IN THE MATTER OF AN ARBITRATION UNDER CHAPTER ELEVEN OF THE NORTH AMERICAN FREE TRADE AGREEMENT AND THE ICSID ADDITIONAL FACILITY RULES

BETWEEN:

KOCH INDUSTRIES, INC., AND KOCH SUPPLY & TRADING LP,

Claimants

AND

GOVERNMENT OF CANADA,

Respondent

ICSID CASE NO. ARB/20/52

GOVERNMENT OF CANADA RESPONSE TO THE SUBMISSION OF THE UNITED STATES OF AMERICA PURSUANT TO NAFTA ARTICLE 1128

November 11, 2022

Trade Law Bureau
Government of Canada
Lester B. Pearson Building
125 Sussex Drive
Ottawa, Ontario
K1A 0G2
Canada

I. INTRODUCTION

1. The NAFTA Article 1128 submission filed by the United States in this arbitration confirms Canada's interpretation of Articles 1139, 1116, 1105, and 1110 in the context of this arbitration.[1] Previous NAFTA Chapter Eleven tribunals have accorded the views of the non-disputing NAFTA Parties considerable weight in the interpretation of the treaty obligations.[2] This Tribunal should do the same.

2. The concordant views of the NAFTA Parties must be considered by this Tribunal in accordance with Article 31(3) of the *Vienna Convention on the Law of Treaties* ("VCLT"),[3] and should be given considerable weight. The Tribunal should consider any previous statements by the NAFTA Parties on the interpretation of the relevant provisions, not only the Article 1128 submission in this arbitration,[4] and no inferences should be drawn with respect to any NAFTA Party' position on a particular issue based on the absence of a NAFTA Article 1128 submission.[5]

[1] *Koch Industries, Inc. and Koch Supply and Trading, LP v. Government of Canada*, Submission of the United States of America, 28 October 2022 ("U.S. Article 1128 Submission").

[2] *See e.g.*, **RL-131**, *Westmoreland Mining Holdings LLC v. Government of Canada* (ICSID Case No. UNCT/20/3) Final Award, 31 January 2022 ("*Westmoreland – Final Award*"), ¶ 214 (accepting that "significant weight" should be placed on the submissions of non-disputing NAFTA Parties, and acknowledging that the NAFTA States "have a unique perspective on how the NAFTA should be interpreted and also in recognition of the systemic interest of States in ensuring consistency of interpretation.").

[3] **RL-029**, Vienna Convention on the Law of Treaties, 1155 U.N.T.S. 331 (entered into force 27 January 1980) 23 May 1969 ("VCLT").

[4] **RL-031**, *Canadian Cattlemen for Fair Trade v. United States* (UNCITRAL) Award on Jurisdiction, 28 January 2008 ("*Canadian Cattlemen – Award on Jurisdiction*"), ¶¶ 181-189, where the tribunal relied on the Article 1128 submission of Mexico and statements of Canada before other tribunals to establish "subsequent practice" and confirm the interpretation of Article 1101(1)(a).

[5] For example, the *Canadian Cattlemen* tribunal found that the absence of an Article 1128 submission from Canada in that arbitration "cannot be seen as evidence of Canadian support for the Claimants' position on this issue". *See* **RL-031**, *Canadian Cattlemen – Award on Jurisdiction*, ¶ 187.

II. THE CLAIMANTS MUST PROVE THE FACTS NECESSARY TO ESTABLISH THE TRIBUNAL'S JURISDICTION

3. All three NAFTA Parties agree that the determination of whether a tribunal has the jurisdiction to hear a claim imposes a burden that falls squarely on the claimant.[6] In its Article 1128 submission, the United States makes clear that:

> [i]n the context of an objection to jurisdiction, the burden is on the claimant to prove the necessary and relevant facts to establish that a tribunal has jurisdiction to hear its claim. Further, it is well-established that where "jurisdiction rests on the existence of certain facts, they have to be proven at the jurisdictional stage."[7]

4. Similarly, Mexico has recently explained its view that "[t]he jurisdiction of a NAFTA Chapter 11 tribunal cannot be presumed, it has to be established and the claimant has the burden of proving the necessary facts and fulfillment of the specific legal requirements."[8]

5. These views have been endorsed in recent jurisdictional rulings by NAFTA tribunals. For example, earlier this year, in finding that it did not have jurisdiction over a NAFTA Chapter Eleven claim, the *Westmoreland Mining Holdings* tribunal stated: "[i]f the Claimant cannot establish, on the balance of probabilities, those facts which are critical to founding jurisdiction, there is no jurisdiction."[9]

6. In light of the recent arbitral jurisprudence and the clearly expressed views of the NAFTA Parties, the Claimants' assertion that they need only establish the Tribunal's jurisdiction to some ill-defined "*prima facie"* standard, or that Canada must adduce evidence to challenge the jurisdiction that the Claimants seem to have presumed, must be rejected.[10] Jurisdiction cannot be presumed. There

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[6] *See* Canada's Counter-Memorial on Jurisdiction and the Merits, 17 February 2022 ("Canada's Counter-Memorial"), ¶¶ 109-111; Canada's Rejoinder Memorial on Jurisdiction and the Merits, 30 September 2022 ("Canada's Rejoinder"), ¶¶ 95-97.

[7] U.S. Article 1128 Submission, ¶ 4, citing, *inter alia*, **CL-047**, *Phoenix Action, Ltd. v. The Czech Republic* (ICSID Case No. ARB/06/5) Award, 15 April 2009, ¶ 61. *See also* **RL-201**, *Tennant Energy, LLC v. Government of Canada* (UNCITRAL) Second Submission of the United States of America, 25 June 2021, ¶ 3 (noting that "the claimant bears the burden of proof with respect to the factual elements necessary to establish jurisdiction").

[8] **RL-202**, *Tennant Energy, LLC v. Government of Canada* (UNCITRAL) Article 1128 Submission of Mexico, 25 June 2021, ¶ 5.

[9] **RL-131**, *Westmoreland – Final Award*, ¶ 193.

[10] *See e.g.*, Claimants' Reply Memorial on Jurisdiction and the Merits, 18 July 2022 ("Claimants' Reply"), ¶ 241.

should be no debate that it is for the Claimants, and the Claimants only, to positively establish the facts necessary to ground this Tribunal's jurisdiction.

III. NOT ALL "INTERESTS" QUALIFY AS "INVESTMENTS" UNDER NAFTA CHAPTER ELEVEN

7. To establish the Tribunal's subject-matter jurisdiction, the Claimants must prove that the dispute falls within the scope of NAFTA Chapter Eleven. Article 1101, the gateway to NAFTA Chapter Eleven, establishes that the Chapter applies to "measures adopted or maintained by a Party relating to: […] (b) *investments* of investors of another Party *in the territory of the Party*."[11] Accordingly, for the Tribunal to have jurisdiction over the Claimants' claim, the Claimants must establish that they held an investment in the territory of Canada.

8. As the United States explains in its Article 1128 Submission, "Article 1139 prescribes an exhaustive, not illustrative, list of what constitutes an investment for purposes of NAFTA Chapter Eleven."[12] All three NAFTA Parties agree.[13] For an interest to qualify as an investment under NAFTA Chapter Eleven, it must meet the requirements of one of the prescribed categories of investment.

9. The United States' Article 1128 Submission confirms Canada's interpretation of both Articles 1139(g) and 1139(h).

[11] **CL-2**, NAFTA Article 1101(1)(b) (emphasis added).

[12] U.S. Article 1128 Submission, ¶ 5, citing **CL-020**, *Grand River Enterprises Six Nations, Ltd., et al. v. United States of* America (UNCITRAL) Award, 12 January 2011 ("*Grand River – Award*"), ¶ 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."). *See also* **RL-024**, *Lion Mexico Consolidated L.P. v. United Mexican States* (ICSID Case No. ARB(AF)/15/2) Decision on Jurisdiction, 30 July 2018, ¶ 182 (describing Article 1139 as "offer[ing] a sophisticated and precise definition of protected investments: the provision lists eight categories of 'interests' which are considered as investments, and two categories which are excluded.").

[13] *See e.g.*, U.S. Article 1128 Submission, ¶ 5; Canada's Counter-Memorial, ¶ 132; Canada's Rejoinder, ¶ 147; **RL-198**, *B-Mex, LLC and Others v. United Mexican States* (ICSID Case No. ARB(AF)/16/3) Third Article 1128 Submission of Canada, 13 June 2022 ("*B-Mex – Canada's Third Article 1128 Submission*"), ¶ 9; **RL-144**, *Lone Pine Resources Inc., v. Government of Canada* (UNCITRAL) Article 1128 Submission of the United States, 16 August 2017, ¶ 2; **RL-199**, *B-Mex, LLC and Others v. United Mexican States* (ICSID Case No. ARB(AF)/16/3) Fourth Article 1128 Submission of the United States, 13 June 2022 ("*B-Mex – Fourth U.S. Article 1128 Submission*"), ¶ 2; **RL-145**, *Methanex Corporation v. United States of America* (UNCITRAL) Second Article 1128 Submission of the Government of Mexico, 15 May 2001, ("*Methanex – Mexico's Second 1128 Submission*"), ¶ 19.

A. NAFTA Article 1139(g) Does Not Recognize Mere Contingent Interests

10. The United States affirms in its Article 1128 Submission that not all interests qualify as "property" within the meaning of NAFTA Article 1139(g): "Chapter Eleven tribunals have consistently declined to recognize as 'property' mere contingent 'interests'."[14]

11. Moreover, the United States agrees with Canada that it is "appropriate to look to the law of the host State for a determination of the definition and scope of the 'property right' at issue."[15] If an interest does not constitute property under the host State's law, then it does not qualify as an "investment" under NAFTA Article 1139(g).

12. To illustrate, the United States notes that it "is well-established under U.S. law, for example, that that [*sic*] revocable government-granted licenses do not confer property interests that give rise to claims for compensation", particularly "when a person voluntarily enters a heavily regulated field."[16] Similarly, under Ontario law, emission allowances were created as non-compensable regulatory interests under a statute that also confers discretion on the government to act with respect to them. As a result, they are non-proprietary interests.[17]

B. NAFTA Article 1139(h) Requires More Than a Mere Commitment of Funds

13. The United States' Article 1128 Submission further confirms three issues concerning the interpretation of NAFTA Article 1139(h).

14. First, "[t]o qualify as an investment under NAFTA Article 1139(h), more than the mere commitment of funds is required".[18] An investor must also possess a "cognizable interest" in the host State's territory that arises out of the commitment of funds.[19] Mexico has taken the same position.[20]

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[14] U.S. Article 1128 Submission, ¶ 6.

[15] U.S. Article 1128 Submission, ¶ 6. *See also* Canada's Counter-Memorial, ¶ 136; Canada's Rejoinder, ¶ 122.

[16] U.S. Article 1128 Submission, fn. 6.

[17] *See e.g.*, **RER-3**, Second Expert Report of Prof. Larissa Katz, 28 September 2022, ¶¶ 7-9.

[18] U.S. Article 1128 Submission, ¶ 8.

[19] U.S. Article 1128 Submission, ¶ 8.

[20] **RL-200**, *B-Mex, LLC and Others v. United Mexican States* (ICSID Case No. ARB(AF)/16/3) Government of Mexico Response to Article 1128 Submissions, 24 June 2022 ("Mexico's Response to Article 1128 Submissions"), ¶ 6.

The agreement between the three Parties that more than a mere commitment of funds is required ought to be given considerable weight pursuant to VCLT Article 31(3).

15. A claimant bears the burden of establishing the "interest" it alleges arises out of its commitment of capital under NAFTA Article 1139(h). Here, the Claimants have merely asserted that they "held rights in a broader carbon trading business in Ontario under Article 1139(h) of the NAFTA",[21] but have failed to even identify the basic parameters of the rights they allege. Given that all three NAFTA Parties agree that a "cognizable interest" that meets the requirements of NAFTA Article 1139(h) is required, the Claimants have failed to meet their burden.

16. Second, the United States confirms the relevance of subparagraphs (h)(i) and (h)(ii) in ascertaining the type of interest that is protected by NAFTA Article 1139(h). In describing the cognizable interest that must arise from the commitment of capital or other resources, the United States explains:

> Specifically, Article 1139(h)(i) states that such interests might arise from, for example, turnkey or construction contracts or concessions. Similar interests might arise, according to Article 1139(h)(ii), from "contracts where remuneration depends substantially on the production, revenues or profits of an enterprise."[22]

17. The Claimants attempt to read the sub-paragraphs out of their interpretation of Article 1139(h).[23] As Canada has explained, that approach is contrary to the principles of proper treaty interpretation, and has been rejected by arbitral tribunals.[24] The sub-paragraphs elucidate the kind of interest that is captured by Article 1139(h). The United States agrees.

18. Third, the United States confirms that "[n]ot every economic interest that comes into existence as a result of a contract, however, constitutes an 'interest' as defined in Article 1139(h)."[25] In particular, Articles 1139(i) and (j) exclude from the definition of investment claims to money that

[21] Claimants' Reply, ¶ 534.

[22] U.S. Article 1128 Submission, ¶ 8.

[23] Claimants' Reply, ¶¶ 342-348.

[24] *See e.g.,* Canada's Rejoinder, ¶¶ 148-149.

[25] U.S. Article 1128 Submission, ¶ 9.

arise solely from commercial contracts for the cross-border sale of goods or services, the extension of credit in connection with a commercial contract, or any other claims to money that do not involve the kinds of interests contemplated by the definition of "investment".

19. Accordingly, and contrary to the Claimants' position in this case,[26] NAFTA Article 1139(h) is not a "catch-all" category of investment.

IV. REFLECTIVE LOSS IS NOT COGNIZABLE UNDER NAFTA ARTICLE 1116

20. The United States provides helpful insight on three issues of the interpretation of NAFTA Article 1116 before the Tribunal.

21. First, the United States recognizes that: "[a]n investor that has not incurred loss or damage by reason of, or arising out of, a Party's alleged breach cannot submit a claim to arbitration under NAFTA Chapter Eleven."[27] As Canada explained in its Counter-Memorial, where a claimant could not have incurred the loss or damage it alleges, the Tribunal lacks jurisdiction to hear its claim.[28]

22. Second, the United States recognizes the agreement of all three NAFTA Parties that reflective loss is not recoverable under NAFTA Article 1116:

> The United States therefore agrees with Canada and Mexico that investors must allege direct damage to recover under Article 1116 and that indirect damage to an investor, based on injury to an enterprise the investor owns or controls, may only be claimed, if at all, under Article 1117.[29]

23. As the United States points out, "[w]ere shareholders to be permitted to claim under Article 1116 for indirect injury, Article 1117's limited carve out from customary international law would be superfluous. Moreover, it is well-recognized that an international agreement should not be held to have tacitly dispensed with an important principle of international law 'in the absence of words

[26] Claimants' Reply, ¶ 313.

[27] U.S. Article 1128 Submission, ¶ 41.

[28] Canada's Counter-Memorial, ¶¶ 172-174. *See also* Canada's Rejoinder, ¶¶ 172-176.

[29] U.S. Article 1128 Submission, ¶ 45 (citations in original omitted). *See also* Canada's Rejoinder, ¶ 173.

making clear an intention to do so'."[30] The common understanding and interpretation of all three NAFTA Parties with respect to the type of loss or damage for which an investor may submit a claim to arbitration under NAFTA Article 1116 must be considered and given considerable weight by the Tribunal.

24. Third, the United States rightly states that NAFTA "does not, however, permit an investor to recover for indirect injuries that fall outside the scope of Article 1117(1), including where the alleged loss or damage is incurred by an enterprise […] of the same Party as the investor."[31] The Claimant Koch Industries alleges loss or damage in this case in the form of "the drop in value of its 100%-owned affiliate KS&T".[32] Canada has explained that there is no basis in NAFTA Chapter Eleven for a U.S. enterprise to claim loss allegedly suffered to the value of another U.S. enterprise in a claim against Canada.[33] The United States agrees.[34]

V. THE MINIMUM OF STANDARD UNDER NAFTA ARTICLE 1105 DOES NOT INCLUDE THE SWEEPING PROTECTIONS PORTRAYED BY THE CLAIMANTS

25. Canada, the United States, and Mexico agree that Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the standard of treatment to be afforded to investments of investors of another Party.[35]

[30] U.S. Article 1128 Submission, ¶ 50, citing to **RL-203**, *Elettronica Sicula S.p.A. (ELSI) (U.S. v. Italy)* 1989 I.C.J. 15, ¶ 50.

[31] U.S. Article 1128 Submission, ¶ 51.

[32] Claimants' Reply, ¶ 392.

[33] Canada's Rejoinder, ¶ 174.

[34] *See also* U.S. Article 1128 Submission, ¶ 44 ("Article 1117 does not apply where the alleged loss or damage is to an enterprise of a non-Party or of the same Part as the investor.")

[35] U.S. Article 1128 Submission ¶ 12; Canada's Counter-Memorial, ¶ 182; Canada's Rejoinder, ¶ 190. *See also*, **RL-145**, *Methanex – Mexico's Second 1128 Submission*, ¶ 9; **RL-204**, *Mercer International Inc v Government of Canada* (ICSID Case No. ARB(AF)/12/3) Submission of Mexico pursuant to Article 1128 of NAFTA, 8 May 2015, ¶¶ 18-20; **RL-162**, *Mesa Power Group, LLC v. Government of Canada* (UNCITRAL) Second Article 1128 Submission of Mexico, 12 June 2015 ("*Mesa – Second Article 1128 Submission of Mexico*"), ¶ 9; **RL-172**, *Eli Lilly and Company v. Government of Canada* (UNCITRAL) Submission of Mexico, 18 March 2016 ("*Eli Lilly – Submission of Mexico*") ¶¶ 10 & 12.

26. The NAFTA Free Trade Commission's 2001 *Notes of Interpretation of Certain Chapter 11 Provisions* (the "FTC Note")[36] are binding on tribunals established under Chapter Eleven.[37] As the Commission stated, 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."[38]

27. In order to establish that a rule of customary international law exists, a claimant must prove both state practice and *opinio juris*.[39] The United States' submission recognizes that "perfunctory reference to these requirements is not sufficient".[40] Relevant state practice and a sense of legal obligation must both be proven with evidence, and the burden of proof rests with the claimant.[41]

28. The three NAFTA Parties agree that the threshold for a breach of the minimum standard of treatment is high.[42] Here, the Claimants seek to impermissibly expand the protections of Article 1105.

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

[37] **CL-2**, NAFTA Article 1131(2).

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

[39] US Article 1128 Submission, ¶ 19; **CL-064**, *S.D. Myers, Inc. v. Government of Canada* (UNCITRAL) First Partial Award, 13 November 2000 ("*S.D. Myers – First Partial Award*"), ¶ 263. *See also* **RL-205**, *Resolute Forest Products Inc. v. Government of Canada* (UNCITRAL) Award, 25 July 2022, ¶ 744 ("Arbitral tribunals adjudicating fair and equitable treatment claims, whether under Article 1105 or under similar investment treaty provisions, have consistently exercised caution in approaching claims of violation of minimum treatment standards, especially in respect of State actions on matters of domestic policy that generally are treated with deference.").

[40] US Article 1128 Submission, ¶ 14.

[41] US Article 1128 Submission, ¶ 18; **RL-206**, *Mesa Power Group LLC v. Government of Canada* (UNCITRAL) Canada's Rejoinder on the Merits, 2 July 2014, ¶ 147 ("[I]t is a well-established principle of international law that the party alleging the existence of a rule of customary international law bears the burden of proving it. Thus, the burden is on the Claimant to prove that customary international law has evolved to include the elements it claims are protected."); **RL-163**, *Mesa Power Group, LLC v. Canada* (UNCITRAL) Second Article 1128 Submission of the United States, 12 June 2015 ("*Mesa – Second Article 1128 Submission of the U.S.*") ¶ 13 ("[T]he burden is on the claimant to establish the existence and applicability of a relevant obligation under customary international law that meets the requirements of State practice and *opinio juris*."); **RL-162**, *Mesa* – Second Article 1128 Submission of Mexico, ¶ 9 (concurring with the United States' position that the burden is on a claimant to establish a relevant obligation under customary international law that meets the requirements of State practice and *opinio juris*).

[42] US Article 1128 Submission, ¶ 12; Canada's Rejoinder, ¶ 190; **RL-162**, *Mesa – Second Article 1128 Submission of Mexico*, ¶ 8.

29. First, the NAFTA Parties are in agreement that NAFTA Article 1105 does not allow tribunals to second-guess government policy and decision making.[43] Moreover, the NAFTA Parties agree that a departure from domestic law does not automatically establish a violation of Article 1105.[44]

30. Second, the three NAFTA Parties agree that the minimum standard under 1105 does not protect investors' legitimate expectations.[45] The United States explains that "[a]n investor may develop its own expectations about the legal regime governing its investment, but those expectations impose no obligations on the State under the minimum standard of treatment."[46]

31. Third, Article 1105 does not include a general protection against discrimination, as the three NAFTA Parties agree.[47] As stated by the United States, "the customary international law minimum standard of treatment set forth in Article 1105(1) does not incorporate a prohibition on economic discrimination against aliens or a general obligation of non-discrimination."[48] Any claim of nationality-based discrimination must be made under NAFTA Article 1102 or Article 1103.[49]

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[43] U.S. Article 1128 Submission, ¶ 19; Canada's Counter-Memorial, ¶ 187; Canada's Rejoinder, ¶ 191; **RL-164**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL) Article 1128 Submission of Mexico, 12 January 2016 ("*Windstream – Mexico's Article 1128 Submission*"); ¶ 6; **RL-165**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL) Article 1128 Submission of the United States of America, 18 March 2016, ¶ 21.

[44] U.S. Article 1128 Submission, ¶ 19; Canada's Rejoinder, ¶ 198; **RL-170**, *Mesa Power Group, LLC v. Canada* (UNCITRAL) Canada's Response to 1128 Submissions, 26 June 2015, ¶ 14; **RL-162**, *Mesa – Second Article 1128 Submission of Mexico*, ¶ 22; **RL-163**, *Mesa – Second Article 1128 Submission of the U.S.*, ¶ 11.

[45] U.S. Article 1128 Submission, ¶ 26; Canada's Counter-Memorial, ¶¶ 192-195; Canada's Rejoinder, ¶ 208; **RL-172**, *Eli Lilly – Submission of Mexico*, ¶ 15 (Mexico agrees with Canada that the "mere failure to meet an investor's legitimate expectations does not constitute a breach [of] Article 1105(1)").

[46] U.S. Article 1128 Submission, ¶ 26.

[47] U.S. Article 1128 Submission, ¶ 26; Canada's Rejoinder, ¶ 193; **RL-167**, *Mercer International v. Government of Canada* (ICSID Case No. ARB(AF)/12/3) Submission of the United States, 8 May 2015, ¶ 21 ("State practice confirms that there is no 'categorical rule' under customary international law requiring non-discrimination."); **RL-164**, *Windstream – Mexico's Article 1128 Submission*, ¶ 20 ("Mexico also agrees with Canada that Article 1105(1) does not provide a blanket prohibition on discrimination against foreign investors or their investments.")

[48] U.S. Article 1128 Submission, ¶ 27.

[49] U.S. Article 1128 Submission, ¶ 27; **RL-168**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL) *Canada's Reply to the 1128 Submissions of the United States and Mexico*, January 2016, ¶ 27 ("[a]ll three NAFTA Parties agree that no established rule of customary international law has emerged that generally prohibits any nationality-based discrimination against foreign investors."); **RL-164**, *Windstream – Mexico's Article 1128 Submission*, ¶ 20.

32. Fourth, the three NAFTA Parties agree that in order to establish a denial of justice, a claimant must have exhausted local remedies unless such action is futile.[50] The United States notes that: "NAFTA Chapter Eleven tribunals are neither meant to, nor are they well equipped to, determine the likelihood of a successful result in exhausting domestic remedies."[51] In addition, the United States' Submission supports Canada's position that sovereign immunity clauses do not, in and of themselves, give rise to a denial of justice.[52] Canada agrees with the United States that: "the conferral of sovereign immunity protections on the host State government under municipal law does not, in general, effect a denial of justice, though it may do so if it is applied in a manner that discriminates against an investor on the basis of nationality."[53]

VI. ARTICLE 1110(1) INCORPORATES CUSTOMARY INTERNATIONAL LAW RULES ON EXPROPRIATION

33. Canada agrees with the United States that NAFTA Article 1110(1) reflects the customary international law standard with respect to expropriation.[54] It provides that 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, except for a public purpose; on a non-discriminatory basis; in accordance with due process of law and Article 1105(1); and on payment of compensation in accordance with paragraphs 2 through 6 of Article 1110.

[50] *See* U.S. Article 1128 Submission, ¶ 24; Canada's Counter-Memorial, ¶ 213; Canada's Rejoinder, ¶ 215; **RL-174**, *Loewen Group, Inc. and Raymond L. Loewen v. United States of America* (ICSID Case No. ARB(AF)/98) Second Article 1128 Submission of the United Mexican States, 9 November 2001, pp. 8-9.

[51] U.S. Article 1128 Submission, ¶ 24.

[52] *See* U.S. Article 1128 Submission, ¶ 22; Canada's Rejoinder, ¶ 214. *See also* **RL-207**, Harvard Research Draft, The Law of Responsibility of States for Damage Done in Their Territory to the Person or Property of Foreigners, art. 9, 23 AM. J. INT'L L. SP. SUPP. 131, 134 (1929); **RL-208**, Charles de Visscher, *Le déni de justice en droit international*, 52 R.C.A.D.I. 367, 395 (1935); **RL-209**, Alwyn V. Freeman, *International Responsibility of States for Denial of Justice* 228 (reprint 1970) (1938).

[53] U.S. Article 1128 Submission, ¶ 24.

[54] U.S. Article 1128 Submission, ¶ 29; Canada's Counter-Memorial, ¶ 229. *See also* **RL-057**, *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.")

34. As the United States notes, the first step in analysing whether there has been a breach of Article 1110 is to determine whether there is an investment capable of being expropriated.[55] As articulated in the United States Article 1128 Submission, "a property right or property interest must have been taken."[56] The domestic law of the host State must be examined for "the definition and scope of the alleged property right or property interest at issue, including any applicable limitations."[57]

35. For there to be an expropriation, a property right must have been taken.[58] 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.[59] Mere interference with an investor's use or enjoyment of the benefits associated with property is insufficient to constitute an expropriation at international law as reflected in Article 1110(1).[60]

36. Consideration of whether there has been an indirect expropriation also includes whether the measure interferes with distinct, reasonable, investment-based expectations. The United States and Canada agree that: "Whether an investor's investment-backed expectations are reasonable depends, to the extent relevant, on factors such as whether the government provided the investor with binding written assurances and the nature and extent of governmental regulation or the potential for government regulation in the relevant sector."[61]

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[55] U.S. Article 1128 Submission, ¶ 29. *See also* **RL-075**, *Generation Ukraine v Ukraine* (ICSID Case No. ARB/00/9) Award, 16 September 2003, ¶ 6.2; **RL-076**, *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v Islamic Republic of Pakistan* (ICSID Case No. ARB/03/29) Award, 27 August 2009, ¶ 442.

[56] U.S. Article 1128 Submission, ¶ 29.

[57] U.S. Article 1128 Submission, ¶ 29. *See also* Canada's Counter-Memorial, ¶ 238; Canada's Rejoinder, ¶ 232.

[58] **CL-018**, *Glamis Gold, Ltd. v. United States of* America (UNCITRAL) Final Award, 8 June 2009 ("*Glamis – Award*"), ¶ 356; **CL-064**, *S.D. Myers – First Partial Award*, ¶ 280.

[59] **CL-086**, *Pope & Talbot Inc. v. Government of Canada* (UNCITRAL) Interim Award, 26 June 2000 ("*Pope & Talbot – Interim Award*"), ¶ 102; **CL-018**, *Glamis – Award*, ¶ 357; **CL-020**, *Grand River – Award*, ¶ 148; **RL-096**, *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States* (ICSID Case No. ARB (AF)/00/2) Award, 29 May 2003, ¶ 115.

[60] **CL-018**, *Glamis – Award*, ¶¶ 356-357; **CL-086**, *Pope & Talbot – Interim Award*, ¶¶ 101-102; **CL-064**, *S.D. Myers – First Partial Award*, ¶¶ 281-282.

[61] U.S. Article 1128 Submission, ¶ 33, citing to **CL-089**, *Methanex Corporation v. United States of America* (UNCITRAL) Final Award on Jurisdiction and Merits, 3 August 2005 ("*Methanex – Final Award*"), Part IV, Ch. D, ¶ 9; **CL-020**, *Grand River – Award*, ¶¶ 144-145 ("The Tribunal also notes that trade in tobacco products has historically been the subject of close and extensive regulation by U.S. states, a circumstance that should have been known to the Claimant

37. In considering allegations that the State has "taken" or "expropriated" the investor's property through its regulatory powers, consideration must be given to State's police power, which is a well recognized concept at customary international law: a host State is not required to compensate an investor for any loss caused by the imposition of a non-discriminatory regulatory measure designed and applied to protect legitimate public welfare objectives, as such measures do not constitute an expropriation.[62] This principle allows governments the necessary flexibility to regulate without having to pay compensation for every effect of regulation.[63]

VII. PRINCIPLES OF DAMAGES: CAUSATION AND CONTRIBUTORY FAULT

38. The NAFTA Parties agree that in order to be entitled to damages, a claimant must demonstrate a sufficient causal link between alleged breach and loss,[64] on the basis of satisfactory evidence that is not inherently speculative.[65]

39. Inherent in the NAFTA requirement that damages are limited to "loss or damage by reason of, or arising out of" the alleged breach[66] is the need for a claimant to establish both factual causation and proximate causation. As the United States points out, under factual causation, an act causes an outcome if the outcome would not have occurred in the absence of the act.[67] Further, Canada agrees with the United States that proximate causation requires that any loss or damage cannot be based on

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from his extensive past experience in the tobacco business. An investor entering an area traditionally subject to extensive regulation must do so with awareness of the regulatory situation.")

[62] *See e.g.*, **RL-210**, *Methanex Corporation v. United States of America* (UNCITRAL) Fourth Submission of The Government of Canada, 30 January 2004, ¶ 14; **CL-089**, *Methanex – Final Award*, Part IV, Chapter D, ¶ 7; **CL-064**, *S.D. Myers – First Partial Award*, ¶¶ 263 and 281-282; **RL-107**, *Joseph Charles Lemire v. Ukraine* (ICSID Case No. ARB/06/18) Decision on Jurisdiction and Liability, 14 January 2010, ¶¶ 273, 505; **RL-089**, *Suez, Sociedad General de Aguas de Barcelona SA, and InterAgua Servicios Integrales del Agua SA v. The Argentine Republic* (ICSID Case No ARB/03/17) Decision on Liability, 30 July 2010, ¶ 128; **RL-048**, *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, ¶ 305; **RL-019**, *Koch Minerals Sarl and Koch Nitrogen International Sarl v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB/11/19) Award, 30 October 2017, ¶¶ 7.17-7.22.

[63] *See e.g.*, **CL-067**, *Chemtura Corporation v. Government of Canada* (UNCITRAL) Award, 2 August 2010, ¶ 266.

[64] U.S. Article 1128 Submission, ¶ 37.

[65] U.S. Article 1128 Submission, ¶ 36. *See also* **RL-200**, *Mexico's Response to Article 1128 Submissions*, ¶ 23, **RL-199**, *B-Mex – Fourth U.S. Article 1128 Submission*, ¶ 60; **RL-198**, *B-Mex – Canada's Third Article 1128 Submission*, ¶ 45.

[66] NAFTA Articles 1116 and 1117.

[67] U.S. Article 1128 Submission, ¶ 37.

an assessment of acts, events or circumstances not attributable to the alleged breach.[68] Injuries that are not sufficiently "direct", "foreseeable" or "proximate" may not, consistent with applicable rules of international law, be considered when calculating a damages award.[69]

40. Canada and the United States agree that "it is well established that a claimant may not be awarded reparation for losses to the extent of its contribution to its losses, and nothing in the NAFTA indicates otherwise."[70] As a result, any award of damages must be reduced to take into account the Claimants' role in their alleged loss.[71]

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Respectfully submitted on behalf of Canada,

E. Alexandra Dosman
Krista Zeman
Michelle Hoffmann
Stefan Kuuskne
Dmytro Galagan
Brendan Robertson

Trade Law Bureau

[68] U.S. Article 1128 Submission, ¶ 40.

[69] **CL-051**, ILC Draft Articles on State Responsibility with Commentary, Art. 31, Commentary (10). *See also* **RL-200**, *Mexico's Response to Article 1128 Submissions*, ¶ 23 ("The breach complained of must be the proximate cause of the damages claimed. Mexico expressly endorses Canada's statement that the claimant is required to prove that "the wrongful conduct was a sufficient, proximate, adequate, foreseeable or direct cause of the injury.")

[70] U.S. Article 1128 Submission, ¶ 52.

[71] Mexico recently agreed on this point. *See* **RL-200**, *Mexico's Response to Article 1128 Submissions*, ¶ 23 ("Damages should take into account any contributory fault on the part of the Claimant").