed, the very market for MTBE in the United States was the result of precisely this regulatory process. […] Methanex entered the United States market aware of and actively participating in this process. It did not enter the United States market because of special representations made to it."

254. The Claimants allege that KS&T purchased emission allowances at the May 2018 joint auction "based on long-term, reasonably held expectations" that "arose from the structure of Ontario's Cap and Trade Program".[460] That allegation lacks merit. Any "expectations" of the Claimants' must have been informed by the regulatory regime that created Ontario's cap and trade program and the emission allowances. As described above, that regulatory regime was clear: no person was "entitled to be compensated for any loss or damages, including loss of revenues, loss of profit or loss of expected earnings" in respect of any action taken by the Minister or the Director under the *Climate Change Act*, and "[n]othing done or not done in accordance with this Act or the regulations constitutes an expropriation or injurious affection for the purposes of the Expropriations Act or otherwise at law."[461]

255. KS&T also knew that the future of cap and trade programs was inherently uncertain due to political opposition and regulatory challenges. Several WCI partners, after initial interest in cap and trade programs, decided not to proceed.[462] New Jersey decided to withdraw from RGGI, a cap and trade program in which KS&T has a long history of participation.[463] Both RGGI and the EU ETS have had to undertake corrective action in order to address over-allocation of emission allowances in these programs.[464]

256. The Claimants allege that "Ontario's long-held acknowledgement and promotion of the role and importance of market participants" gave rise to reasonable, investment-backed expectation.[465] As noted above, the Claimants exaggerate the importance of market participants; as explained by Mr. Litz, the WCI cap and trade program design contemplated a limited role for market participants.[466]

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[460] Claimants' Memorial, ¶ 410. The Claimants fail to specify what "distinct, reasonable investment-backed expectations" they had and instead merely allege that Ontario's actions "interfered" with such alleged expectations. *See* Claimants' Memorial, ¶¶ 410-411.

[461] **R-6**, *Climate Change Act*, ss. 70(1), (2).

[462] **RER-2**, Litz - Expert Report, ¶ 119.

[463] **RER-2**, Litz - Expert Report, ¶¶ 119, 122, 145-147.

[464] **RER-2**, Litz - Expert Report, ¶¶ 99, 125-127, 142-144, 150.

[465] Claimants' Memorial, ¶ 410.

[466] **RER-2**, Litz - Expert Report, ¶¶ 43, 77-83.

Nor Ontario did "chase" potential market participants[467] or "actively invite[] and encourage[]" market participants to play an "integral role" in its cap and trade program.[468] Ontario published general information and guidance documents on its website[469], and the MECP Help Desk sent correspondence to all cap and trade stakeholders.[470]

257. The Claimants further allege that "Ontario's express written commitments" in the Harmonization Agreement "created reasonable and justifiable expectations" that "Ontario would act in good faith to ensure that any exit from the cap and trade program would be long term and orderly".[471] In fact, the Harmonization Agreement was signed by the representatives of three subnational entities and "expressed the parties' intentions to continue consulting and collaborating on their respective cap-and-trade program."[472] The Harmonization Agreement "did not link the three programs."[473] Each participating jurisdiction – California, Ontario and Québec – independently

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[467] Claimants' Memorial, ¶ 111.

[468] Claimants' Memorial, ¶¶ 92, 105, 117, 216, 370, 392-393.

[469] *See, e.g.,* **C-30**, Ontario Government, "What you need to know about Ontario's carbon market using a cap and trade program, including how it works and who is required to participate", 2 June 2016, updated 8 June 2021: "Even if your company doesn't have emissions to report, you can still participate in the auction as a market participant. Market participants can include individuals, not-for-profit organizations and companies without compliance obligations."; **C-31**, Ontario Government, "Cap and Trade CITSS Registration", 15 July 2016, updated 12 July 2021: "Capped and Market Participants of the Ontario cap and trade program are required to open CITSS."; **C-32**, Ontario Government, "Cap and Trade: Register and Participate in CITSS", 20 July 2016, updated 2019: "Market participants can apply any time for CITSS registration."; **C-35**, Ontario Government, "Cap and Trade: Auction of Allowances", 31 October 2016: "You must be registered and approved in the Compliance Instrument Tracking System Service (CITSS) […] as a mandatory, voluntary or market participant of Ontario's cap and trade program before you can participate in an auction."

[470] *See, e.g.,* **C-34**, Email from MOECC, "Ontario Cap and Trade Registration Deadline", 30 September 2016: "Dear Ontario cap and trade program stakeholder: […]".

[471] Claimants' Memorial, ¶ 410.

[472] **R-76**, *The United States of America v. The State of California*, Declaration of Rajinder Sahota In Support of State Defendants' Opposition to Plaintiff's Summary Judgement Motion and State Defendants' Cross-Motion for Summary Judgement, 2:19-cv-02142-WBS-EFB, 9 March 2020 ("*Declaration of Rajinder Sahota*"), ¶ 65. *See also* ¶ 67: "The intent of the agreement was to endeavor to continue coordinating, in light of the linkage, as each jurisdiction moved forward managing its own program."; **R-6**, *Climate Change Act*, s. 76(1): "The Minister may enter into one or more agreements with representatives of other jurisdictions for the *harmonization and integration* of the cap and trade program under this Act with corresponding programs of those jurisdictions." and 38(1): "If the Minister enters into an agreement with a jurisdiction other than Ontario under section 76, *the regulations may prescribe* instruments created by that jurisdiction as instruments that are recognized for use in Ontario's cap and trade program under this Act…" (*emphasis* added).

[473] **R-76**, *Declaration of Rajinder Sahota*, ¶ 66.

promulgated its own linkage regulations.[474] Furthermore, the provision relating to withdrawal from the Harmonization Agreement "does not, and was not intended to, prevent any party to the agreement from withdrawing unilaterally or without providing 12-months notice."[475]

258. The non-binding Harmonization Agreement did not, and could not, impose any enforceable limitations on Ontario's ability to amend its legislation or replace its cap and trade program with a different regulatory regime.[476] The Harmonization Agreement could not have created any of the Claimants' alleged reasonable, investment-backed expectations.

b) Nothing Ontario Did on June 15, 2018 Substantially Deprived KS&T of the Economic Value of Its Alleged Property Rights

259. For there to be an expropriation, a property right must have been "taken".[477] In other words, there must be a taking of fundamental ownership rights, either directly or indirectly, that causes a "substantial deprivation" of economic value of the investment.[478] The threshold the claimants have

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[474] **R-76**, *Declaration of Rajinder Sahota*, ¶ 66. *See also* **R-6**, *Climate Change Act*, s. 38(1); **R-13**, Regulation 450/17, ss. 4; **RWS-2**, Ramlal – Witness Statement, ¶ 25.

[475] **R-76**, *Declaration of Rajinder Sahota*, ¶ 70. *See also* **RL-95**, Danny Cullenward & David Victor, "Making Climate Policy Work", (Polity Press, 2020), pp. 44-45: "There was no significant impact on the market because all players knew that Ontario could withdraw and, indeed, once the provincial elections took place, would almost certainly withdraw. That the market could anticipate and price these impacts […] tells us is that the market knew Ontario's promise to remain in the WCI program was uenforceable and therefore not credible."

[476] *See also* **RL-95**, Danny Cullenward & David Victor, "Making Climate Policy Work", (Polity Press, 2020), pp. 44: "In 2017 Ontario signed a similar document and joined the WCI as well. By their own terms, however, these documents are not treaties. They do not create any formal, legally binding obligations because subnational governments lack the legal authority to write treaties.", p. 45: "[T]he examples of Ontario and New Jersey […] show how there is no legal recourse for withdrawal from subnational multilateral cap-and-trade programs. Multilateral market links operated by subnational governments have limited credibility because market participants know that if political fortunes change in one jurisdiction, there are few options remaining jurisdictions have to enforce their commitments."

[477] *See, e.g.*, **RL-27**, McLachlan: Substantive Principles, ¶ 8.68: "In fact, the central element is that property must be 'taken' by State authorities or the investor must be deprived of it by State authorities."; **CL-86**, *Pope & Talbot – Interim Award*, ¶ 102: "[T]he test is whether that interference is sufficiently restrictive to support a conclusion that the property has been 'taken' from the owner."; **CL-18**, *Glamis Gold – Award*, ¶ 356: "There is for all expropriations, however, the foundational threshold inquiry of whether the property or property right was in fact taken."; **CL-79**, *ADM – Award*, ¶ 240: "The test on which other Tribunals and doctrine have agreed […] is the "effects test." Judicial practice indicates that the *severity of the economic impact* is the decisive criterion in deciding whether an indirect expropriation or a measure tantamount to expropriation has taken place. An expropriation occurs if *the interference is substantial and deprives* the investor *of all or most of the benefits of the investment*." (*emphasis* added).

[478] **CL-86**, *Pope & Talbot – Interim Award*, ¶ 102; **RL-96**, *Tecnicas Medioambientales Tecmed S.A. v. The United Mexican States* (ICSID Case No. ARB(AF)/00/2) Award, 29 May 2003 ("*Tecmed – Award*"), ¶ 115: "[I]t must be first determined if the Claimant […] was radically deprived of the economical use and enjoyment of its investments, as if the

to meet is high,[479] and mere interference with an investor's use or enjoyment of the benefits associated with property is insufficient to constitute an expropriation at international law.[480] The Claimants agree that "substantial deprivation" is the requisite threshold for the finding of indirect expropriation.[481]

260. The Claimants allege that the June 15, 2018 announcement of Premier-Designate "amounted to a *de facto* taking of the Claimants' property" because "[t]he manner in which Ontario abruptly withdrew from the Cap and Trade Program *de facto* stranded all of the Claimants' Ontario-held carbon allowances immediately".[482] The Claimants also allege that the June 15, 2018 announcement "effectively destroyed KS&T's broader carbon trading business in Ontario."[483] These assertions are incorrect for several reasons.

261. First, as a threshold issue, the June 15, 2018 announcement of the Premier-Designate was not a "measure". All Ontario did on June 15, 2018 was decline to issue notice of participation in a

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rights related thereto […] had ceased to exist."; **CL-18**, *Glamis Gold – Award*, ¶ 357: the tribunal began its analysis "by determining whether the federal and California measures 'substantially impair[ed] the investor's economic rights […] by rendering them useless. Mere restrictions on the property rights do not constitute takings.'"; **CL-19**, *Merrill & Ring – Award*, ¶ 145; **CL-20**, *Grand River – Award*, ¶ 148: "Other NAFTA Tribunals have regularly construed Article 1110 to require a complete or very substantial deprivation of owners' rights in the totality of the investment […]"; **CL-63**, *Windstream Energy LLC v. Canada (UNCITRAL)* Award, 27 September 2016 ("*Windstream – Award*"), ¶ 285. *See also* **RL-86**, Newcombe: Law and Practise of Investment Treaties, p. 341, s. 7.12: "[T]he claimant must establish that the measure in question results in a substantial deprivation." and p. 344, s. 7.16: "The deprivation of property must be severe, fundamental or substantial and not ephemeral."

[479] **CL-12**, *Waste Management – Award*, ¶ 160: "It is not the function of Article 1110 to compensate for failed business ventures, absent arbitrary intervention by the State amounting to *a virtual taking or sterilising of the enterprise*." (emphasis added); **CL-88**, *Fireman's Fund – Award*, ¶ 176(c): "The taking must be a *substantially complete* deprivation of the economic use and enjoyment of the rights to the property, or of identifiable distinct parts thereof (*i.e.*, it *approaches total impairment*)." (emphasis added) and FN 157: "A number of tribunals employ the adjective 'significant,' 'fundamental,' 'radical' or 'serious.'"; **RL-97**, *CMS Gas Transmission Company v. Argentine Republic* (ICSID Case No. ARB/01/8) Award, 12 May 2005, ¶ 262: "The essential question is […] to establish whether the enjoyment of the property has been *effectively neutralized*.".

[480] **CL-18**, *Glamis Gold – Award*, ¶ 357; **RL-98**, OECD, "Indirect Expropriation" and the "Right to Regulate" In International Investment Law, OECD Working Papers on International Investment, No. 2004/4, p. 11.

[481] Claimants' Memorial, ¶ 407: "[A]n indirect expropriation will exist when the *de facto* taking of property has amounted to a substantial deprivation of an investor's investments, as considered on a case-by-case, fact-based inquiry."

[482] Claimants' Memorial, ¶ 408.

[483] Claimants' Memorial, ¶ 409.

subsequent joint auction.[484]

262. Second, neither the emission allowances in KS&T's Ontario CITSS account nor KS&T's alleged "carbon trading business", "business model" and "ability to trade" constitute property rights. Third, even if KS&T held property rights in Ontario capable of being expropriated, Ontario did not "substantially deprive" KS&T of the economic value of its alleged "investments" on June 15, 2018.

263. Third, the Claimants fail to explain how Mr. Ford's statement could have permanently "taken" or "sterilized" KS&T's alleged "investments". The statement did not, and could not, change the law of Ontario, cancel compliance obligations of capped participants, or prohibit participants from transferring emission allowances. The legal framework governing emission allowances remained the same until July 3, 2018, when Regulation 386/18 came into force.[485] Until July 3, 2018, emission allowances retained their essential characteristics of a limited authorization to emit GHG coupled with immunity from penalty.

264. Even assuming that KS&T had property rights in the emission allowances, nothing Ontario did on June 15, 2018 substantially deprived the Claimants of the economic value of the emission allowances.

c) Ontario's Measures Constitute a Valid Exercise of Police Powers Under International Law

265. Many types of government regulation will have effects on an investment, and potentially even significant effects. However, prohibitions against indirect expropriation do not function so as to limit the policy space of governments to such an extent that they are hampered in their ability to regulate

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[484] If Ontario wished to participate in the next joint auction (scheduled for August 14, 2018), it would need to provide notice of the auction 60 days in advance, on June 15, 2018. **R-6**, *Climate Change Act*, s. 74(1); **R-7**, Regulation 144/16, s. 60(1). On that date, and at all times until June 29, 2018, the only people with authority to issue a notice of auction were the incumbent Minister and the Minister's delegate. As explained by Mr. Wood, in keeping with caretaker principles, Ontario did not issue an auction notice because to do so would have frustrated the incoming government's policy intentions. **RWS-1**, Wood – Witness Statement, ¶ 15.

[485] Regulation 386/18 was made under the *Climate Change Act.* It prohibited trading in emission allowances and repealed Regulation 144/16.

in the public interest.[486] Determining whether a measure constitutes an indirect expropriation requires a contextual inquiry that goes beyond purely the effects of a measure.[487] Here, the character of the measures heavily weighs against a finding of indirect expropriation.

266. As explained below, police powers are recognized by customary international law and NAFTA Article 1110, and Ontario's measures satisfy the test for the validity of police powers because they were non-discriminatory, designed and applied to protect legitimate public welfare objectives, and did not constitute one of the rare cases of regulatory measures that are not a valid exercise of police powers.

(i) Police Powers Are Recognized by Customary International Law, as Reflected in NAFTA Article 1110

267. Police powers, which allow States to adopt measures for the protection of the public good, are recognized as part of customary international law and under NAFTA Article 1110. As Professor Lévesque explains, "customary international law recognizes the distinction, present in internal law, between the right of expropriation […] and the police power of the state".[488] Many tribunals have

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[486] **RL-99**, *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc. v. Argentine Republic* (ICSID Case No. ARB/02/1) Decision on Liability, 3 October 2006 ("*LG&E Energy Corp. – Decision on Liability*"), ¶¶ 194-195 citing **RL-96**, *Tecmed – Award*, ¶ 115: "It is important not to confound the State's right to adopt policies with its power to take an expropriatory measure. 'This determination is important because it is one of the main elements to distinguish, from the perspective of an international tribunal between a regulatory measure, which is an ordinary expression of the exercise of the state's police power that entails a decrease in assets or rights, and a de facto expropriation that deprives those assets and rights of any real substance.' With respect to the power of the State to adopt its policies, it can generally be said that the State has the right to adopt measures having a social or general welfare purpose."

[487] **RL-86**, Newcombe: Law and Practise of Investment Treaties, p. 335, ¶ 7.7: "[T]he case-by-case, fact-based inquiry for indirect expropriation focusing on economic impact, legitimate expectations and the character of the government action is generally consistent with customary international law authorities on the scope of expropriation and the developing IIA jurisprudence on the scope of expropriation under IIAs."; **RL-23**, Kinnear: Investment Disputes under NAFTA, pp. 1110-16: "in the context of allegations of regulatory expropriation, […] arguably the economic effects of the measure are irrelevant so long as the measure is a *bona fide*, non-discriminatory regulation enacted for a public purpose in accordance with due process"; and "the context in which the government acted and the purpose of the measure" are "often considered in an indirect expropriation analysis"; p. 1110-17: the fact that indirect expropriation cases "arise in a myriad of different circumstances […] has led many observers to conclude that the best approach is a fact-based, case-by-case assessment which draws on various of the factors discussed above"; **CL-79**, *ADM – Award*, ¶ 250: "Other factors may be taken into account, together with the effects of the government's measure".

[488] **RL-100**, Céline Lévesque, "Distinguishing Expropriation and Regulation under NAFTA Chapter 11: Making Explicit the Link to Property", in Kevin C. Kennedy, ed., "The First Decade of NAFTA: The Future of Free Trade in North America" (Transnational Publishers, 2004), p. 305. *See also* **RL-101**, John Herz, "Expropriation of Foreign Property" (1941) 35:2 Am. J. Int'l. L. 243, pp. 251-252: "The right of the state to interfere with private property in the exercise of its police power has been recognized by general international law as referring to foreign property also: interference with

recognized the existence of these powers.[489]

268. NAFTA Chapter Eleven does not limit the State's police powers.[490] To the contrary, the NAFTA Parties explicitly preserved their flexibility to adopt measures to protect legitimate public welfare objectives.[491] NAFTA tribunals have recognized that the police powers doctrine applies to Chapter Eleven claims. For example, the tribunal in *Feldman v. Mexico* recognized the police powers doctrine in all but name when it stated:

> The Tribunal notes that the ways in which governmental authorities may force a company out of business, or significantly reduce the economic benefits of its

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foreign property in the exercise of police power is not considered expropriation."; **CL-119**, Harvard Draft Convention on the International Responsibility of States for Injuries to Aliens (1961), Art. 10(5); **RL-102**, G.C. Christie, "What Constitutes a Taking of Property under International Law?" (1962) 38 Brit. Y.B. Int'l L. 307 ("Christie: What Constitutes a Taking of Property under International Law"), pp. 331-332, 338; **RL-103**, George H. Aldrich, "What Constitutes a Compensable Taking of Property? The Decisions of the Iran–United States Claims Tribunal", (1994) 88 AM. J. INT'L L. 585, p. 609: "Liability does not arise from actions that are non-discriminatory and are within the commonly accepted taxation and police powers of states. Liability is not affected by the fact that the state has acted for legitimate economic or social reasons and in accordance with its laws." *See also* **RL-104**, Restatement of the Law (Third), Foreign Relations Law of the United States (1987), s. 712, Commentary g: "A state is not responsible for loss of property or for other economic disadvantage resulting from bona fide general taxation, regulation, forfeiture for crime, or other action of the kind that is commonly accepted as within the police powers of states, if it is not discriminatory.", cited in **RL-90**, *Feldman – Award*, ¶¶ 103-105; **RL-17**, *El Paso – Award*, ¶ 238; **CL-18**, *Glamis Gold – Award*, ¶ 354; **RL-89**, *Suez – Decision on Liability*, ¶ 139.

[489] **RL-105**, *Sedco, Inc. v. National Iranian Oil Company and The Islamic Republic of Iran,* Interlocutory Award (Award No. ITL 55-129-3), 17 September 1985, ¶ 90: it is "an accepted principle of international law that a State is not liable for economic injury which is a consequence of a bona fide 'regulation' within the accepted police powers of states."; **RL-106**, *Lauder (U.S.) v. Czech Republic* (UNCITRAL) Final Award, 3 September 2002, ¶ 198: "Parties to the Treaty are not liable for economic injury that is the consequence of bona fide regulation within the accepted police powers of the State"; **RL-33**, *Saluka – Partial Award*, ¶¶ 255: "It is now established in international law that States are not liable to pay compensation to a foreign investor when, in the normal exercise of their regulatory powers, they adopt in a non-discriminatory manner *bona fide* regulations that are aimed at the general welfare." and 262: "[T]he principle that a State does not commit an expropriation and is thus not liable to pay compensation to a dispossessed alien investor when it adopts general regulations that are 'commonly accepted as within the police power of States' forms part of customary international law today."; **RL-43**, *Invesmart – Award*, ¶ 498; **RL-107**, *Joseph Charles Lemire v. Ukraine* (ICSID Case No. ARB/06/18) Decision on Jurisdiction and Liability, 14 January 2010, ¶ 505; **RL-17**, *El Paso – Award*, ¶¶ 239-240; **RL-108**, *Oxus Gold plc v. Republic of Uzbekistan* (UNCITRAL) Final Award, 17 December 2015, ¶¶ 741-743; **RL-19**, *Koch Minerals – Award*, ¶¶ 7.17-7.22.

[490] **RL-23**, Kinnear: Investment Disputes under NAFTA, p. 1110-50: "NAFTA does not expressly address the distinction between regulation and expropriation. As a result, the issue is governed by customary international law, which recognizes that certain measures exist which interfere, perhaps significantly, with property or investment rights and yet cannot be considered expropriation, and hence there is no obligation to compensate for loss attributable to such measures."

[491] The preamble to the NAFTA indicates that the governments of Canada. Mexico and the United States "resolved to", in particular, "PRESERVE their flexibility to safeguard the public welfare". *See also* **CL-2**, *NAFTA*, Art. 1101(4) and 1114.

> business, are many […] At the same time, governments must be free to act in the broader public interest through protection of the environment, new or modified tax regimes, the granting or withdrawal of government subsidies, reductions or increases in tariff levels, imposition of zoning restrictions and the like. Reasonable governmental regulation of this type cannot be achieved if any business that is adversely affected may seek compensation, and it is safe to say that customary international law recognizes this.[492]

269. Similarly, the tribunal in *Glamis Gold v. United States* stated that a State "is not responsible […] 'for loss of property or for other economic disadvantage resulting from bona fide … regulation … if it is not discriminatory."[493]

270. In *Methanex v. United States*, the claimant alleged that "a substantial portion of its investments, including its share of the California and wider U.S. oxygenate markets, was taken by a discriminatory measure and handed to the US domestic ethanol industry."[494] The tribunal, which rejected the claimant's expropriation claim in its entirety,[495] noted that a non-discriminatory regulation for a public purpose "is not deemed expropriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation.[496]

(ii) Ontario Measures Were a Valid Exercise of Police Powers

271. Measures which fall within a State's police powers are not considered expropriatory and do

[492] **RL-90**, *Feldman – Award*, ¶ 103. *See also* **CL-88**, *Fireman's Fund – Award*, ¶176 (j): the tribunal raised the issue of "whether the measure is within the recognized police powers of the host State" as one of the factors that helps the tribunal to "distinguish between a compensable expropriation and a non-compensable regulation by a host State"

[493] **CL-18**, *Glamis Gold – Award*, ¶ 354.

[494] **CL-89**, *Methanex – Final Award*, Part IV, Chapter D, ¶ 2.

[495] **CL-89**, *Methanex – Final Award*, Part IV, Chapter D, ¶ 15: "[T]he Tribunal concludes that the California ban was made for a public purpose, was non-discriminatory and was accomplished with due process. Hence, Methanex's central claim under Article 1110(1) of expropriation under one of the three forms of action in that provision fails. From the standpoint of international law, the California ban was a lawful regulation and not an expropriation."

[496] **CL-89**, *Methanex – Final Award*, Part IV, Chapter D, ¶ 7 (emphasis added). See also **CL-67**, *Chemtura – Award*, ¶ 266: "Irrespective of the existence of a contractual deprivation, the Tribunal considers in any event that the measures challenged by the Claimant constituted a valid exercise of the Respondent's police powers."; **CL-63**, *Windstream – Award*, ¶ 284: "In certain circumstances, the question may also arise as to whether the alleged taking is excused by a justification provided under international law, such as the police powers doctrine."

not give rise to any obligation of compensation.[497] In this case, because Ontario's measures were non-discriminatory and designed and applied to protect legitimate public welfare objectives,[498] there is no obligation to pay compensation to the Claimants.

272. The Claimants concede that the protection of the environment is a legitimate public welfare objective.[499] However, they argue that the challenged Ontario measures were instead "taken for an ulterior motive, to serve the political interests" of the Progressive Conservative Party "by ostensibly minimizing the amount of compensation the government would need to pay as a result of its measures", and that Ontario's cap and trade program "was swiftly replaced by the Federal backstop program"[500] The Claimants' arguments fail to put the Ontario measures into their proper context.

273. Ontario's new government acknowledged that climate change is a real and urgent threat, but considered that carbon pricing was not the preferred policy approach due to its cost for Ontario's households and the economy.[501] This policy decision must be viewed in the context of the conclusion of Ontario's Auditor General in her 2016 report that "the cap-and-trade system will result in only a small portion of the required greenhouse-gas reductions needed to meet Ontario's 2020 target"[502] and "at significant cost to Ontario businesses and households".[503]

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[497] The tribunal in *Saluka* described its own task in this regard as follows: "[I]nternational law has yet to identify in a comprehensive and definitive fashion precisely what regulations are considered 'permissible' and 'commonly accepted' as falling within the police or regulatory power of States and, thus, non-compensable […] It thus inevitably falls to the adjudicator to determine whether particular conduct by a state 'crosses the line' that separates valid regulatory activity from expropriation." **RL-33**, *Saluka – Partial Award*, ¶¶ 263 and 264. *See also* **RL-90**, *Feldman – Award*, ¶ 102: "Ultimately, decisions as to when regulatory action becomes compensable under Article 1110 and similar provisions in other agreements appear to be made based on the facts of specific cases. This Tribunal must necessarily take the same approach."

[498] *See, e.g.,* **RL-74**, CUSMA, Annex 14-B: Expropriation, s. 3; **RL-62**, CPTPP, Annex 9-B: Expropriation, s. 3.

[499] Claimants' Memorial, ¶ 414, 415, 418, 431.

[500] Claimants' Memorial, ¶ 414. *See also* ¶¶ 415, 418, 431.

[501] *See* Sections II.B.1 and II.C.3.d above.

[502] **R-36**, Minister of the Environment and Climate Change, 2016 Annual Report of the Office of the Auditor General of Ontario, Chapter 3 Section 3.02, p. 149. *See also* p. 167: "Under its plans to link its cap-and-trade system with Quebec and California, Ontario is expected to achieve only a relatively small reduction in actual emissions within Ontario from implementation through to 2020."; **R-37**, Office of the Auditor General of Ontario, News Release "Ontario's Cap and Trade Will Not Significantly Lower Emissions Within the Province by 2020: Auditor General".

[503] **R-36**, Minister of the Environment and Climate Change, 2016 Annual Report of the Office of the Auditor General of Ontario, Chapter 3 Section 3.02, pp. 149, 150, and 174-175. Preliminary estimates by the Ministry of Finance estimated

274. In the absence of evidence of illegitimate ulterior motives, the State's intention should not be subject to challenge. With respect to police powers, Professor G.C. Christie wrote that, "[i]f the reasons given are valid and bear some plausible relationship to the action taken, no attempt may be made to search deeper to see whether the state was activated by some illicit motive."[504] Several arbitral tribunals have applied this principle. For instance, the tribunal in *Invesmart v. Czech Republic* stated in the context of an expropriation analysis:

> Numerous tribunals have held that when testing regulatory decisions against international law standards, the regulators' right and duty to regulate must not be subjected to undue second-guessing by international tribunals. Tribunals need not be satisfied that they would have made precisely the same decision as the regulator in order for them to uphold such decisions.[505]

275. The *Cancellation Act* required the Minister to prepare, with the approval of the Lieutenant Governor in Council, a climate change plan and to produce and share with the public regular reports in respect of the plan.[506] As Mr. Alex Wood explains, on November 29, 2018, the Minister released for public consultation the new Made-in-Ontario Environment Plan.[507]

276. The Claimants also allege that Ontario's measures were "manifestly arbitrary" and "discriminatory" because capped participants while market participants (and other categories of

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that the direct costs to the average Ontario household in 2019 would be $210, plus an additional $75 in indirect costs (e.g., goods and services). Furthermore, cap and trade was expected to bring higher electricity prices, which could lead people to switch to cheaper natural gas, a fossil fuel that also produces greenhouse gases. Electricity prices were projected to increase by 14% for businesses and 25% for households.

[504] **RL-102**, Christie: What Constitutes a Taking of Property under International Law, p. 338.

[505] **RL-43**, *Invesmart – Award*, ¶ 501. *See also* **RL-109**, *Rusoro Mining Ltd. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB(AF)/12/5, Award, 22 August 2016, ¶ 385: "States enjoy extensive discretion in establishing their public policy. It is not the role of investment tribunals to second-guess the appropriateness of the political or economic model adopted by the legitimate organs of a sovereign State."

[506] **R-59**, *Cancellation Act, 2018*, ss. 4(1) and 5(1). *See also See* **C-111**, Ontario Government News Release, Ontario Introduces Legislation to End Cap and Trade Carbon Tax Era in Ontario, 25 July 2018: "The proposed legislation will also include measures to help replace the cap-and-trade carbon tax with a better plan for achieving real environmental goals." The plan was released for public consultation on November 29, 2018. *See* **R-62**, 2018 Environment Plan, p. 2; **R-63**, Ontario, News Release, "Ontario Releases Plan to Protect the Environment", 29 November 2018.

[507] **RWS-1**, Wood – Witness Statement, ¶ 34.

participants) were not.[508] As discussed above at Section II.C.3.b, all market participants were ineligible for compensation, not just KS&T. Other types of participants were also excluded, such as fuel distributors, because of their ability to directly pass on to their consumers the cost of compliance.[509] There is also no allegation of nationality-based discrimination.

277. Finally, the Claimants' suggestion that Ontario measures were not "clearly not adopted in good faith"[510] is without merit and must be rejected. In making this allegation, the Claimants rely on the Premier-Designate's announcement on 15 June 2018.[511] The Claimants, however, fail to explain why it was "out of bounds" for a Premier-Designate to announce his government's intention, upon swearing-in, to implement certain environmental policies that had been a central part of his electoral platform. International law does not presume bad faith.[512] The Claimants bear the burden of proving that Ontario's actions constitute one of the rare cases of regulatory measures that are not a valid exercise of police powers, and the Claimants have failed to do so.[513]

278. The role of the Tribunal is not to second-guess the Ontario government's policy decisions on how best to address the challenges posed by climate change.[514] The Tribunal's role in analyzing police powers is limited to distinguishing measures that constitute a valid exercise of police powers

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[508] Claimants' Memorial, ¶¶ 222, 230-231, 243, 249, 258, 281, 287-294, 351-374, 399, 415, 432: "The actions taken by Ontario effectively picked 'winners and losers', and unfairly singled out market participants for non-compensation […]."

[509] **R-59**, *Cancellation Act*, s. 8(5). No compensation was payable to electricity importers, natural gas distributors, operators of equipment related to the transmission, storage or transportation of natural gas, suppliers of petroleum products, operators of equipment for electricity transmission systems, or electricity generators.

[510] Claimants' Memorial, ¶ 414. *See also* ¶¶ 415: "the actions taken by Ontario were not in good faith, but rather were taken for political reasons" and 418: "the measures were not taken in good faith in accordance with due process."

[511] Claimants' Memorial, ¶ 415: "'excessive', because […] the measure was 'so out of bounds as to compel the inference that an expropriation had occurred'" and "[t]he actions of the Premier-elect on 15 June 2018, before even being formally sworn into office, were clearly out of bounds as a matter of law."

[512] **RL-110**, *Case Concerning Certain German Interests in Polish Upper Silesia* (The Merits), 1926 P.C.I.J. (Ser. A) No. 7, 25 May 1925, ¶ 88; **RL-111**, Michel Virally, "Review Essay: Good Faith in Public International Law" (1983) 77:1 Am. J. Int'l L. 130, p. 132.

[513] **RL-61**, *Les Laboratoires Servier, S.A.A., Biofarma, S.A.S., Arts et Techniques du Progres S.A.S. v. Republic of Poland* (UNCITRAL) Final Award, 14 February 2012, ¶¶ 582-584.

[514] **RL-102**, Christie: What Constitutes a Taking of Property under International Law, p. 332: "if the facts are such that the reasons actually given are plausible, search for the unexpressed 'real' reasons is chimeral. No such search is permitted in municipal law, and the extreme deference paid to the honour of States by international tribunals excludes the possibility of supposing that the rule is different in international law"; **RL-43**, *Invesmart – Award*, ¶ 501.

from those that are manifestly incoherent or constitute a disguised form of protectionism. Ontario's measures were non-discriminatory, were designed and applied to protect legitimate public welfare objectives, and constituted a legitimate exercise of police powers.

d) There Was No Compulsory Transfer of Property from the Claimants to the Government of Ontario or an Ontario-Mandated Third Party

279. The Claimants do not even attempt to argue that any of Ontario's measures amounted to a compulsory transfer of property from the Claimants to Ontario or an Ontario-mandated third party. Instead, they put forward an "alternative case" that Ontario committed a direct expropriation by enacting the *Cancellation Act*[515] and that this "cancellation of the Claimants' rights" was for the benefit of the State."[516] The Claimants' arguments are legally and factually flawed.

280. Direct expropriation requires that "the government measures in question result in a state-sanctioned compulsory transfer of property from the foreigner to either the government or a state-mandated third party."[517] Arbitral tribunals have consistently concluded that direct expropriation requires a *compulsory transfer* or *outright physical seizure* of property.[518] In particular, the *National Grid v. Argentina* tribunal was not persuaded that a direct expropriation took place because "[n]o formal right of property has been transferred to the State or to other parties by the State."[519] The *El Paso Energy v. Argentina* tribunal stated that "[i]n direct expropriation, there is a formal transfer of

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[515] Claimants' Memorial, ¶¶ 401, 460.

[516] Claimants' Memorial, ¶¶ 420-421.

[517] **RL-86**, Newcombe: Law and Practise of Investment Treaties", p. 325, s. 7.3. *See also* **RL-84**, UNCTAD, Series on International Investment Agreements II, "Expropriation: A Sequel" (2012), p. 6: "Direct expropriation means a mandatory legal transfer of the title to the property or its outright physical seizure. Normally, the expropriation benefits the State itself or a State-mandated third party."

[518] *See* **RL-75**, *Generation – Award*, 16 September 2003, ¶ 20.21: the impugned measure could not constitute a direct expropriation of the claimant's investment because the State "never purported to transfer Heneratsiya's proprietary rights in its investment to the State or to a third party."; **RL-113**, *Enron Creditors Recovery Corporation v. Argentine Republic* (ICSID Case No. ARB/01/3) Award, 22 May 2007, ¶ 243: the tribunal "d[id] not believe there can be a direct form of expropriation if at least some *essential component of property rights* has not been *transferred to a different beneficiary, in particular the State*." (emphasis added); **CL-114**, *Sempra Energy International v. Argentine Republic* (ICSID Case No. ARB/02/16) Award, 28 September 2007, ¶ 280; **RL-99**, *LG&E Energy Corp. – Decision on Liability*, ¶ 187: the tribunal understood direct expropriation to mean "the *forcible appropriation by the State* of the tangible or intangible property of individuals by means of administrative or legislative action." (emphasis added); **CL-78**, *BG Group Plc. v. Republic of Argentina* (UNCITRAL) Award, 24 December 2007, ¶ 259; **CL-115**, *Crystallex – Award*, ¶ 667.

[519] **CL-37**, *National Grid P.L.C. v. Argentina Republic* (UNCITRAL) Award, 3 November 2008, ¶ 145 (emphasis added).

the title of ownership from the foreign investor to the State engaged in the expropriation or to a national company of that State".[520] In *Teinver v. Argentina*, the tribunal pointed that "a *de facto* taking, without a transfer of title or physical seizure of the investment, is not a direct expropriation."[521]

281. Here, Ontario did nothing which constitutes a direct expropriation. The *Cancellation Act* did not result in a compulsory transfer of any property right from the Claimants to Ontario or an Ontario-mandated third party. Instead, the *Cancellation Act* retired or cancelled all emission allowances held in cap and trade accounts of registered participants as of July 3, 2018.[522] Emission allowances held in CITSS accounts of capped participants were retired in the amount corresponding to the verified GHG emissions of such participants.[523] The *Cancellation Act* cancelled all remaining emission allowances held in cap and trade accounts of registered participants as of July 3, 2018.[524]

282. KS&T was a market participant, not a capped participant. KS&T did not have any GHG emissions to report and did not have any compliance obligations. Under the *Cancellation Act*, none of the emission allowances held by KS&T were retired. Instead, emission allowances were cancelled

[520] **RL-17**, *El Paso – Award*, ¶ 265 (emphasis added).

[521] **RL-114**, *Teinver v. Argentine Republic* (ICSID Case No. ARB/09/01), Award, 21 July 2017, ¶ 964.

[522] *See* **R-59**, *Cancellation Act, 2018*, s. 7: "The following cap and trade instruments are cancelled: 1. All cap and trade instruments held in the cap and trade accounts of participants on July 3, 2018, other than any number of cap and trade instruments in the accounts that are retired under section 6. 2. All cap and trade instruments that were created under the *Climate Change Mitigation and Low-carbon Economy Act, 2016* and were never distributed." The Claimants mistakenly claim that the *Cancellation Act* "specifically provided" that emission allowances held in KS&T's Ontario CITSS account "were deemed by Ontario to have been 'never distributed' in the first place." Claimants' Memorial, ¶ 420. In reality, s. 7(2) of the *Cancellation Act* merely *cancelled* those emission allowances that had been "created", but "never distributed"; therefore, s. 7(2) does not apply to the emission allowances held in KS&T's CITSS account because such allowances indisputably have been "distributed".

[523] **RWS-1**, Wood – Witness Statement, ¶¶ 19-22.

[524] *See* **R-59**, *Cancellation Act, 2018*, s. 7: "The following cap and trade instruments are cancelled: 1. All cap and trade instruments held in the cap and trade accounts of participants on July 3, 2018, other than any number of cap and trade instruments in the accounts that are retired under section 6. 2. All cap and trade instruments that were created under the *Climate Change Mitigation and Low-carbon Economy Act, 2016* and were never distributed." The Claimants mistakenly claim that the *Cancellation Act* "specifically provided" that emission allowances held in KS&T's Ontario CITSS account "were deemed by Ontario to have been 'never distributed' in the first place." Claimants' Memorial, ¶ 420. In reality, s. 7(2) of the *Cancellation Act* merely *cancelled* those emission allowances that had been "created", but "never distributed". Section 7(2) does not apply to the emission allowances held in KS&T's CITSS account because such allowances had been "distributed".

together with the Ontario regulatory framework that created them. The Claimants do not allege that emission allowances in KS&T's CITSS account were transferred to Ontario or to any third party mandated by Ontario (e.g., KS&T's emission allowances were not transferred to another participant in Ontario's cap and trade program).[525] Furthermore, it is undisputable that KS&T did not transfer its alleged "carbon trading business", "business model", or "ability to trade", to Ontario.

283. To constitute direct expropriation, the compulsory transfer or physical seizure must be for the benefit of the host State or a State-mandated third party. The tribunal in *Glamis Gold v. United States*, interpreting NAFTA Article 1110, stated that a "direct expropriation is readily apparent: there is an 'open, deliberate and acknowledged taking of property, such as outright seizure or formal or obligatory transfer of title *in favour of the host State*…'".[526]

284. The cancellation of emission allowances was not, as the Claimants allege, "for the benefit of the State."[527] The Claimants confuse matters by referring to the *total* amount of revenue Ontario raised from *all* participants in *six* auctions that took place in 2017-2018.[528] The Claimants' direct expropriation claim is, however, for the purchase price of the emission allowances acquired by KS&T at the May 15, 2018 joint auction. KS&T deposited the purchase price for these allowances into a Deutsche Bank account on May 25, 2018, and Ontario received only its share of proceeds – USD ██████ – on June 11, 2018.[529] Ontario would have received this amount whether or not Ontario enacted the *Cancellation Act* on October 31, 2018.

285. In the absence of compulsory transfer of the Claimants' property and any benefit to Ontario

[525] The Claimants also do not allege that Ontario physically seized the emission allowances in question.

[526] **CL-18**, *Glamis Gold – Award*, ¶ 355 (emphasis added), citing **CL-16**, *Metalclad Corporation v. The United Mexican States* (ICSID Case No. ARB(AF)/97/1), Award, 30 August 2000, ¶ 103. *See also* **RL-115**, *Caratube International Oil Company LLP and Devincci Salah Hourani v. Republic of Kazakhstan* (ICSID Case No. ARB/13/13) Award, 27 September 2017, ¶ 822: "a direct expropriation involves the transfer of the title to the property or its outright physical seizure, usually to the benefit of the state itself or a state-mandated third party".

[527] Claimants' Memorial, ¶ 421.

[528] Claimants' Memorial, ¶ 421.

[529] **RWS-2**, Ramlal – Witness Statement, ¶¶ 48, 57 and Attachment 1, transfer No. 126873. The exact sum is USD 7,904,568.65.

or a third party, Ontario's actions cannot constitute direct expropriation.

V. THE CLAIMANTS HAVE FAILED TO ESTABLISH THAT THEY ARE ENTITLED TO COMPENSATION

286. The Claimants have pled a defective damages claim. While they ask this Tribunal to award them damages of approximately USD 31 million, this amount does not correspond to their claims for breach of the NAFTA.[530] Rather, the Claimants only attempt to quantify losses related to the purchase price paid by KS&T for emission allowances at the May 2018 joint auction. The Claimants cannot simply assert an entitlement to damages.[531] Even if the Tribunal were to decide that certain acts of Ontario violate NAFTA Chapter Eleven, the Claimants have neglected the indispensable requirement of establishing causation and no damages can be awarded as a result.

287. It is a generally accepted rule of international law that a claimant must prove that the specific breach caused the specific loss that they seek to recover. For the Claimants to be entitled to damages, they must prove (1) that a measure of Canada breached an obligation in Section A of NAFTA Chapter Eleven; (2) that the specific breach was the proximate cause of the Claimants' losses; and (3) that the Claimants' means of quantifying those losses is reasonable, rational and not speculative. Not one of the Claimants' claimed losses is compensable on this standard.

288. With respect to the claim that KS&T's emission allowances were expropriated (**Section A**), the Claimants present an overly simplistic case that fails to prove causation in fact and in law. The crux of the Claimants' complaint stems from the fact that California de-linked its system from Ontario on June 15, 2018, thereby preventing KS&T from transferring emission allowances to California for resale. But this is not a measure of Ontario, and Canada cannot be held liable under NAFTA and at international law for the sovereign act of another State. In addition to not constituting a "measure", the Premier-Designate's announcement that, once in power, his government would implement an "orderly wind-down" of the cap and trade program does not establish legal causation between the

[530] Claimants' Memorial, ¶¶ 21, 450, 490, 510-511, 538(b). The Tribunal lacks personal jurisdiction over Koch Industries because it has failed to meet the "loss or damage" requirement of NAFTA Article 1116(1). *See* III.E., above. However, for convenience, Canada refers to "Claimants' in this section.

[531] The Claimants' suggestion that they "reserve the right" to re-plead their damages case should it be rejected. The Claimants have chosen to present one approach to damages and should not be permitted to re-plead a new case once the fatal weaknesses of its first one have been exposed. *See* Claimants' Memorial, ¶¶ 484, 492

alleged breach (expropriation under Article 1110) and the claimed damage. It was California's de-linking of its system from Ontario's that prevented KS&T from transferring the allowances to California.

289. Nor have the Claimants properly established legal causation between the alleged breaches of NAFTA Article 1105 and their alleged losses (**Section B**). The Claimants simply invite the Tribunal to award the same damages amount as for its expropriation claim. However, refunding the purchase price of the emission allowances is not a correct quantification of what was "lost" as a result of the specific breaches of Article 1105 alleged by the Claimants.[532] For example, if the Tribunal finds that the Crown immunity provision in the *Cancellation Act* violates Article 1105, there is no causal link between that specific breach and the specific loss claimed. Any "damage" caused was, at most, a lost opportunity to challenge the legislation in an Ontario court. The Claimants have not established that this lost opportunity should be quantified as the purchase price paid for the emission allowances. The Claimants also allege other miscellaneous categories of losses[533] but fail to connect any of these to a specific NAFTA breach. As a result, even if the Tribunal were to find a violation of NAFTA Chapter Eleven, the Claimants are not entitled to any damages.

290. Finally, any compensation awarded by the Tribunal must account for the Claimants' failure to take steps that would have prevented it from suffering any harm (**Section C**). KS&T was, by its own description, an experienced and sophisticated trader.[534] It had several options at its disposal that could have insulated it from incurring any loss whatsoever, including transferring the emission allowances to California at any time between June 11 (the day the allowances were deposited into its

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[532] The Claimants' allege that Ontario's "abrupt" cancellation of the cap and trade system, the decision not to compensate market participants, and the Crown immunity clause of the *Cancellation Act* violate Article 1105. If the Tribunal finds that one or more of these measures are a breach of Article 1105, each has a different valuation date and a different quantification of compensable loss.

[533] Claimants' Memorial, ¶ 490: "The Claimants' losses arising from Canada's breaches of the NAFTA can be categorised as follows: (i) the loss of KS&T's Ontario emissions trading business, including its future profits arising therefrom; (ii) the loss of the carbon allowances held in KS&T's Ontario CITSS account as at the date of expropriation; (iii) the cost of obtaining additional carbon allowances from alternative sources in order to meet KS&T's existing contractual obligations; (iv) the costs associated with taking remedial action. Each will be addressed in turn. In summary, the Claimants value their losses at USD 31,322,474.62 in damages, plus interest and costs."

[534] Claimants' Memorial, ¶ 141, "As explained by Mr. Martin, KS&T was marketing the company – both internally and externally – as leaders in the field"; **R-22**, KS&T Energy Derivatives Brochure, "The Global Source for Commodities".

Ontario account) and June 15 (the day California delinked its CITSS accounts from Ontario). If the Tribunal were to find that KS&T or the Claimants are entitled to compensation, it must accordingly reduce the amount of damages to take account of KS&T`s contribution to its own loss.

A. The Claimants Have Failed to Prove that Ontario Caused the Loss They Claim in Relation to the Emission Allowances

291. The Claimants allege that the emission allowances purchased at the May 2018 joint auction were expropriated on June 15, 2018 when the Premier-Designate announced that, once his government assumed power, Ontario would proceed to an orderly wind down of the cap and trade program and/or on July 3, 2018, when Regulation 386/18 came into force.[535] They claim that the June 15 announcement prevented KS&T from using the emission allowances in the United States, resulting in loss, which they equate with the purchase price paid for those emission allowances.[536] Alternatively, the Claimants argue that the allowances were expropriated on October 31, 2018 when the *Cancellation Act* came into force.[537] In either case, the Claimants argue, the expropriation became "known" on June 15, 2018 and so the relevant date for valuation purposes is June 14, 2018.[538] The Claimants' damages case suffers from a fundamental deficiency: Ontario did not take any action on June 15, 2018 that caused the Claimants loss.

292. Causation is a necessary component of a claimant's damages case. In order to be entitled to damages, a claimant must prove, to the satisfaction of the tribunal, that specific actions of the State caused them actual and quantifiable loss. This is consistent with principles of customary international law on State responsibility. A claimant must prove that the specific breach caused the specific loss that it seeks to recover.[539]

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[535] Claimants' Memorial, ¶ 401. *See also* Claimants' Memorial, ¶¶ 459, 493.

[536] Claimants' Memorial, ¶¶ 128, 163, 208, 230, 496-501.

[537] Claimants' Memorial, ¶¶ 20, 401, 420, 459, 460, 493.

[538] Claimants' Memorial, ¶¶ 448, 453, 459-460, 472, 483, 493.

[539] *See* **RL-116**, M. Kazazi, "Burden of Proof and Related Issues: A Study on Evidence Before International Tribunals" (Kluwer Law International, 1996), p. 222: "As a general principle, however, it is necessary for the party who alleges a fact to prove the truth of its claim, if not accepted by the other party, before the authority which is charged with the duty to adjudicate the dispute. This rule is so well-founded in municipal law that it could easily be concluded to be a generally accepted principle of municipal law which, in accordance with Article 38 of the Statute of the International Court of

293. This customary rule is reflected and explained in Article 31 of the *Draft Articles on the Responsibility of States for Internationally Wrongful Acts* (**ILC Articles**): a State that has committed a wrongful act must make "full reparation," but only for "any damage […] *caused by* the internationally wrongful act."[540] In other words, "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."[541] As the tribunal in *Pey Casado* explained, the operation of the rule "depends on injury, and that injury in turn depends on causation"[542] and "the injury in question must be caused by that specific breach."[543]

294. The Commentary to Article 31 of the ILC Articles similarly explains that "causality in fact is a necessary but not a sufficient condition of reparation. […] 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, but without the addition of any particular qualifying phrase."[544] Even where a claimant establishes that an identified breach was a "but for" cause in the chain of causation, recovery of damages is not permitted unless the claimant can prove that "the wrongful conduct was a *sufficient*, *proximate*, *adequate*, *foreseeable* or *direct* cause of the injury."[545]

Justice, is a source of international law."; **RL-117**, M. Kantor, "Valuation for Arbitration: Compensation Standards, Valuation Methods and Expert Evidence" (Kluwer Law International, 2008), pp. 105-106: "The injured claimant, therefore, has the burden of demonstrating that the claimed quantum flowed from that conduct. Shelves of books and papers contain discussions of the fundamental role the principle of 'causation' plays in determining both liability and compensation. While this volume is not the place to repeat those detailed analyses, we cannot overemphasize the crucial role causation performs in valuation issues. The claimant must satisfy the tribunal that the causal relationship is sufficiently close (i.e., not 'too remote') to satisfy the applicable standard of causation."

[540] **CL-51**, International Law Commission, "Draft Articles on the Responsibility of States for Internationally Wrongful Acts, with Commentaries", (New York: UN, 2001) ("ILC Draft Articles on State Responsibility with Commentary"), Art. 31 (emphasis added). *See* **RL-118**, T.W. Walde & B. Sabahi, "Compensation, Damages, and Valuation in The Oxford Handbook of International Investment Law", (OUP 2008), p. 1057: The commission of an internationally wrongful act entails the obligation to put the victim back into the position it would "have – in theory – [been in] had the unlawful act not occurred."

[541] **CL-51**, ILC Draft Articles on State Responsibility with Commentary, Art. 31, Commentary (9).

[542] **RL-119**, *Victor Pey Casado and President Allende Foundation v. Republic of Chile* (ICSID Case No ARB/98/2), Award, 13 September 2016 ("*Pey Casado – Award*"), ¶ 204.

[543] **RL-119**, *Pey Casado – Award*, ¶ 218.

[544] **CL-51**, ILC Draft Articles on State Responsibility with Commentary, Art. 31, Commentary (10) (citations omitted).

[545] **RL-120**, S. Ripinsky, "Damages in International Investment Law", (London, British Institute of International and Comparative Law: 2008), p. 135 (emphasis in original).

In other words, causation in international law "comprises a number of different elements, including (*inter alia*) (a) a sufficient link between the wrongful act and the damage in question, and (b) a threshold beyond which damage, albeit linked to the wrongful act, is considered too indirect or remote."[546]

295. The requirement to establish causation is reflected in the text of the NAFTA itself. Article 1116(1) accords standing only to a claimant alleging that it "has incurred loss or damage, *by reason of, or arising out of*" an alleged breach of the NAFTA.[547] This language requires a sufficient causal link or an "adequate[] connect[ion]"[548] between the alleged breach of NAFTA and the loss sustained by the investor.[549]

296. Tribunals have been unwilling to allow damages with respect to claims that are highly conjectural or "too remote or speculative,"[550] or to "provide compensation for claims with inherently speculative elements."[551] Tribunals have also refused to award damages when the claimant has failed to properly establish legal causation with the specific loss claimed, even if a discrete treaty breach has been found.[552]

297. The Claimants' case fails on both legal and factual causation. Any measure of Ontario that

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[546] **RL-121**, *Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania* (ICSID Case No. ARB/05/22) Award, 24 July 2008 ("*Biwater – Award*"), ¶ 785; **RL-122**, *Duke Energy Electroquil Partners & Electroquil S.A. v Republic of Ecuador* (ICSID Case No. ARB/04/19) Award, 18 August 2008, ¶ 468.

[547] **CL-2**, *NAFTA*, Art. 1116(1) (emphasis added).

[548] **RL-90**, *Feldman – Award*, ¶ 194. *See also* **RL-121**, *Biwater – Award*, ¶ 779: "Compensation for any violation of the BIT, whether in the context of unlawful expropriation or the breach of any other treaty standard, will only be due if there is a sufficient causal link between the actual breach of the BIT and the loss sustained by [the Enterprise]."

[549] The *Biwater* tribunal similarly explained that "'causing injury' must mean more than simply the wrongful act itself (e.g., an expropriation, or unfair or inequitable treatment), otherwise the element of causation would have to be taken as present in every case, rather than being a separate enquiry." **RL-121**, *Biwater – Award*, ¶ 803-804. *See also* **RL-123**, *Nordzucker AG v. The Republic of Poland* (UNCITRAL) Third Partial and Final Award, 23 November 2009 ("*Nordzucker – Final Award*"), ¶ 64.

[550] **RL-124**, *LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. Argentine Republic* (ICSID Case No. ARB/02/1) Award, 25 July 2007, ¶ 89.

[551] **CL-51**, ILC Draft Articles on State Responsibility with Commentary, Art. 36(27), pp. 259-260.

[552] *See, for example* **RL-123**, *Nordzucker – Final Award*, ¶ 64. **RL-125**, *Pawlowski AG and Projekt Sever S.R.O. v. Czech Republic* (ICSID Case No. ARB/17/11) Award, 1 November 2021, ¶ 737; **RL-121**, *Biwater – Award*, ¶ 798.

could constitute a breach of Article 1105 or 1110 took place *after* California de-linked its system from Ontario. The Claimants would be in the same situation with or without a NAFTA breach by Canada: prohibited by California from transferring their emission allowances into that jurisdiction. It was California's act of de-linking that caused the Claimants loss.

298. ████████ [553] The Claimants confirmed that this was KS&T's practice in their public comment to Bill 4.[554] KS&T could have transferred the emission allowances it acquired in the May 2018 auction to California at any time between June 11 and 15.[555] While this is a factor for the Tribunal to take into account if it decides any compensation is owed (see **Section C** below), the principal issue is whether the June 15 press release was the *direct legal cause* of the Claimants' inability to transfer their emission allowances to California. It was not.

299. On June 15, 2018, the Office of the Premier-Designate issued a press release stating that "following the swearing-in of" the new government on 29 June 2018, "Ontario would be serving notice of its withdrawal" from the Harmonization Agreement and from future auctions.[556] The press release added that, "[t]he government will provide clear rules for the orderly wind down of the cap-and-trade program."[557] None of these statements could have directly or indirectly expropriated the

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[553] On ████ California, Ontario and Quebec deposited the emission allowances from the February 2018 joint auction into KS&T's Ontario CITSS account. In ████ KS&T Ontario transferred the ████ of its Ontario CITSS account to its California CITSS account. Between ████ the balance of KS&T's Ontario CITSS account was ████ **RWS-2**, Ramlal – Witness Statement, ¶¶ 53-55 and Attachment 1, ████.

[554] This explains why, in this arbitration, the Claimants are only claiming damages related to the purchase of emission allowances at the May 2018 auction: KS&T repeatedly ████ its Ontario CITSS account by transferring emission allowances to its California CITSS account. **RS-86**, Koch Comment on Bill 4, Cap and Trade Cancellation Act, p. 1. Between ████ as well as between ████ the ████ of KS&T's Ontario CITSS account ████ **RWS-2**, Ramlal – Witness Statement, ¶¶ 53, 55.

[555] **RWS-2**, Ramlal – Witness Statement, ¶¶ 58.

[556] **C-7**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Announces an End to Ontario's Cap-and-Trade Carbon Tax," 15 June 2018; *See also*, **R-49**, "Doug Ford to Become Ontario's 26th Premier", 8 June 2018; **R-51**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Commits to Protecting Jobs at Pickering Nuclear Generating Station", 21 June 2018; **R-52**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford will build Memorial to Honour Canadian Heroes of the War in Afghanistan", 27 June 2018.

[557] **C-7**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Announces an End to Ontario's Cap-and-Trade Carbon Tax," 15 June 2018.

emission allowances in KS&T's Ontario CITSS account, nor did these statements prevent KS&T from transferring the allowances to California.

300. Ontario took no action to prohibit purchase, sale or trading of emission allowances in Ontario until July 3, 2018, when Regulation 386/18 came into force. Indeed, the Claimants themselves have stated (contrary to what they now argue in this arbitration[558]) that "[w]hen Ontario froze all registry accounts *on July 3, 2018* these allowances effectively became stranded."[559]

301. Rather, it was the decision of the California Air Resources Board on June 15 to de-link the California system from Ontario that prevented the Claimants from transferring the emission allowances to California.[560] That prohibition of transfers by California, which was fully within California's sovereign right,[561] caused the specific loss claimed by the Claimants, not any action of Ontario.

B. The Claimants Fail to Prove Legal Causation for Each of their Claims

302. Aside from their primary argument with respect to the loss of the ability to use emission allowances in the United States, the Claimants claim several other categories of losses.[562] All of these claims fail – for lack of sufficient evidence, or failure to connect the loss to an alleged NAFTA breach, or both.

1. The Claimants Have Failed to Establish Actual and Specific Loss Pursuant to the Alleged Breaches of the Minimum Standard of Treatment

303. The Claimants' damages claim for alleged breach of the minimum standard of treatment is

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[558] Claimants' Memorial, ¶¶ 11, 408.

[559] **RS-86**, Koch Comment on Bill 4, Cap and Trade Cancellation Act, p. 2 (emphasis added).

[560] **C-104**, California Air Resources Board, "Market Notice: New Functionality in CITSS", 15 June 2018. *See also* **C-105**, ICE Futures U.S., "Notice: California Carbon Allowances Futures Contracts – Changes to Deliverable Allowances in the Compliance Instrument Tracking System Service", 18 June 2018; **C-103**, CA CITSS Help Desk, "Market Notice – New Functionality in CITSS", 15 June 2018.

[561] **R-25**, Harmonization Agreement, Preamble: "[Whereas], the Parties further recognize that the present Agreement does not, will not and cannot be interpreted to restrict, limit or otherwise prevail over relevant national obligations of each Party, if applicable, and each Party's sovereign right and authority to adopt, maintain, modify, repeal or revoke any of their respective program regulations or enabling legislation [...]".

[562] Claimants' Memorial, ¶ 490.

perfunctory, simply stating "the standard [for damages] entails an assessment by reference to the investments' fair market value, *i.e.* the same test that which [*sic*] applies to the expropriation claim."[563] This argument does not correspond to the case pled by the Claimants.

304. The Claimants allege that several alleged measures of Ontario constitute a breach of Article 1105: the "abrupt" cancellation of the cap and trade system; the decision not to compensate market participants; and the Crown immunity provision of the *Cancellation Act*.[564] For the purposes of quantifying damages, if the Tribunal were to find that any of these measures constitute a breach, a different analysis would apply.

305. As Canada explained above, under customary international law "a State that has committed a wrongful act must make "full reparation," but only for "any damage […] *caused by* the internationally wrongful act." If the wrongful act is the decision to "abruptly" cancel the cap and trade system, the burden is on the Claimants to establish the but-for world where Ontario withdrew on a different timeline. The Claimants' have made no attempt to establish a damages case whereby Ontario withdrew from the system in a manner that was not "abrupt".[565] If the wrongful act is the decision to deny compensation to market participants, the burden is on the Claimants to establish the measure of compensation that would otherwise have been paid to a market participant. The Claimants have not even attempted to establish that such compensation would have been the same as that paid to eligible participants. If the Tribunal were to find that the Crown immunity provision of the *Cancellation Act* amount to a breach of NAFTA Chapter Eleven, the burden would be on the Claimants to establish the value of what was "lost", which is the opportunity to have their case heard by an Ontario court, not a refund of the purchase price of the emission allowances.

306. As a result, even if the Tribunal finds a breach of Article 1105, the Claimants are not entitled to any damages.

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[563] Claimants' Memorial, ¶ 449.

[564] Claimants' Memorial, s. IV. B 1-2.

[565] Claimants' Memorial, ¶ 351. The Claimants do not allege that Ontario withdrawing from cap and trade in and of itself is a violation of NAFTA Article 1105 but rather focus on the alleged "abruptness" of the process.

2. The Claimants Have Failed to Establish Actual and Specific Loss of their "Emissions Trading Business in Ontario"

307. The Claimants allege that KS&T's "emissions trading business in Ontario" was "destroy[ed]" and request "damages corresponding to the fair market value of that lost business."[566] Their claim does not specify whether this loss was a result of the alleged breach of Article 1110 or 1105.

308. The Claimants have not provided any evidence of a KS&T "emissions trading business in Ontario" apart from business development efforts by U.S. employees of KS&T and by non-KS&T employees.[567] As discussed in Section III.D.1 and III.D.2 above, this is not an "investment" within the meaning of NAFTA Article 1139(a) or (h).[568]

309. Regardless, the Claimants do not provide the particulars of loss that this "emissions trading business in Ontario" suffered. This allegation is particularly dubious when considered in light of the Claimants' statements that KS&T had promised its Ontario emission allowances to its related entity Flint Hills Resources in California.[569] The Claimants have not explained how the same allowances can simultaneously be promised to its related entity to satisfy compliance obligations, as well as forming the basis of an "emissions trading business" in Ontario.

310. The Claimants state that this approach is "inherently conservative in nature" and that they "reserve the right to amend their claim so as to include a claim for KS&T's lost business" in a future pleading.[570] The Claimants' approach is not "inherently conservative"; it is incomplete. The Claimants had an opportunity to explain how KS&T's alleged "emissions trading business" suffered any loss as a result of a NAFTA breach, but failed to do so. As a result, their claim must be rejected.

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[566] Claimants' Memorial, ¶ 491.

[567] **R-50**, KS&T Participant Registration Form, [redacted] s. 2.0.

[568] **CL-2**, *NAFTA*, Art. 1139(a)(h).

[569] Claimants' Memorial, ¶¶ 165, 178, 205, 496. *See also* CWS-4, Witness Statement of Frank King, 6 October 2021, ¶¶ 24-25.

[570] Claimants' Memorial, ¶ 492.

3. The Claimants Have Failed to Establish Actual and Specific Loss with Respect to KS&T's Related Party Contracts

311. The Claimants assert that KS&T was required to expend [redacted] to purchase allowances from a third party in order to meet its delivery obligations under a contract with [redacted][571]

312. The evidence that the Claimants provide in respect of this claim is scant. They provide two spreadsheets that were seemingly generated for the purposes of creating an exhibit in this arbitration. The Claimants do not cite the underlying contract as an exhibit in support of this argument, or explain its provisions, or provide context into how and when the price was agreed.[572] The Claimants have again failed to establish factual and legal causation with respect to this claimed loss and their claim must be rejected.

4. The Claimants Have Failed to Establish that They Are Entitled to Lobbying Costs

313. The Claimants assert that they are entitled to the "management, administrative, overhead and legal costs" associated with the "remedial steps" they took to lobby the Ontario government when it announced its policy intent.[573] Lobbying costs do not fall within the full reparation standard. In addition, the Claimants have failed to identify the relevant persons, entities, and activities for which they now claim reimbursement from Canada.[574]

314. As discussed above, a State liable for a breach of international law must make "full reparation" for the injury caused. However, there must be a "sufficiently clear direct link" between

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[571] Claimants' Memorial, ¶ 498.

[572] The Claimants provided **C-144**, Extract from ICE's ICEXL Excel Addin, and **C-146**, FHR Trades Extract as support for this argument. However, the relevant contract appears to be exhibit **C-73**, [redacted] That document anticipates a situation where "Buyer nominates a Monthly Quantity, but Seller is unable to Deliver Contract Credits to Buyer to fulfill such Monthly Quantity due to a change in Applicable Law that terminates or suspends indefinitely the Program", but the Claimants fail to explain whether and how they acted in accordance with these contractual terms.

[573] Claimants' Memorial, ¶ 505, the Claimants seek [redacted] for their "external lobbying consultant"; [redacted] for its "external Canadian legal counsel costs", and [redacted] for its "initial NAFTA counsel legal costs", for a total of [redacted]

[574] Canada notes that the full extent of the Claimants' lobbying is not known, as they have failed to identify the relevant persons and entities involved.

the wrongful act and the alleged injury. As with the other claims, the Claimants fail to posit the "but-for" scenario. It is not reasonable to assume that the but-for scenario is one in which the Ontario government did not exercise its sovereign right to change its policy direction and cancel the cap and trade program. Nor is it reasonable to assume that the but-for scenario is one in which the Claimants obtain compensation from a process that expressly excluded them from participating in the first place.

315. The Claimants have again failed to prove their case, and cannot be compensated for attempting to use their influence and their resources to lobby the Ontario government to rewrite the rules in their favour.

C. Any Damages Awarded Must Be Diminished or Disallowed As a Result of the Claimants' Role in their Loss

316. If the Tribunal disagrees with Canada's position and finds that the Claimants are entitled to reparation even in the absence of a direct link to a specific NAFTA breach, any damages awarded must be reduced in order to account for the Claimants' role in their loss occurring prior to July 3, 2018.[575] If a claimant commits a fault that contributes to the prejudice it suffered, either by carelessness, negligence or wilful conduct, the tribunal has discretion to determine that the claimant should bear some responsibility and accordingly diminish or disallow any damages claim.[576]

317. Article 39 of the ILC Articles addresses a situation in which a claimant has contributed to its own injury:

> In the determination of reparation, *account shall be taken* of the contribution to the injury by wilful or negligent action or omission of the injured State or any person or entity in relation to whom reparation is sought.[577]

318. Commentary to Article 39 clarifies that "[t]he phrase 'account shall be taken' indicates that the article deals with factors that are capable of affecting the form or reducing the amount of

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[575] As Canada explained in Section IV.B.4(b), Canada submits that if the Tribunal finds that there is an expropriation, the relevant date is 3 July 2018.

[576] **RL-126**, *Yukos Universal Limited (Isle of Man) v. The Russian Federation* (UNCITRAL) Final Award, 18 July 2014 ("*Yukos – Award*"), ¶ 1633; *See also* **CL-51**, ILC Draft Articles on State Responsibility with Commentary, Art. 39.

[577] **CL-51**, ILC Draft Articles on State Responsibility with Commentary, Art. 39 (emphasis added).

reparation in an appropriate case."[578] Further, "Article 39 allows to be taken into account only those actions or omissions which can be considered as wilful or negligent, i.e. which manifest a lack of due care on the part of the victim of the breach for his or her own property or rights."[579] The purpose of Article 39 is to ensure fairness as between the State and the victim of the breach, ensuring that "full reparation is due for the injury – but nothing more – arising in consequence of the internationally wrongful act."[580]

319. Tribunals have a wide margin of discretion to proportionately reduce any award of damages.[581] The tribunals in *Occidental v. Ecuador* and *Yukos v. Russia* stated that to make a finding of contributory fault, the trier of fact must ascertain whether there was a causal link between the negligent act of the claimant and the respondent State's unlawful act and resulting damages. However, not just any contribution to the injury would suffice: "the contribution must be material and significant."[582] Ultimately, both of these tribunals found that the claimant had contributed to its claimed losses and reduced the damages award by 25%.[583]

320. If this Tribunal decides that the Claimants have established their claim with reasonable certainty and awards damages as a result, any damages awarded must be reduced to take into account the role that the Claimants had in their own loss. The Tribunal should examine how the Claimants chose to structure their business, including its inaction in the days leading up to the alleged breach.[584]

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[578] **CL-51**, ILC Draft Articles on State Responsibility with Commentary, Art. 39, commentary (5), p. 110.

[579] **CL-51**, ILC Draft Articles on State Responsibility with Commentary, Art. 39, commentary (5), p. 110.

[580] **CL-51**, ILC Draft Articles on State Responsibility with Commentary, Art. 39, commentary (2), p. 110.

[581] **RL-127**, *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador* (ICSID Case No. ARB/06/11) Award, 5 October 2012 ("*Occidental – Award*"), ¶ 670.

[582] **RL-127**, *Occidental – Award*, ¶ 670; *See also* **RL-126**, *Yukos – Award*, ¶ 1600.

[583] Similarly, in *MTD v. Chile* the claimant incurred loss due to a series of business decisions that increased its risks in the relevant transactions, and the Tribunal reduced its damages award by 50%. **RL-128**, *MTD Equity Sdn. Bhd. And MTD Chile S.A. v. Republic of Chile* (ICSID Case No. ARB/01/7) Award, 25 May 2004, ¶¶ 242-243. The annulment committee reviewing this award affirmed the principle that damages should be reduced to reflect the claimant's contribution to loss and declined to annul this portion of the award. **RL-129**, *MTD Equity Sdn. Bhd. And MTD Chile S.A. v. Republic of Chile* (ICSID Case No. ARB/01/7) Decision on Annulment, 21 March 2007, ¶¶ 93-101.

[584] As Canada explained in Section IV.B.4(b) above, if the Tribunal finds that Ontario committed an expropriation the relevant date is July 3, 2018. However, in the event that the Tribunal agrees with the Claimants' date of expropriation of June 15, the Claimants' contributory fault is relevant to any assessment of damages. Further, the Claimants have provided no details for the alleged breaches of Article 1105.

321. Any award of damages to the Claimants must be reduced to take into account the fact that KS&T could have avoided incurring any loss if it had acted prudently in the weeks leading up to and following the May 2018 joint auction.

322. **KS&T could have bid in the May 2018 auction from its California accounts**: The May 2018 joint auction was held on May 15, 2018. By that time, the Ontario election was underway and the Progressive Conservative Party, which was widely forecasted to win the election set for June 7, had promised to withdraw Ontario from the WCI program. KS&T was a particularly savvy operator, and had registered as a market participant in both California and Ontario. Given the uncertainty of a provincial election during this intervening period, it would have been prudent for KS&T to bid as a California-registered market participant, using its California CITSS account, rather than as an Ontario-registered market participant, using its Ontario CITSS account. This would have ensured that the allowances would have been deposited in that account and could have been used in California.

323. **KS&T could have transferred the allowances to its California CITSS account**: As noted above, KS&T was registered as a market participant in both the California and the Ontario cap and trade programs, and thus had CITSS accounts in both jurisdictions. The allowances from the May 2018 auction were deposited in KS&T's Ontario CITSS accounts as scheduled on June 11, 2018. Four days earlier, on June 7, 2018, the anti-cap and trade Progressive Conservative Party had won a majority in the Ontario election. KS&T, however, chose to keep the emission allowances in its Ontario CITSS account. At any point between June 11 and 15, KS&T could have transferred the balance of its Ontario CITSS holdings to its California account, as it had done after previous auctions. Further, if market participants like KS&T are "active participants, monitoring and trading every day, with specialized expertise and knowledge" as the Claimants suggest, KS&T would have been well positioned to take swift action.[585] KS&T could simply have transferred between its CITSS accounts, preventing the alleged losses that the Claimants now seek to recoup in this arbitration.

324. **KS&T could have transferred to the allowances to related entities**: As discussed above, KS&T alleges that it was procuring allowances partly to comply with the compliance obligations of

[585] Claimants' Memorial, ¶ 72.

Koch entities. KS&T could have transferred the emission allowances from its Ontario CITSS account to the CITSS account of one of the members of the corporate association group. Such transfers could be completed on the same day they were initiated.[586]

D. The Claimants' Request for Interest Must Be Rejected

325. Under NAFTA Article 1135(1), a tribunal has discretion to award "any applicable interest." However, with the exception of Article 1110 claims, both NAFTA and the ICSID Rules are silent on the terms of such interest. The guiding principle under international law is that interest is only necessary to ensure full reparation; there is no automatic right to interest.[587] As a result, the Claimants bear the burden of proving that the circumstances of this case justify an award of interest to ensure full reparation.

326. The Claimants have failed to meet the burden of establishing why, in this case, full reparation requires an award of interest – much less compound interest at a rate of 5% annually. If the Tribunal were to award damages for a breach of the expropriation obligation, simple interest is sufficient to meet the full reparation standard. If the Tribunal were to find a breach of the Minimum Standard of Treatment, the Claimants should not be entitled to any interest, as they have failed to plead their damages case at all.

VI. REQUEST FOR RELIEF

327. For the foregoing reasons, Canada respectfully requests that this Tribunal:

(a) dismiss the Claimants' claims in their entirety;

(b) require the Claimants to bear all costs of the arbitration, including Canada's costs of legal assistance and representation; and

(c) grant any other relief that it deems appropriate.

[586] **RWS-2**, Ramlal – Witness Statement, ¶ 37.

[587] **CL-51**, ILC Draft Articles on State Responsibility with Commentary, p. 107.

February 17, 2022

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