

**MOBIL INVESTMENTS CANADA INC. & MURPHY OIL CORPORATION**

v.

**GOVERNMENT OF CANADA**

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

**PARTIAL DISSENTING OPINION**

**PROFESSOR PHILIPPE SANDS Q.C.**

1. The Tribunal has had little difficulty in reaching a clear consensus that the 2004 Guidelines and their application to the Hibernia and Terra Nova (“the Projects”) do not violate Article 1105 of the NAFTA, but that they are caught by the Article 1106 rules relating to performance requirements. The outstanding issue is whether the 2004 Guidelines – and their application to the Projects – may benefit from Canada’s reservation under Article 1108(1). In particular, do the 2004 Guidelines as applied to the Projects constitute a “subordinate measure” that has been adopted “consistent with” the “non-conforming measure” maintained by Canada as set out in its Schedule to Annex I?
2. The Majority of the Tribunal concludes that, in order to be covered by Canada’s reservation, the subsidiary measure that is reflected in the 2004 Guidelines must be adopted under the authority of and be consistent with both the Federal Accord Act and the earlier Benefits Plans adopted in relation to the Projects. The Majority has not found any inconsistency between the 2004 Guidelines and Federal Accord Act taken on its own, a conclusion with which I agree.<sup>1</sup> They have further concluded, however, that insofar as the 2004 Guidelines are applied to the Projects, they are not covered by Canada’s reservation, because (1) they are to be “evaluated with respect to the reserved measure and the existing subordinate measures that meet the criteria of Article 2 (f),”<sup>2</sup> and (2) the existing subordinate measures include the earlier Benefits Plans adopted in respect of those projects

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<sup>1</sup> See e.g. Award, paras. 365 and 387.

<sup>2</sup> Award, para. 319.

(by Decision 86.01 for Hibernia and Decision 97.02 for Terra Nova), and (3) as applied to the Projects, the 2004 Guidelines are not consistent with Decisions 86.01 and 97.02.

3. It is with respect to this further conclusion that I am in fundamental disagreement. This partially dissenting opinion explains the basis for my conclusion that the 2004 Guidelines (and their application to the Projects) are to be assessed for consistency and lawfulness under the NAFTA, exclusively by reference to the Federal Accord Act, and that since they are consistent with the requirements of the Federal Accord Act they are covered by Canada's reservation to Article 1106. Accordingly, on the basis of considerations canvassed early on and here set out in detail, I dissent from certain paragraphs of the Award in relation to Article 1108,<sup>3</sup> and from the entirety of the section on Damages which, on the basis of my conclusion, is a matter that does not arise at all.<sup>4</sup> To the extent that the Award sets out the arguments of the parties, as well as the submissions of Mexico and the United States, I will not repeat matters there addressed.

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4. The issue giving rise to the difference turns on the meaning of the words "the measure" in Article 1108(1), which provides that Article 1106 does "not apply to (a) any existing non-conforming measure that is maintained by (i) a Party at the federal level, as set out in its Schedule to Annex I or II." This question does not appear to have arisen before, is a matter of first impression and is of considerable significance for the reservations under the NAFTA more generally. Although the issue was only recognised to be central somewhat late in the proceedings, it was fully and well argued by both parties. The conclusion turns on the application of the rules of treaty interpretation reflected in the 1969 Vienna Convention on the

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<sup>3</sup> The partial dissent relates to Award, paras. 318-349, 367-397 and 402-406.

<sup>4</sup> The partial dissent relates to Award, paras. 407-482.

Law of Treaties (“VCLT”),<sup>5</sup> which both parties have treated as being applicable to Article 1108 and to Canada’s reserved measure, and on the evidence that is before the Tribunal.

5. Under the NAFTA, the three NAFTA Parties were free to make reservations as appropriate to their national needs, and each has done so. As I understand it, the reservations were not the subject of formal negotiations, as each Party was free to decide on its reservations. In relation to Article 1106 and other provisions of the NAFTA, each Party has made a significant number of reservations. It is apparent on their face that they were not made lightly and concern matters of considerable national interest.
6. In the present case, Canada’s reservation is made in respect of an agreement entered into between Canada and Newfoundland in 1985, known as the Atlantic Accord, the Memorandum of Agreement between the Government of Canada and the Government of Newfoundland and Labrador on Offshore Oil and Gas Resource Management and Revenue Sharing.<sup>6</sup> The Atlantic Accord provides in section 51 that:

“a plan must be submitted satisfactory to the Board for the employment of Canadians and, in particular, members of the provincial labour force and for providing manufacturers, consultants, contractors and service companies in Newfoundland and other parts of Canada with a full and fair opportunity to participate in the supply of goods and services used in that work or activity.”
7. The Atlantic Accord is implemented into federal and provincial law by the 1987 Canada-Newfoundland Atlantic Accord Implementation Act (“Federal Accord Act”)<sup>7</sup> and the 1990 Canada-Newfoundland and Labrador Atlantic Accord

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<sup>5</sup> Both parties agreed that the principles set forth in the VCLT govern the interpretation of the NAFTA, including the reservations.

<sup>6</sup> CA-10, The Atlantic Accord.

<sup>7</sup> CA-11, Federal Accord Act.

Implementation Newfoundland and Labrador Act (“Provincial Accord Act”).<sup>8</sup> Together these are known as the “Accord Acts”. Section 45 of the Federal Accord Act sets out the requirements concerning a Benefits Plan, including the obligation to ensure that expenditures on research and development be carried out in the Province, and for education and training to be provided in the Province.<sup>9</sup> Section 151.1 allows the Board to issue and publish guidelines with respect to the application and administration of section 45. It is a matter of public record that the Atlantic Accord addresses matters of considerable significance and sensitivity in the relations between Newfoundland and Canada.

8. Article 1108 and Annex I of the NAFTA allow reservations in respect to Article 1106. They adopt the same approach as that set forth by Article 1409 and Annex VII of the NAFTA, in relation to the financial services sector. On its face, Article 1108 establishes a clear distinction between a “measure” that has been reserved, and a “subordinate measure” adopted under that “measure”.
9. Article 1108(1) provides that Article 1106 does not apply *inter alia* to:
  - “(a) any existing non-conforming measure that is maintained by
    - (i) a Party at the federal level, as set out in its Schedule to Annex I or III (...);
    - (b) the continuation or prompt renewal of any non-conforming measure referred to in subparagraph (a); or
    - (c) an amendment to any non-conforming measure referred to in subparagraph (a) to the extent that the amendment does not decrease the conformity of the measure, as it existed immediately before the amendment, with Articles 1102, 1103, 1106 and 1107.”

Article 1108(2) requires each Party to

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<sup>8</sup> CA-12, Provincial Accord Act.

<sup>9</sup> Section 45(3).

“set out in its Schedule to Annex I, within two years of the date of entry into force of [the NAFTA], any existing nonconforming measure maintained by a state or province, not including a local government.”

Canada’s reservation was duly set out.

10. Annex I (entitled ‘Reservations for Existing Measures and Liberalization Commitments’) to the NAFTA provides further guidance to the NAFTA Parties as to the details they are to set out in their Schedules. Annex I provides *inter alia*:

“1. The Schedule of a Party sets out, pursuant to Articles 1108(1) (Investment) [...] the reservations taken by that Party with respect to existing measures that do not conform with obligations imposed by:

[...]

(d) Article 1106 (Performance Requirements),

[...]

and, in certain cases, sets out commitments for immediate or future liberalization.”

11. Paragraph 2 of Annex 1 specifies eight elements that “each reservation must set out.” The reservation must set out the sector, sub-sector and industry classification, and it must specify the type of reservation, the level of government taking the measure, and the timetable (if there is any) for a phase-out of the non-conforming measure. For the purposes of the present case, paragraph 2(f) of Annex I is of central importance in setting out the specification and description of the measure that is being reserved. Paragraph 2(f) of Annex I provides that:

“(f) **Measures** identifies the laws, regulations or other measures, as qualified, where indicated, by the **Description** element, for which the reservation is taken. A measure cited in the **Measures** element

(i) means the measure as amended, continued or renewed as of the date of entry into force of this Agreement, and

(ii) includes any subordinate measure adopted or maintained under the authority of and consistent with the measure.”

Unlike the requirement to “set out” a measure, there is no requirement by Article 1108 or otherwise for a Party to set out any “subordinate measure” that has been adopted or maintained. Whilst an investor can easily ascertain, by reference to the reserved measures set out pursuant to Annex I, any reserved measure adopted by a Party, it cannot so ascertain any existing or new “subordinate measure”. There is no requirement that these be included in Annex I, or listed or published anywhere else.

12. Paragraph 3 of Annex I addresses the interpretation of a reservation:

“3. In the interpretation of a reservation, all elements of the reservation shall be considered. A reservation shall be interpreted in the light of the relevant provisions of the Chapters against which the reservation is taken.

To the extent that:

(a) the **Phase-Out** element provides for the phasing out of non-conforming aspects of measures, the **Phase-Out** element shall prevail over all other elements;

(b) the **Measures** element is qualified by a liberalization commitment from the **Description** element, the **Measures** element as so qualified shall prevail over all other elements; and

(c) the **Measures** element is not so qualified, the **Measures** element shall prevail over all other elements, unless any discrepancy between the **Measures** element and the other elements considered in their totality is so substantial and material that it would be unreasonable to conclude that the **Measures** element should prevail, in which case the other elements shall prevail to the extent of that discrepancy.”

13. A few brief preliminary observations may be made in respect of Article 1108 and Annex I. These are not in dispute between the parties in these proceedings:

- each NAFTA Party is free to adopt a reservation in respect of Article 1106;

- a reserving Party must meet certain requirements, including the publication of specified information on specified “elements” of the reservation;
- Article 1108 and Annex I distinguish between (i) a “non-conforming measure” as referred to in Article 1108(1) and set out in the Schedule to Annex I, and (ii) “any subordinate measure” (as referred to in Annex 1, paragraph 2(f)(ii), but not required to be set out in the Schedule to Annex I);
- Article 1108 and Annex I further distinguish between (i) an amendment to a “non-conforming measure” referred to in Article 1108(1), and (ii) the adoption of a new “subordinate measure” under a “non-conforming measure”, and provide for a different standard to be applied in respect of each.

The distinction between a “non-conforming measure” and “any subordinate measure” is central to this case and to the system of reservations established under the NAFTA.

14. In accordance with these provisions, Canada made a reservation in relation to the Federal Accord Act. The reservation is set out in full at paragraph 99 of the Award. The law set out in the “Measures element” is:

*“Canada - Newfoundland Atlantic Accord Implementation Act, S.C. 1987, c. 3” (“the Federal Accord Act”).*

This is Canada’s “non-conforming measure entry”, as described by the United States.<sup>10</sup> The “Description element” of the Federal Accord Act includes a reference to the requirement that the Federal Accord Act

“requires that the benefits plan ensure that [...] (b) expenditures be made for research and development to be carried out in the province, and for education and training to be provided in the province.”

There is no dispute between the parties that the Federal Accord Act, as qualified by the “Description element” constitutes the “existing non-conforming measure”

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<sup>10</sup> U.S. 2<sup>nd</sup> Art. 1128, para. 10.

in respect of which the application of Article 1106 has been reserved. This ‘Measures element’ refers to a reservation that has been adopted at the federal level. Moreover, the reservation is not qualified by any “liberalization commitment from the Description element.”<sup>11</sup> Canada’s reservation is open-ended and not time limited. Canada has no obligation over time to decrease non-conforming aspects of the Federal Accord Act with Article 1106.

15. On its face, Canada’s reservation is a broad one. It refers to the requirement that a Benefits Plan shall “ensure” that certain expenditure requirements that would otherwise be prohibited by Article 1106 are to be imposed. The reservation does not specify any particular *modalities* for giving effect to such required expenditures, or the *amount* of any expenditure that may be imposed, whether by way of floor or ceiling, or to any formula or other means for *quantifying* the amount of any required expenditures. The Tribunal is agreed on this.<sup>12</sup> The Federal Accord Act merely refers to the broad principles, leaving it open to Canada’s federal or provincial authorities to determine, as they see appropriate and in accordance with the requirements of the Federal Accord Act, (i) the modalities for ensuring that the expenditure requirement is met, and (ii) the level of expenditure that would be required for an investor to meet the requirements of the reserved measure. There is nothing on the face of the reservation itself that limits the ability of the federal or provincial governments to adopt or maintain any particular approach or methodology to ensure that Benefits Plans require expenditures to be made for research and development to be carried out in Newfoundland.

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16. Articles 1106 and 1108 of the NAFTA do not refer to the term “subordinate measures”, and it is not to be found anywhere in Chapter 11 of the NAFTA. As

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<sup>11</sup> See NAFTA Annex I, para. 3(b).

<sup>12</sup> Award, para. 387.

relevant to these proceedings, it appears only in paragraph 2(f) of Annex I (entitled ‘Measures’), which sets out two types of measures that may be covered by a reservation (measures and subordinate measures), and the conditions that a “subordinate measure” must meet if it is to be covered by a reservation and avoid being caught by Article 1106.

17. Paragraph 2(f) of Annex I is divided into two sentences. The first sentence provides that “Measures identifies the laws, regulations or other measures, as qualified [...] by the Description element.” It follows from this that the term “Measures” refers to a measure that is expressly referred to in a Party’s Schedule to Annex I, and only to the extent “qualified [...] by the Description element.” The Federal Accord Act is set out in Canada’s Schedule I, and is an instrument cited in the ‘Measures’ element.

18. As noted above, the second sentence of paragraph 2(f) provides that

“A measure cited in the Measures element

- (i) means the measure as amended, continued or renewed as of the date of entry into force of [the NAFTA], and
- (ii) includes any subordinate measure adopted or maintained under the authority of and consistent with the measure.”

This sentence makes clear the distinction between “the measure” (referred to in paragraph 2(f)(i)) and “any subordinate measure” (referred to in paragraph 2(f)(ii)). Neither party has argued that the existing subordinate measures (the 1987 Guidelines, Decision 86.01, or Decision 97.02) are to be considered a “measure” within the meaning of paragraph 2(f)(i). For the purposes of this case, “the measure” there referred to only means the Federal Accord Act (sections 45 and 151.1), which is expressly listed in the Respondent’s entry in that reservation.

19. Paragraph 2(f)(ii) of Annex I sets out the conditions that are to be met for any “subordinate measure” to be covered by a reservation. It provides that a

subordinate measure will be covered by a reservation if it has been “adopted or maintained *under the authority of and consistent with the measure.*” A number of points may be made.

20. *First*, the ordinary meaning of these words indicates that two cumulative conditions must be met for a “subordinate measure” to be reserved. The “subordinate measure” must be:

- under the authority of the reserved measure set out in the Party’s Schedule to Annex I, and
- consistent with the reserved measure set out in the Party’s Schedule to Annex I.

21. *Second*, the ordinary meaning of these words indicates that the two conditions are exhaustive, so that there are no other conditions that must be met. In particular, there is no additional requirement – as exists in relation to the adoption of an amendment to a listed measure – that a new subordinate measure should not decrease conformity with the situation that pertains prior to the adoption of the new subordinate measure, a matter addressed in more detail below. This is a significant difference. The conditions are ‘authority’ and ‘consistency’, no more and no less.

22. *Third*, the conditions of ‘authority’ and ‘consistency’ are connected: both requirements are to be assessed by reference to “the measure”, which indicates that it must be the same “measure”. At paragraph 324 the Majority recognizes that in this case ‘authority’ is to be determined solely by reference to the Federal Accord Act as “it clearly makes no sense to suggest that the 2004 Guidelines [...] have to be ‘under the authority’ of the [...] Benefits Plans and Board Decisions,” since “both sets of subordinate instruments are [...] in a vertical relationship to that Act but are not in a vertical relationship with each other.” The Majority states, however, that it can envision other situations

“where there are a number of subordinate measures that are in a vertical relationship to each other such that a new rule or regulation is specifically introduced in order to implement a provision of an existing subordinate measure, both of which legally owe their existence up to the reserved measure. In such circumstances, to understand whether the new subordinate measure is under the authority of the reserved measure, the treaty interpreter would be required to look at the reserved measure as well as other subordinate measures in the vertical chain in order to make sense of the legal framework.”<sup>13</sup>

The conclusion that a new subordinate measure can draw its authority from an existing subordinate measure, rather than the listed measure, is mere assertion: does the ‘authority’ of a new subordinate measure derive from the measure that is listed in the Annex, or a subordinate measure to that measure, or both? As a matter of law, the answer could be any of the three, although in every case ultimate authority must logically be the listed measure (a new subordinate measure adopted under the authority of an existing subordinate measure that is not itself under the authority of a listed measure would not be “under the authority of the measure”). On what basis then does the Majority conclude that authority could derive from an existing subordinate measure rather than the listed measure? There is no way to know, as no explanation is given as to why authority in such a situation refers to (i) the listed measure or (ii) the listed measure and the existing subordinate measure. For this reason, in the absence of clear explanation, the impression is created that the Majority may simply have assumed the conclusion it comes to. In any event, on the approach of the Majority, in the present case it is apparent that the words “the measure” mean one thing for the assessment of ‘authority’ (only the Federal Accord Act) and a different thing for the assessment of ‘consistency’ (the Federal Accord Act and Decisions 86.01 and 97.02).

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<sup>13</sup> Award, para., 324.

23. *Fourth*, the same two conditions apply to existing subordinate measures (the 1987 Guidelines, Decision 86.01, and Decision 97.02) and “new subordinate measures” (the 2004 Guidelines and measures taken in application thereof).

24. *Fifth*, it is plain that the two conditions for assessing whether a subordinate measure is covered by a reservation differ from the conditions that determine whether an amendment to a measure is covered by a reservation. Under Article 1108(1)(c), an amendment to a measure that has been reserved will only benefit from the reservation

“to the extent that the amendment does not decrease the conformity of the measure, as it existed immediately before the amendment, with [Article 1106].”

This requires an assessment of ‘conformity’ immediately before the amendment is adopted, and an assessment of the effect of the amendment on ‘conformity’. If the amendment decreases conformity it will not benefit from the reservation. As already noted, there is no such requirement for assessing a new subordinate measure. The NAFTA Parties have not explicitly determined that there is any requirement that a new subordinate measure should “not decrease the conformity of the measure, as it existed immediately before” the adoption of the new subsidiary measure. On its face, therefore, a new ‘subordinate measure’ may lead to a situation in which additional burdens are imposed, so that conformity may be decreased, but the requirements of ‘authority’ and ‘consistency’ are still met (all three NAFTA Parties confirm that this is the approach they intended and drafted).<sup>14</sup> Despite the manifest difference in the test to be applied, and notwithstanding its concurrence that the 2004 Guidelines are consistent with the Federal Accord Act, the Majority (albeit with a variety of formulations) applies the standard relating to amendments to its consideration of the consistency of the application of the 2004 Guidelines to the Projects. The Majority compares the extent of inconsistency introduced by the 2004 Guidelines with that which pertained before the 2004 Guidelines were adopted (although it never actually sets

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<sup>14</sup> Mex. 2<sup>nd</sup> Art. 1128, paras. 4 -5; U.S. 2<sup>nd</sup> Art. 1128, para. 10.

out the standard that is to be applied in determining where a line has been crossed so as to give rise to “inconsistency”).<sup>15</sup> This is despite the fact that, for obvious reasons, neither party has argued that the 2004 Guidelines, Decision 86.01 and Decision 97.02 are to be treated as amendments to the Federal Accord Act. It is difficult to see how they could so argue: the 2004 Guidelines are not amendments to the Federal Accord Act, or amendments to an existing subordinate measure (understandably, the Majority does not proceed on the basis that the words “the measure” in Article 1108(1)(c) also include a “subordinate measure” and the existing Benefits Plans). They are “subordinate measures” to the Federal Accord Act. As such, the question of whether or not the application of the 2004 Guidelines “decreases conformity” or “increases inconsistency,” for example, with Article 1106, by reference to the situation that existed prior to their application, is wholly without justification. The Majority has, in effect, introduced a new element that the drafters of the NAFTA plainly intended to exclude. The Majority provides no proper explanation to support its approach.

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25. The points set out in the preceding paragraphs should not be contentious. The heart of my disagreement with the Majority is as to the meaning and effect of the words “the measure”, as used in paragraph 2(f)(ii) of Annex I (“adopted or maintained under the authority of and consistent with *the measure*”). The Majority concludes that these words, “the measure” mean both the Federal Accord Act and existing subordinate measures, namely the 1987 Guidelines, Decision 86.01 and Decision 97.02. How is this conclusion reached?

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<sup>15</sup> The Majority uses a raft of different formulations: see *e.g.* Award, para. 328 (“*the extent of consistency or inconsistency* introduced by the new subordinate measure vis-a-vis the obligation against which the reservation is taken”); para. 330 (“the new measures *enlarge* the non-conforming features of the reservation”); para. 332 (“new subordinate measures *extend* the non-conformity of the legal framework vis-a-vis the obligation against which the original measure is reserved”); para. 402 (the 2004 Guidelines “render the local content regime that arises, *more non-conforming* with Article 1106” than before); para. 404 (the new subordinate measures “significantly alter the legal obligations required of the Claimants in such ways as to render the local content regime *more contradictory and incompatible with Article 1106*”). Emphasis added.

26. The Majority adopts a three-limbed approach. First, it relies on the interpretative note, a point to which I return below, at paragraph 32. Second, it asserts that the text of the reserved measure makes specific reference to the words “benefits plans.”<sup>16</sup> It is difficult to see how the mere utilisation of the words “benefits plans” in the abstract – with no express reference to Decisions 86.01 or 97.02 or any other Benefits Plans that may have been adopted – can support such a conclusion. It is a classic bootstraps approach: the reserved measure as listed is to be treated as also listing Decisions 86.01 and 97.02 because they are concerned with the same subject matter as the actual law that is listed. If Canada had wanted to list Decision 86.01 (or other measures that are not in the form of primary legislation) it could presumably have done so, since it (as well as Mexico and the United States) have listed other measures that are subordinate to primary legislation in their respective Schedules to Annex I.<sup>17</sup>

27. The third limb of the Majority’s argument is constructed around the need to avoid undue changes to the “legal framework”<sup>18</sup> that existed prior to the adoption and application of the 2004 Guidelines, and the need to assess whether the NAFTA Party, by adopting a subordinate measure, is “altering *their framework of laws and associated measures*.”<sup>19</sup> According to the Majority, an interpretation of the words “the measure” that “ignores subordinate measures that are explicitly referenced as the necessary instruments to implement the requirements of the non-conforming measure would ignore a potentially crucial part of *the legal framework*.”<sup>20</sup> From this initial reference, the Majority then constructs an edifice,

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<sup>16</sup> Award, para. 322.

<sup>17</sup> See e.g. *Canada Oil and Gas Land Regulations*, C.R.C. 1978, c. 1518, listed in Canada’s Schedule to Annex I (along with the Federal Accord Act) in relation to the oil and gas sector and national treatment (Article 1102); See e.g. Mexico, *Reglamento de Telecomunicaciones*; See e.g. the United States FCC Decision on International Communications Policies Governing Designation of Recognized Private Operating Agencies, 104 FCC 2d, 208, n. 123, n. 126 (1986).

<sup>18</sup> Award, para. 333.

<sup>19</sup> Award, para. 332, emphasis added. This suggests that the Majority is introducing by alternative means the arguments (made by the Claimants in relation to Article 1105, and rejected by the Tribunal) concerning the need to avoid certain changes to the regulatory framework that existed when the investment was made.

<sup>20</sup> Award, para. 322, emphasis added.

to the effect that Decisions 86.01 and 97.02 were amongst the instruments that “constituted *the legal framework* that applied to these investment projects prior to the introduction of the 2004 Guidelines.”<sup>21</sup> Its next step is to read into the text a need to avoid an inappropriate fracturing of or change to the pre-existing “legal framework”:

“[c]onsideration of the latest subordinate measure exclusively against the reserved measure even if other subordinate measures have been introduced would reduce the evaluation of consistency to *only a subset of the framework of measures* that apply to the investment project,”<sup>22</sup> and would result in “a superficial and partial examination of *the legal system*.”<sup>23</sup>

Finally, the Majority states that “[t]here is little basis for evaluating the consistency of the new subordinate measure without examining *the totality of measures that apply to the investment project*.”<sup>24</sup>

28. Other references to the concept of a “legal framework” abound in the approach of the Majority,<sup>25</sup> but no explanation is provided as to its source, or from where is drawn the idea of the need to preserve the integrity of the “legal framework” by treating it holistically. The concept seems to have been plucked out of the air. Chapter XI of the NAFTA does not include the words “legal framework”, and they do not feature in the Interpretative Note. Indeed, the words “legal framework” are not referred to anywhere in the NAFTA.<sup>26</sup> The closest one gets to the notion of a “legal framework” is the reservation Mexico has entered in relation to Chapter 14 of the NAFTA, and their application to “existing Operations of Foreign Commercial Banks,” which states *inter alia* that:

“The benefits of this Agreement shall not be extended to a foreign bank branch existing in Mexico on the date of entry into force of this

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<sup>21</sup> Award, para. 374, emphasis added.

<sup>22</sup> Award, para. 326, emphasis added.

<sup>23</sup> Award, para. 328, emphasis added.

<sup>24</sup> Award, para. 328, emphasis added.

<sup>25</sup> See also Award, paras. 387, 394, referring to “the earlier legal framework”, 403, 404, 394.

<sup>26</sup> The closest one gets is in Chapter 7 of the NAFTA, but this does not assist the Majority since it refers to “a framework of rules and disciplines to guide the development, adoption and enforcement of sanitary and phytosanitary measures” (Article 709).

Agreement. The existing legal regime will continue to apply to such a branch for so long as it operates in that form.”

It seems that when a NAFTA Party wanted to ensure that an “existing legal regime” applicable on a particular date should continue to apply, it entered language to make that clear.<sup>27</sup> By contrast, Chapter XI refers to “any existing non-conforming measure that is maintained by (i) a Party at the federal level, as set out in its Schedule to Annex I or III [...]” (emphasis added), not to “any existing non-conforming legal regime.” Paragraph 2(f)(ii) of Annex I provides that authority and consistency are to be assessed by reference to the “the measure”, not to a “legal framework”. There is a world of difference between “any measure [...] set out in [...] Schedule I” or “the measure”, on the one hand, and a “legal framework,” on the other.

29. For this reason I am unable to agree with the Majority’s conclusion that the words “the measure” should encompass the totality of a “legal framework” that applies to a project at the moment before a new subordinate measure is adopted.<sup>28</sup> The words “the measure” as used in Article 1108(1)(c) plainly do not mean the totality of the “legal framework” when used by reference to an amendment. I disagree too with the Majority’s view that purports to derive support for its conclusion from a part of the United States’ first submission, which it says “suggests that consideration is needed of both the reserved non-conforming measure and subsequent subordinate measures and it does not limit the subordinate measures that are covered by this provision.”<sup>29</sup> The United States and Mexico were invited to express a view on the point in issue, and both declined to accede to the invitation. Mexico concludes that the issue of ‘consistency’ is governed exclusively by Canadian law.<sup>30</sup> Since the Majority accepts that the Canadian courts ruled that the 2004 Guidelines were applied lawfully to the Projects, the

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<sup>27</sup> NAFTA, Annex VII, Schedule of Mexico, Section B, point 17.

<sup>28</sup> The conclusion also suffers from selectivity and inconsistency, since the Majority does not apply its interpretation of the words ‘the measure’ in Article 1108(1)(a) to the same words when they are used in Article 1108(1)(c).

<sup>29</sup> Award, para. 308.

<sup>30</sup> Mex. 2<sup>nd</sup> Art. 1128, para. 3.

position adopted by the Majority cannot derive any support from Mexico. None of the three NAFTA Parties has expressed views that support the Majority's approach. Whilst not dispositive, that ought to set alarm bells ringing.

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30. I turn to other concerns. In my view, the Majority's approach is not consistent with the requirements applicable to the interpretation of treaties, as reflected in the VCLT.<sup>31</sup> Moreover, it has consequences that give rise to complexities, uncertainties and other difficulties.

31. Article 1108(1) of the NAFTA must be interpreted "in good faith in accordance with the ordinary meaning to be given to the terms of the [NAFTA] in [its] context and in the light of [the NAFTA's] object and purpose."<sup>32</sup> Under the VCLT the "ordinary meaning" of words are given a premium. An initial difficulty with the approach taken by the Majority is that it is not premised on the ordinary meaning of the words "the measure". Article 1108(1) provides that Article 1106 does not apply *inter alia* to: "(a) any existing non-conforming measure that is maintained by (i) a Party at the federal level, as set out in its Schedule to Annex I." The words "any existing non-conforming measure" refer to a measure in the singular, not in the plural. It is also apparent that the "measure" must have been "set out in [Canada's] Schedule to Annex I." The Federal Accord Act is set out in Canada's Schedule to Annex I, but none of the existing subsidiary measures (such as Decision 86.01 and Decision 97.02) are there set out. It follows that the ordinary meaning of the words "the measure" in Article 1108(1) (and, in my view, the only plausible meaning that avoids an endless and unhappy circularity of reasoning) is the measure listed by the Party. In this case that measure is the Federal Accord Act, and the Federal Accord Act alone.

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<sup>31</sup> See Articles 31 and 32.

<sup>32</sup> See Article 31(1) VCLT.

32. Against this ordinary meaning, I recognise that paragraph 2(f)(ii) of Annex I introduces a hint of uncertainty, by stating that the term “measure (...) includes any subordinate measure adopted or maintained under the authority of and consistent with the measure.” The Majority pins its conclusion on this definitional language to conclude that the words “the measure” in Article 1108(1)(a) (but not 1108(1)(c)) mean not only the Federal Accord Act, but also the earlier subordinate measures (the 1987 Guidelines and Decisions 86.01 and 97.02). The approach might seem to be superficially attractive for its simplicity. However, it ignores the context in which the words “the measure” appear in Article 1108(1)(c) and paragraph 2(f)(ii) of Annex I, as well as the object and purpose of the NAFTA.
33. The more plausible object of paragraph 2(f)(ii) of Annex I is to achieve a limited interpretative effect that ensures, for the avoidance of doubt, that any listed reserved measure that benefits from the reservation also “includes any subordinate measure adopted or maintained under the authority of and consistent with the measure.” Without paragraph 2(f)(ii), it might be concluded that it is only the listed reserved measure that benefits from the reservation, and not also any subordinate measure that is adopted under the authority of and consistent with that listed measure. The Majority concludes that paragraph 2(f)(ii) – which is only found in an interpretative annex - has the significant additional effect of imposing upon each NAFTA Party the obligation to ensure that a new subordinate measure is further and additionally consistent with certain existing subordinate measures. I use the word “certain”, because it is not immediately apparent from the Majority’s approach when an existing subordinate measure is to be taken into account for the assessment of ‘consistency’: at paragraph 391 of the Award the standard applied by the Majority is whether an existing subordinate measure was “previously applied” to the project in question. The Majority once again provides no explanation of the basis for this conclusion. There is nothing in the NAFTA or the Interpretative Note that references such a standard.

34. I have already referred to a further difficulty with the Majority's approach, namely that the relevant section of paragraph 2(f)(ii) of Annex I requires not only that a new subordinate measure must be "consistent with" the measure, but that it must also be adopted "under the authority of the [...] measure." The ordinary meaning of the text is that the authority and consistency of a subordinate measure is to be assessed by reference to the same standard: that is also confirmed by the context of paragraph 2(f)(ii). The point was made by Canada:

"the determination of whether a challenged measure is consistent with "the measure" is part of an overall determination whether the challenged measure is subordinate to "the measure." The meaning of "consistent with" is thus informed by the requirement that the challenged measure is under the authority of the listed measure. The requirement of "consistency" cannot be removed and applied in isolation."<sup>33</sup>

The approach adopted by the Majority is not compelling.

35. There is a third, practical difficulty with the approach adopted by the Majority, beyond the apparent circularity of the logic on which its conclusion is premised.<sup>34</sup> The approach necessarily leads to the result that the identification of "the measure" by reference to which an assessment as to "authority" and "consistency" is to be made, will not be to a constant or fixed point (subject to any formal amendment of the listed measure): "authority" and "consistency" are to be assessed by reference to a continually evolving standard, as new subsidiary measures are adopted, whereby "the measure" by which authority and consistency are assessed incorporates any new "subordinate measure" (whether existing as at 1994 or new) that meets the requirements of "authority" and "consistency". In this way, the assessment of "authority" and "consistency" of an earlier set of guidelines (or the Benefits Plans reflected in Decisions 86.01 and 97.02) and the 2004 Guidelines would fall to be assessed by reference to different standards: the former would only have to be consistent with the Federal Accord Act, but the

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<sup>33</sup> Respondent's Response to Tribunal's Letter of June 23, 2011, para. 19 (August 2, 2011).

<sup>34</sup> See Respondent's Reply to Claimants' Response to Tribunal's Letter of June 23, 2011, para. 9 (August 26, 2011).

latter would have to be consistent with the Federal Accord Act and the 1987 Guidelines, as well as any other prior “subordinate measures” that had already been determined to be consistent.

36. Over time it is inevitable that this will give rise to significant practical difficulties: since there is no NAFTA requirement that subordinate measures must be published (NAFTA Parties are only required to set out in their Annex I Schedule “the measure” that was reserved as at 1994), how is an investor to ascertain the standard for determining “authority” and “consistency”? This raises transparency issues: if the NAFTA Parties had intended that the standard by which “authority” and “consistency” is to be assessed evolves and changes each and every time a new subordinate measure is adopted, one assumes that they might have adopted a provision requiring a “new subordinate measure” to be duly “set out”. The fact that they have not imposed such a requirement supports the conclusion that “the measure” referred to in Article 1108(1) is limited to the measure that is set out in Annex I. The Majority is silent on transparency, despite the fact that it is “one of the key objectives of the NAFTA,” as reflected in Article 102.<sup>35</sup> The Majority accepts that its approach “implies an evolving legal and regulatory framework,” but has nothing to say about the practical and other difficulties that will follow from the approach it has adopted.<sup>36</sup>

37. A fourth difficulty arises with that approach: it has the effect of elevating the status of “subordinate measures”, giving them the same quality and effect as acts of primary legislation (such as the Federal Accord Act and other reserved measures listed by the NAFTA Parties). The scheme for reservations established by the NAFTA allowed the Parties a single opportunity to list a reservation. That reservation could then be amended, so long as the amendment did not decrease conformity with the NAFTA. In addition, a NAFTA Party was free in the future to adopt a new subordinate measure under the reserved measure, provided that it

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<sup>35</sup> U.S. 2<sup>nd</sup> Art. 1128, para. 8.

<sup>36</sup> Award, para. 332.

was under the authority of and consistent with the reserved measure. In this way, the reserved measure set a ceiling, and that ceiling remained in place indefinitely, unless it was subject to a commitment to liberalise over time, in accordance with a specified phase out (the reservation in relation to the Federal Accord Act is not subject to any such phase out, and Canada is entitled to rely upon it in perpetuity). The approach adopted by the Majority rewrites this regulatory approach: it means that every time a NAFTA Party adopts a new subordinate measure that is under the authority of and consistent with a reserved measure, it in effect lowers the ceiling, by constraining the right of a NAFTA Party to adopt (for an entity that is subject to the earlier subordinate measure) only such new subordinate measure that is “consistent with” the listed reserved measure as well as with every other applicable (or “previously applied,” to take the Majority’s approach) subordinate measure. The consequences of such an approach are far-reaching. It is not an approach that the drafters of the NAFTA expressly agreed to, and it seems most unlikely that they could have done so inadvertently, given the matters addressed by the reservations and the implications. If correct, it means that once a NAFTA Party has adopted a subordinate measure, it fetters its ability to adopt a new subordinate measure in relation to any activity to which that earlier subordinate measure is applicable.

38. In seeking to point out the consequences, the response of the Majority is to say that it is not appropriate to “examine how this interpretation would apply to the operation of specific laws that are not in dispute before us”<sup>37</sup> (although elsewhere the Majority seems content to “envision other factual circumstances”<sup>38</sup> beyond the present case). There is ample international authority to support the principle that it is indeed appropriate and useful to consider the “result” of a particular interpretation for the implementation of an international agreement more generally, including before the International Court of Justice.<sup>39</sup> Surely

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<sup>37</sup> Award, para. 336.

<sup>38</sup> Award, para. 324.

<sup>39</sup> See e.g. *Application of the Interim Accord of 13 September 1995 (The Former Yugoslav Republic of Macedonia v. Greece)*, International Court of Justice, Judgment of December 5, 2011, para. 36.

international arbitrators cannot be required to ignore the consequences for the NAFTA, more generally, of the approach they decide to adopt?

39. The point may be illustrated by reference to a measure reserved by another NAFTA Party, which is not in issue in this case but which was the subject of illustrative argument by the Claimants in the proceedings (and this is the only reason it is here taken as an example).<sup>40</sup> The United States Schedule to Annex I includes the *Atomic Energy Act of 1954* (42 U.S.C. §§ 2011 *et seq.*) Between 1954 and 1994 the United States adopted a number of subordinate measures under the *Atomic Energy Act of 1954*. Adopted before 1994, these are existing subordinate measures. Between 1994 and 2010 the United States has adopted further subordinate measures under the *Atomic Energy Act of 1954*. These are new subordinate measures. On the approach of the Majority, it would appear that every new subordinate measure adopted since 1994 that is applicable to a particular activity would be subject to the requirement that it must be under the authority of and consistent with every previous subordinate measure that had already been adopted and was applicable to that activity. The point only needs to be stated for the far-reaching consequences of the proposition to become clear. Given the care with which the NAFTA was drafted, it is unlikely that the NAFTA Parties might have unwittingly stumbled into a set of rules that fettered their right to adopt a new subordinate measure in this way.

40. Finally, there is a fifth difficulty that flows from the Majority's approach: will a new subordinate measure that is consistent with the listed reserved measure (as the 2004 Guidelines are with the Federal Accord Act) apply to a new project to which the existing subordinate measures do not apply (e.g. because they are not subject to the 1987 Guidelines or Decision 86.01 or Decision 97.02), whilst not being applied to an existing project subject to an existing subordinate measure? The matter is left entirely open, notwithstanding Article 1101(1)(c) of the

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<sup>40</sup> Cl. Response 1<sup>st</sup> Art. 1128, para. 31.

NAFTA.<sup>41</sup> If a new subordinate measure, for example a new Benefits Plan applied to a new investor, can give effect to the 2004 Guidelines, then the consequence is that there would be no level playing field in the application of subordinate measures, as between new and old projects. This appears to be the position adopted by the Claimants:

“Although the Terra Nova Benefits Plan was not submitted or approved until after the NAFTA went into effect, Canada’s Annex I reservation for the Federal Accord Act permitted the Board to implement its Section 45 requirement to provide for R&D and E&T in a benefits plan.”<sup>42</sup>

The Claimants elaborated on this in a later submission stating that

“Claimants have at no point in this arbitration ever suggested that the Board’s decision adopting the Terra Nova Benefits Plan violates the NAFTA.”<sup>43</sup>

Is there any indication in the text of the NAFTA that a discrimination of this kind might be permitted, in relation to the rules governing the application of a reservation? I am unable to find any such indication. I find it difficult to understand on what basis it can properly be concluded, on the approach taken by the Majority, that some projects will be subject to the 2004 Guidelines and others will not. In this way, an existing US or Mexican investor might be able to argue that it should not be subject to the 2004 Guidelines because of an earlier Benefits Plan that predates those Guidelines, but a new US or Mexican investor to which an earlier Benefits Plan was not “previously applied” could not do so, and would be fully subject to the 2004 Guidelines. This would give rise to an obvious potential discrimination, as between existing and new US or Mexican entities investing in the same kinds of projects. Such a result would appear to be difficult to justify, whether by reason of law, policy or logic, and it is difficult to see how the approach may be said to advance the purposes of the NAFTA. Against that, if

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<sup>41</sup> Article 1101(1)(c) provides that: “This Chapter applies to measures adopted or maintained by a Party relating to: (...) (c) with respect to Articles 1106 and 1114, all investments in the territory of the Party.” It was touched upon briefly in the pleadings, *see e.g.* Claimants’ Memorial, para. 137, but not fully argued or addressed.

<sup>42</sup> Cl. Reply, fn. 8.

<sup>43</sup> Cl. Response 1<sup>st</sup> Art. 1128, para. 30.

Article 1101(1)(c) somehow cuts in to create a level playing field - an approach that was not argued by the parties and on which the Majority expresses no view - then the effect of the Majority's expansive interpretation of the words "the measure" would be to cause the adoption of a subordinate measure in relation to one investment, to have significant constraining effects on a NAFTA Party in relation to future investments in the same domain but not governed by the existing subordinate measure. Either consequence raises the most serious concerns, reinforcing the view that the Majority has fallen into error.

41. The consequences of the interpretation adopted by the Majority are therefore highly problematic. In my view, the difficulties identified for this case, for specific sectors and for the NAFTA system as a whole, point clearly to the conclusion that Article 1108(1) means that the authority and consistency of a "new subordinate measure" is to be assessed exclusively by reference to the "existing non-conforming measure that is maintained by [the Respondent] at the federal level, as set out in its Schedule to Annex I." For this reason, I conclude without difficulty or hesitation that the 2004 Guidelines are covered by Canada's reservation in relation to the Atlantic Accord, and they may be applied to these Projects as to others.

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42. Given my conclusions on the merits, it follows that the question of damages does not arise. I therefore dissent from the findings of the Majority on the subject of damages, as set out at paragraphs 407-482. The subject is not without its complexities, with which the Majority has sought to grapple in a fair and balanced manner. The Claimants and the Respondent, and perhaps also the other NAFTA Parties and even other investors, will no doubt reflect on the consequences of the findings of the Majority, having regard *inter alia* to Article 1101(1)(c) of the NAFTA.<sup>44</sup> I note the curiosity of a situation in which the level of compensation to

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<sup>44</sup> See *supra*. fn. 41.

be paid, assuming it to arise, falls to be assessed by reference to the difference between the amount the Claimants say they would have spent on R&D and E&T under the existing Benefits Plans (by unilateral self-determination), on the one hand, and the amounts required to be paid under the 2004 Guidelines, on the other. This may be a rare case in which a claimant is given such a role in contributing in this way to the assessment of the level of damages that it might in future be able to claim.

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43. There remains a final point that requires a brief comment. Whilst accepting that the new approach set forth in the 2004 Guidelines is “consistent with” the Federal Accord Act, the Majority nevertheless expresses discomfort with the consequences of the application of the 2004 Guidelines, variously described as imposing “additional burdens” on the projects, or a “fundamentally different approach to compliance,” or measures that “alter the regime in a fundamental manner.”<sup>45</sup> The Claimants have a legitimate interest, in the fullest respect, of being accorded their rights under Chapter XI of the NAFTA. What happened in this case? In short, the 1987 Guidelines and Decisions 86.01 and 97.02 created an auto-determining system, in which the project sponsors could effectively set in broad terms the amounts they would spend on R&D and E&T in the Province. Initially the payments were quite significant, but over the years they dropped off very significantly, as reflected in footnotes 31, 51 and 52, so that the benefits received by the Province dropped. This is apparently what caused the Board to review the guidelines and, eventually, adopt the new 2004 Guidelines. With these Guidelines, the payments to be made by the projects under the Benefits Plans returned to the amounts of earlier levels. They were also extended to the production phase, a change that the Majority accepts to be consistent with the Federal Accord Act and, more curiously, the existing subordinate measures.<sup>46</sup> Can it be said that the approach in the 2004 Guidelines was precluded by the earlier

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<sup>45</sup> Award, paras. 387, 402, 403.

<sup>46</sup> Award, para. 392.

guidelines and Decision 86.01 and 97.02? In my view, no. Neither Decision precluded the possibility of change. Decision 86.01 noted that the “development and implementation of a benefits plan is, because of the nature of the subject matter, an evolutionary process,”<sup>47</sup> and recording the Board’s “expectation” that the project sponsor’s responsiveness to issues of concern “will continue through the duration of the project.”<sup>48</sup> The monitoring system was the means to review the level and extent of payments. There is no undertaking not to replace Decision 86.01 if the project sponsor is not responsive. When difficulties did arise, the Benefits Plan was changed to put in place new arrangements that would provide for more regular payments. In relation to Article 1106 and 1108, the Claimants had the right to ensure that any new Benefits Plan was under the authority of and consistent with the Federal Accord Act. In my view it plainly was, as the Majority also accepts, and that is the end of the matter.

Philippe Sands

17 May 2012

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<sup>47</sup> CE-47, Board Decision 86.01, para. 2.1.

<sup>48</sup> *Id.*