CENTRE FOR INTERNATIONAL LAW

Global and Number One v. Republic of Anchuria

Reference Materials for

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Contents

WHO FRAMEWORK CONVENTION ON TOBACCO CONTROL

FCTC

WHO FRAMEWORK CONVENTION
ON TOBACCO CONTROL

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Preamble

The Parties to this Convention,

Determined to give priority to their right to protect public health,

Recognizing that the spread of the tobacco epidemic is a global problem with serious consequences for public health that calls for the widest possible international cooperation and the participation of all countries in an effective, appropriate and comprehensive international response,

Reflecting the concern of the international community about the devastating worldwide health, social, economic and environmental consequences of tobacco consumption and exposure to tobacco smoke,

Seriously concerned about the increase in the worldwide consumption and production of cigarettes and other tobacco products, particularly in developing countries, as well as about the burden this places on families, on the poor, and on national health systems,

Recognizing that scientific evidence has unequivocally established that tobacco consumption and exposure to tobacco smoke cause death, disease and disability, and that there is a time lag between the exposure to smoking and the other uses of tobacco products and the onset of tobacco-related diseases,

Recognizing also that cigarettes and some other products containing tobacco are highly engineered so as to create and maintain dependence, and that many of the compounds they contain and the smoke they produce are pharmacologically active, toxic, mutagenic and carcinogenic, and that tobacco dependence is separately classified as a disorder in major international classifications of diseases,

Acknowledging that there is clear scientific evidence that prenatal exposure to tobacco smoke causes adverse health and developmental conditions for children,

Deeply concerned about the escalation in smoking and other forms of tobacco consumption by children and adolescents worldwide, particularly smoking at increasingly early ages,

Alarmed by the increase in smoking and other forms of tobacco consumption by women and young girls worldwide and keeping in mind the need for full participation of women at all levels of policy-making and implementation and the need for gender-specific tobacco control strategies,

Deeply concerned about the high levels of smoking and other forms of tobacco consumption by indigenous peoples,

Seriously concerned about the impact of all forms of advertising, promotion and sponsorship aimed at encouraging the use of tobacco products,

Recognizing that cooperative action is necessary to eliminate all forms of illicit trade in cigarettes and other tobacco products, including smuggling, illicit manufacturing and counterfeiting,

Acknowledging that tobacco control at all levels and particularly in developing countries and in countries with economies in transition requires sufficient financial and technical resources commensurate with the current and projected need for tobacco control activities,

Recognizing the need to develop appropriate mechanisms to address the long-term social and economic implications of successful tobacco demand reduction strategies,

Mindful of the social and economic difficulties that tobacco control programmes may engender in the medium and long term in some developing countries and countries with economies in transition, and recognizing their need for technical and financial assistance in the context of nationally developed strategies for sustainable development,

Conscious of the valuable work being conducted by many States on tobacco control and commending the leadership of the World Health Organization as well as the efforts of other organizations and bodies of the United Nations system and other international and regional intergovernmental organizations in developing measures on tobacco control,

Emphasizing the special contribution of nongovernmental organizations and other members of civil society not affiliated with the tobacco industry, including health professional bodies, women's, youth, environmental and consumer groups, and academic and health care institutions, to tobacco control efforts nationally and internationally and the vital importance of their participation in national and international tobacco control efforts,

Recognizing the need to be alert to any efforts by the tobacco industry to undermine or subvert tobacco control efforts and the need to be informed of activities of the tobacco industry that have a negative impact on tobacco control efforts,

Recalling Article 12 of the International Covenant on Economic, Social and Cultural Rights, adopted by the United Nations General Assembly on 16 December 1966, which states that it is the right of everyone to the enjoyment of the highest attainable standard of physical and mental health,

Recalling also the preamble to the Constitution of the World Health Organization, which states that the enjoyment of the highest attainable standard of health is one of the fundamental rights of every human being without distinction of race, religion, political belief, economic or social condition,

Determined to promote measures of tobacco control based on current and relevant scientific, technical and economic considerations,

Recalling that the Convention on the Elimination of All Forms of Discrimination against Women, adopted by the United Nations General Assembly on 18 December 1979, provides that States Parties to that Convention shall take appropriate measures to eliminate discrimination against women in the field of health care,

Recalling further that the Convention on the Rights of the Child, adopted by the United Nations General Assembly on 20 November 1989, provides that States Parties to that Convention recognize the right of the child to the enjoyment of the highest attainable standard of health,

Have agreed, as follows:

PART I: INTRODUCTION

Article 1
Use of terms

For the purposes of this Convention:

(a) "illicit trade" means any practice or conduct prohibited by law and which relates to production, shipment, receipt, possession, distribution, sale or purchase including any practice or conduct intended to facilitate such activity;

(b) "regional economic integration organization" means an organization that is composed of several sovereign states, and to which its Member States have transferred competence over a range of matters, including the authority to make decisions binding on its Member States in respect of those matters;[1]

(c) "tobacco advertising and promotion" means any form of commercial communication, recommendation or action with the aim, effect or likely effect of promoting a tobacco product or tobacco use either directly or indirectly;

(d) "tobacco control" means a range of supply, demand and harm reduction strategies that aim to improve the health of a population by eliminating or reducing their consumption of tobacco products and exposure to tobacco smoke;

(e) "tobacco industry" means tobacco manufacturers, wholesale distributors and importers of tobacco products;

(f) "tobacco products" means products entirely or partly made of the leaf tobacco as raw material which are manufactured to be used for smoking, sucking, chewing or snuffing;

(g) "tobacco sponsorship" means any form of contribution to any event, activity or individual with the aim, effect or likely effect of promoting a tobacco product or tobacco use either directly or indirectly;

[1] Where appropriate, national will refer equally to regional economic integration organizations.

Article 2
Relationship between this Convention and other agreements and legal instruments

1. In order to better protect human health, Parties are encouraged to implement measures beyond those required by this Convention and its protocols, and nothing in these instruments shall prevent a Party from imposing stricter requirements that are consistent with their provisions and are in accordance with international law.

2. The provisions of the Convention and its protocols shall in no way affect the right of Parties to enter into bilateral or multilateral agreements, including regional or subregional agreements, on issues relevant or additional to the Convention and its protocols, provided that such agreements are compatible with their obligations under the Convention and its protocols. The Parties concerned shall communicate such agreements to the Conference of the Parties through the Secretariat.

PART II: OBJECTIVE, GUIDING PRINCIPLES AND GENERAL OBLIGATIONS

Article 3
Objective

The objective of this Convention and its protocols is to protect present and future generations from the devastating health, social, environmental and economic consequences of tobacco consumption and exposure to tobacco smoke by providing a framework for tobacco control measures to be implemented by the Parties at the national, regional and international levels in order to reduce continually and substantially the prevalence of tobacco use and exposure to tobacco smoke.

Article 4
Guiding principles

To achieve the objective of this Convention and its protocols and to implement its provisions, the Parties shall be guided, *inter alia*, by the principles set out below:

1. Every person should be informed of the health consequences, addictive nature and mortal threat posed by tobacco consumption and exposure to tobacco smoke and effective legislative, executive, administrative or other measures should be contemplated at the appropriate governmental level to protect all persons from exposure to tobacco smoke.

2. Strong political commitment is necessary to develop and support, at the national, regional and international levels, comprehensive multisectoral measures and coordinated responses, taking into consideration:

(a) the need to take measures to protect all persons from exposure to tobacco smoke;

(b) the need to take measures to prevent the initiation, to promote and support cessation, and to decrease the consumption of tobacco products in any form;

(c) the need to take measures to promote the participation of indigenous individuals and communities in the development, implementation and evaluation of tobacco control programmes that are socially and culturally appropriate to their needs and perspectives; and

(d) the need to take measures to address gender-specific risks when developing tobacco control strategies.

3. International cooperation, particularly transfer of technology, knowledge and financial assistance and provision of related expertise, to establish and implement effective tobacco control programmes, taking into consideration local culture, as well as social, economic, political and legal factors, is an important part of the Convention.

4. Comprehensive multisectoral measures and responses to reduce consumption of all tobacco products at the national, regional and international levels are essential so as to prevent, in accordance with public health principles, the incidence of diseases, premature disability and mortality due to tobacco consumption and exposure to tobacco smoke.

5. Issues relating to liability, as determined by each Party within its jurisdiction, are an important part of comprehensive tobacco control.

6. The importance of technical and financial assistance to aid the economic transition of tobacco growers and workers whose livelihoods are seriously affected as a consequence of tobacco control programmes in developing country Parties, as well as Parties with economies in transition, should be recognized and addressed in the context of nationally developed strategies for sustainable development.

7. The participation of civil society is essential in achieving the objective of the Convention and its protocols.

Article 5
General obligations

1. Each Party shall develop, implement, periodically update and review comprehensive multisectoral national tobacco control strategies, plans and programmes in accordance with this Convention and the protocols to which it is a Party.

2. Towards this end, each Party shall, in accordance with its capabilities:

(a) establish or reinforce and finance a national coordinating mechanism or focal points for tobacco control; and

(b) adopt and implement effective legislative, executive, administrative and/or other measures and cooperate, as appropriate, with other Parties in developing appropriate policies for preventing and reducing tobacco consumption, nicotine addiction and exposure to tobacco smoke.

3. In setting and implementing their public health policies with respect to tobacco control, Parties shall act to protect these policies from commercial and other vested interests of the tobacco industry in accordance with national law.

4. The Parties shall cooperate in the formulation of proposed measures, procedures and guidelines for the implementation of the Convention and the protocols to which they are Parties.

5. The Parties shall cooperate, as appropriate, with competent international and regional intergovernmental organizations and other bodies to achieve the objectives of the Convention and the protocols to which they are Parties.

6. The Parties shall, within means and resources at their disposal, cooperate to raise financial resources for effective implementation of the Convention through bilateral and multilateral funding mechanisms.

PART III: MEASURES RELATING TO THE REDUCTION OF DEMAND FOR TOBACCO

Article 6
Price and tax measures to reduce the demand for tobacco

1. The Parties recognize that price and tax measures are an effective and important means of reducing tobacco consumption by various segments of the population, in particular young persons.

2. Without prejudice to the sovereign right of the Parties to determine and establish their taxation policies, each Party should take account of its national health objectives concerning tobacco control and adopt or maintain, as appropriate, measures which may include:

(a) implementing tax policies and, where appropriate, price policies, on tobacco products so as to contribute to the health objectives aimed at reducing tobacco consumption; and

(b) prohibiting or restricting, as appropriate, sales to and/or importations by international travellers of tax- and duty-free tobacco products.

3. The Parties shall provide rates of taxation for tobacco products and trends in tobacco consumption in their periodic reports to the Conference of the Parties, in accordance with Article 21.

Article 7

Non-price measures to reduce the demand for tobacco

The Parties recognize that comprehensive non-price measures are an effective and important means of reducing tobacco consumption. Each Party shall adopt and implement effective legislative, executive, administrative or other measures necessary to implement its obligations pursuant to Articles 8 to 13 and shall cooperate, as appropriate, with each other directly or through competent international bodies with a view to their implementation. The Conference of the Parties shall propose appropriate guidelines for the implementation of the provisions of these Articles.

Article 8

Protection from exposure to tobacco smoke

1. Parties recognize that scientific evidence has unequivocally established that exposure to tobacco smoke causes death, disease and disability.

2. Each Party shall adopt and implement in areas of existing national jurisdiction as determined by national law and actively promote at other jurisdictional levels the adoption and implementation of effective legislative, executive, administrative and/or other measures, providing for protection from exposure to tobacco smoke in indoor workplaces, public transport, indoor public places and, as appropriate, other public places.

Article 9
Regulation of the contents of tobacco products

The Conference of the Parties, in consultation with competent international bodies, shall propose guidelines for testing and measuring the contents and emissions of tobacco products, and for the regulation of these contents and emissions. Each Party shall, where approved by competent national authorities, adopt and implement effective legislative, executive and administrative or other measures for such testing and measuring, and for such regulation.

Article 10
Regulation of tobacco product disclosures

Each Party shall, in accordance with its national law, adopt and implement effective legislative, executive, administrative or other measures requiring manufacturers and importers of tobacco products to disclose to governmental authorities information about the contents and emissions of tobacco products. Each Party shall further adopt and implement effective measures for public disclosure of information about the toxic constituents of the tobacco products and the emissions that they may produce.

Article 11
Packaging and labelling of tobacco products

1. Each Party shall, within a period of three years after entry into force of this Convention for that Party, adopt and implement, in accordance with its national law, effective measures to ensure that:

(a) tobacco product packaging and labelling do not promote a tobacco product by any means that are false, misleading, deceptive or likely to create an erroneous impression about its characteristics, health effects, hazards or emissions, including any term, descriptor, trademark, figurative or any other sign that directly or indirectly creates the false impression that a particular tobacco product is less harmful than other tobacco products. These may include terms such as “low tar”, “light”, “ultra-light”, or “mild”; and

(b) each unit packet and package of tobacco products and any outside packaging and labelling of such products also carry health warnings describing the harmful effects of tobacco use, and may include other appropriate messages. These warnings and messages:

(i) shall be approved by the competent national authority,

(ii) shall be rotating,

(iii) shall be large, clear, visible and legible,

(iv) should be 50% or more of the principal display areas but shall be no less than 30% of the principal display areas,

(v) may be in the form of or include pictures or pictograms.

2. Each unit packet and package of tobacco products and any outside packaging and labelling of such products shall, in addition to the warnings specified in paragraph 1(b) of this Article, contain information on relevant constituents and emissions of tobacco products as defined by national authorities.

3. Each Party shall require that the warnings and other textual information specified in paragraphs 1(b) and paragraph 2 of this Article will appear on each unit packet and package of tobacco products and any outside packaging and labelling of such products in its principal language or languages.

4. For the purposes of this Article, the term "outside packaging and labelling" in relation to tobacco products applies to any packaging and labelling used in the retail sale of the product.

Article 12

Education, communication, training and public awareness

Each Party shall promote and strengthen public awareness of tobacco control issues, using all available communication tools, as appropriate. Towards this end, each Party shall adopt and implement effective legislative, executive, administrative or other measures to promote:

(a) broad access to effective and comprehensive educational and public awareness programmes on the health risks including the addictive characteristics of tobacco consumption and exposure to tobacco smoke;

(b) public awareness about the health risks of tobacco consumption and exposure to tobacco smoke, and about the benefits of the cessation of tobacco use and tobacco-free lifestyles as specified in Article 14.2;

(c) public access, in accordance with national law, to a wide range of information on the tobacco industry as relevant to the objective of this Convention;

(d) effective and appropriate training or sensitization and awareness programmes on tobacco control addressed to persons such as health workers, community workers, social workers, media professionals, educators, decision-makers, administrators and other concerned persons;

(e) awareness and participation of public and private agencies and nongovernmental organizations not affiliated with the tobacco industry in developing and implementing intersectoral programmes and strategies for tobacco control; and

(f) public awareness of and access to information regarding the adverse health, economic, and environmental consequences of tobacco production and consumption.

Article 13

Tobacco advertising, promotion and sponsorship

1. Parties recognize that a comprehensive ban on advertising, promotion and sponsorship would reduce the consumption of tobacco products.

2. Each Party shall, in accordance with its constitution or constitutional principles, undertake a comprehensive ban of all tobacco advertising, promotion and sponsorship. This shall include, subject to the legal environment and technical means available to that Party, a comprehensive ban on cross-border advertising, promotion and sponsorship originating from its territory. In this respect, within the period of five years after entry into force of this Convention for that Party, each Party shall undertake appropriate legislative, executive, administrative and/or other measures and report accordingly in conformity with Article 21.

3. A Party that is not in a position to undertake a comprehensive ban due to its constitution or constitutional principles shall apply restrictions on all tobacco advertising, promotion and sponsorship. This shall include, subject to the legal environment and technical means available to that Party, restrictions or a comprehensive ban on advertising, promotion and sponsorship originating from its territory with cross-border effects. In this respect, each Party shall undertake appropriate legislative, executive, administrative and/or other measures and report accordingly in conformity with Article 21.

4. As a minimum, and in accordance with its constitution or constitutional principles, each Party shall:

(a) prohibit all forms of tobacco advertising, promotion and sponsorship that promote a tobacco product by any means that are false, misleading or deceptive or likely to create an erroneous impression about its characteristics, health effects, hazards or emissions;

(b) require that health or other appropriate warnings or messages accompany all tobacco advertising and, as appropriate, promotion and sponsorship;

(c) restrict the use of direct or indirect incentives that encourage the purchase of tobacco products by the public;

(d) require, if it does not have a comprehensive ban, the disclosure to relevant governmental authorities of expenditures by the tobacco industry on advertising, promotion and sponsorship not yet prohibited. Those authorities may decide to make those figures available, subject to national law, to the public and to the Conference of the Parties, pursuant to Article 21;

(e) undertake a comprehensive ban or, in the case of a Party that is not in a position to undertake a comprehensive ban due to its constitution or constitutional principles, restrict tobacco advertising, promotion and sponsorship on radio, television, print media and, as appropriate, other media, such as the internet, within a period of five years; and

(f) prohibit, or in the case of a Party that is not in a position to prohibit due to its constitution or constitutional principles restrict, tobacco sponsorship of international events, activities and/or participants therein.

5. Parties are encouraged to implement measures beyond the obligations set out in paragraph 4.

6. Parties shall cooperate in the development of technologies and other means necessary to facilitate the elimination of cross-border advertising.

7. Parties which have a ban on certain forms of tobacco advertising, promotion and sponsorship have the sovereign right to ban those forms of cross-border tobacco advertising, promotion and sponsorship entering their territory and to impose equal penalties as those applicable to domestic advertising, promotion and sponsorship originating from their territory in accordance with their national law. This paragraph does not endorse or approve of any particular penalty.

8. Parties shall consider the elaboration of a protocol setting out appropriate measures that require international collaboration for a comprehensive ban on cross-border advertising, promotion and sponsorship.

Article 14

Demand reduction measures concerning tobacco dependence and cessation

1. Each Party shall develop and disseminate appropriate, comprehensive and integrated guidelines based on scientific evidence and best practices, taking into account national circumstances and priorities, and shall take effective measures to promote cessation of tobacco use and adequate treatment for tobacco dependence.

2. Towards this end, each Party shall endeavour to:

(a) design and implement effective programmes aimed at promoting the cessation of tobacco use, in such locations as educational institutions, health care facilities, workplaces and sporting environments;

(b) include diagnosis and treatment of tobacco dependence and counselling services on cessation of tobacco use in national health and education programmes, plans and strategies, with the participation of health workers, community workers and social workers as appropriate;

(c) establish in health care facilities and rehabilitation centres programmes for diagnosing, counselling, preventing and treating tobacco dependence; and

(d) collaborate with other Parties to facilitate accessibility and affordability for treatment of tobacco dependence including pharmaceutical products pursuant to Article 22. Such products and their constituents may include medicines, products used to administer medicines and diagnostics when appropriate.

PART IV: MEASURES RELATING TO THE REDUCTION OF THE SUPPLY OF TOBACCO

Article 15

Illicit trade in tobacco products

1. The Parties recognize that the elimination of all forms of illicit trade in tobacco products, including smuggling, illicit manufacturing and counterfeiting, and the development and implementation of related national law, in addition to subregional, regional and global agreements, are essential components of tobacco control.

2. Each Party shall adopt and implement effective legislative, executive, administrative or other measures to ensure that all unit packets and packages of tobacco products and any outside packaging of such products are marked to assist Parties in determining the origin of

tobacco products, and in accordance with national law and relevant bilateral or multilateral agreements, assist Parties in determining the point of diversion and monitor, document and control the movement of tobacco products and their legal status. In addition, each Party shall:

(a) require that unit packets and packages of tobacco products for retail and wholesale use that are sold on its domestic market carry the statement: *"Sales only allowed in (insert name of the country, subnational, regional or federal unit)"* or carry any other effective marking indicating the final destination or which would assist authorities in determining whether the product is legally for sale on the domestic market; and

(b) consider, as appropriate, developing a practical tracking and tracing regime that would further secure the distribution system and assist in the investigation of illicit trade.

3. Each Party shall require that the packaging information or marking specified in paragraph 2 of this Article shall be presented in legible form and/or appear in its principal language or languages.

4. With a view to eliminating illicit trade in tobacco products, each Party shall:

(a) monitor and collect data on cross-border trade in tobacco products, including illicit trade, and exchange information among customs, tax and other authorities, as appropriate, and in accordance with national law and relevant applicable bilateral or multilateral agreements;

(b) enact or strengthen legislation, with appropriate penalties and remedies, against illicit trade in tobacco products, including counterfeit and contraband cigarettes;

(c) take appropriate steps to ensure that all confiscated manufacturing equipment, counterfeit and contraband cigarettes and other tobacco products are destroyed, using environmentally-friendly methods where feasible, or disposed of in accordance with national law;

(d) adopt and implement measures to monitor, document and control the storage and distribution of tobacco products held or moving under suspension of taxes or duties within its jurisdiction; and

(e) adopt measures as appropriate to enable the confiscation of proceeds derived from the illicit trade in tobacco products.

5. Information collected pursuant to subparagraphs 4(a) and 4(d) of this Article shall, as appropriate, be provided in aggregate form by the Parties in their periodic reports to the Conference of the Parties, in accordance with Article 21.

6. The Parties shall, as appropriate and in accordance with national law, promote cooperation between national agencies, as well as relevant regional and international intergovernmental organizations as it relates to investigations, prosecutions and proceedings, with a view to eliminating illicit trade in tobacco products. Special emphasis shall be placed on cooperation at regional and subregional levels to combat illicit trade of tobacco products.

7. Each Party shall endeavour to adopt and implement further measures including licensing, where appropriate, to control or regulate the production and distribution of tobacco products in order to prevent illicit trade.

Article 16
Sales to and by minors

1. Each Party shall adopt and implement effective legislative, executive, administrative or other measures at the appropriate government level to prohibit the sales of tobacco products to persons under the age set by domestic law, national law or eighteen. These measures may include:

(a) requiring that all sellers of tobacco products place a clear and prominent indicator inside their point of sale about the prohibition of tobacco sales to minors and, in case of doubt, request that each tobacco purchaser provide appropriate evidence of having reached full legal age;

(b) banning the sale of tobacco products in any manner by which they are directly accessible, such as store shelves;

(c) prohibiting the manufacture and sale of sweets, snacks, toys or any other objects in the form of tobacco products which appeal to minors; and

(d) ensuring that tobacco vending machines under its jurisdiction are not accessible to minors and do not promote the sale of tobacco products to minors.

2. Each Party shall prohibit or promote the prohibition of the distribution of free tobacco products to the public and especially minors.

3. Each Party shall endeavour to prohibit the sale of cigarettes individually or in small packets which increase the affordability of such products to minors.

4. The Parties recognize that in order to increase their effectiveness, measures to prevent tobacco product sales to minors should, where appropriate, be implemented in conjunction with other provisions contained in this Convention.

5. When signing, ratifying, accepting, approving or acceding to the Convention or at any time thereafter, a Party may, by means of a binding written declaration, indicate its commitment to prohibit the introduction of tobacco vending machines within its jurisdiction or, as appropriate, to a total ban on tobacco vending machines. The declaration made pursuant to this Article shall be circulated by the Depositary to all Parties to the Convention.

6. Each Party shall adopt and implement effective legislative, executive, administrative or other measures, including penalties against sellers and distributors, in order to ensure compliance with the obligations contained in paragraphs 1-5 of this Article.

7. Each Party should, as appropriate, adopt and implement effective legislative, executive, administrative or other measures to prohibit the sales of tobacco products by persons under the age set by domestic law, national law or eighteen.

Article 17

Provision of support for economically viable alternative activities

Parties shall, in cooperation with each other and with competent international and regional intergovernmental organizations, promote, as appropriate, economically viable alternatives for tobacco workers, growers and, as the case may be, individual sellers.

PART V: PROTECTION OF THE ENVIRONMENT

Article 18

Protection of the environment and the health of persons

In carrying out their obligations under this Convention, the Parties agree to have due regard to the protection of the environment and the health of persons in relation to the environment in respect of tobacco cultivation and manufacture within their respective territories.

PART VI: QUESTIONS RELATED TO LIABILITY

Article 19
Liability

1. For the purpose of tobacco control, the Parties shall consider taking legislative action or promoting their existing laws, where necessary, to deal with criminal and civil liability, including compensation where appropriate.

2. Parties shall cooperate with each other in exchanging information through the Conference of the Parties in accordance with Article 21 including:

(a) information on the health effects of the consumption of tobacco products and exposure to tobacco smoke in accordance with Article 20.3(a); and

(b) information on legislation and regulations in force as well as pertinent jurisprudence.

3. The Parties shall, as appropriate and mutually agreed, within the limits of national legislation, policies, legal practices and applicable existing treaty arrangements, afford one another assistance in legal proceedings relating to civil and criminal liability consistent with this Convention.

4. The Convention shall in no way affect or limit any rights of access of the Parties to each other's courts where such rights exist.

5. The Conference of the Parties may consider, if possible, at an early stage, taking account of the work being done in relevant international fora, issues related to liability including appropriate international approaches to these issues and appropriate means to support, upon request, the Parties in their legislative and other activities in accordance with this Article.

PART VII: SCIENTIFIC AND TECHNICAL COOPERATION AND COMMUNICATION OF INFORMATION

Article 20
Research, surveillance and exchange of information

1. The Parties undertake to develop and promote national research and to coordinate research programmes at the regional and international levels in the field of tobacco control. Towards this end, each Party shall:

Guidelines for implementation of Article 5.3 of the WHO Framework Convention on Tobacco Control

on the protection of public health policies with respect to tobacco control from commercial and other vested interests of the tobacco industry

INTRODUCTION

1. World Health Assembly resolution WHA54.18 on transparency in tobacco control process, citing the findings of the Committee of Experts on Tobacco Industry Documents, states that "the tobacco industry has operated for years with the express intention of subverting the role of governments and of WHO in implementing public health policies to combat the tobacco epidemic".

2. The Preamble of the WHO Framework Convention on Tobacco Control recognized the Parties'[1] "need to be alert to any efforts by the tobacco industry to undermine or subvert tobacco control efforts and the need to be informed of activities of the tobacco industry that have a negative impact on tobacco control efforts".

3. Further, Article 5.3 of the Convention requires that "in setting and implementing their public health policies with respect to tobacco control, Parties shall act to protect these policies from commercial and other vested interests of the tobacco industry in accordance with national law".

4. The Conference of the Parties, in decision FCTC/COP2(14), established a working group to elaborate guidelines for implementation of Article 5.3 of the Convention.

5. Without prejudice to the sovereign right of the Parties to determine and establish their tobacco control policies, Parties are encouraged to implement these guidelines to the extent possible in accordance with their national law.

Purpose, scope and applicability

6. Use of the guidelines for implementation of Article 5.3 of the Convention will have an overarching impact on countries' tobacco control policies and on implementation of the Convention, because the guidelines recognize that tobacco industry interference, including that from the State-owned tobacco industry, cuts across a number of tobacco control policy areas, as stated in the Preamble of the Convention, articles referring to specific tobacco control policies and the Rules of Procedure of the Conference of the Parties to the WHO Framework Convention on Tobacco Control.

[1] "The term 'Parties' refers to States and other entities with treaty-making capacity which have expressed their consent to be bound by a treaty and where the treaty is in force for such States and entities." (Source: United Nations Treaty Collections: http://untreaty.un.org/English/guide.asp#signatories).

7. The purpose of these guidelines is to ensure that efforts to protect tobacco control from commercial and other vested interests of the tobacco industry are comprehensive and effective. Parties should implement measures in all branches of government that may have an interest in, or the capacity to, affect public health policies with respect to tobacco control.

8. The aim of these guidelines is to assist Parties[2] in meeting their legal obligations under Article 5.3 of the Convention. The guidelines draw on the best available scientific evidence and the experience of Parties in addressing tobacco industry interference.

9. The guidelines apply to setting and implementing Parties' public health policies with respect to tobacco control. They also apply to persons, bodies or entities that contribute to, or could contribute to, the formulation, implementation, administration or enforcement of those policies.

10. The guidelines are applicable to government officials, representatives and employees of any national, state, provincial, municipal, local or other public or semi/quasi-public institution or body within the jurisdiction of a Party, and to any person acting on their behalf. Any government branch (executive, legislative and judiciary) responsible for setting and implementing tobacco control policies and for protecting those policies against tobacco industry interests should be accountable.

11. The broad array of strategies and tactics used by the tobacco industry to interfere with the setting and implementing of tobacco control measures, such as those that Parties to the Convention are required to implement, is documented by a vast body of evidence. The measures recommended in these guidelines aim at protecting against interference not only by the tobacco industry but also, as appropriate, by organizations and individuals that work to further the interests of the tobacco industry.

12. While the measures recommended in these guidelines should be applied by Parties as broadly as necessary, in order best to achieve the objectives of Article 5.3 of the Convention, Parties are strongly urged to implement measures beyond those recommended in these guidelines when adapting them to their specific circumstances.

GUIDING PRINCIPLES

Principle 1: There is a fundamental and irreconcilable conflict between the tobacco industry's interests and public health policy interests.

13. The tobacco industry produces and promotes a product that has been proven scientifically to be addictive, to cause disease and death and to give rise to a variety of social ills, including increased poverty. Therefore, Parties should protect the formulation and implementation of public health policies for tobacco control from the tobacco industry to the greatest extent possible.

[2] Where appropriate, these guidelines also refer to regional economic integration organizations.

Principle 2: Parties, when dealing with the tobacco industry or those working to further its interests, should be accountable and transparent.

14. Parties should ensure that any interaction with the tobacco industry on matters related to tobacco control or public health is accountable and transparent.

Principle 3: Parties should require the tobacco industry and those working to further its interests to operate and act in a manner that is accountable and transparent.

15. The tobacco industry should be required to provide Parties with information for effective implementation of these guidelines.

Principle 4: Because their products are lethal, the tobacco industry should not be granted incentives to establish or run their businesses.

16. Any preferential treatment of the tobacco industry would be in conflict with tobacco control policy.

RECOMMENDATIONS

17. The following important activities are recommended for addressing tobacco industry interference in public health policies:

(1) Raise awareness about the addictive and harmful nature of tobacco products and about tobacco industry interference with Parties' tobacco control policies.

(2) Establish measures to limit interactions with the tobacco industry and ensure the transparency of those interactions that occur.

(3) Reject partnerships and non-binding or non-enforceable agreements with the tobacco industry.

(4) Avoid conflicts of interest for government officials and employees.

(5) Require that information provided by the tobacco industry be transparent and accurate.

(6) Denormalize and, to the extent possible, regulate activities described as "socially responsible" by the tobacco industry, including but not limited to activities described as "corporate social responsibility".

(7) Do not give preferential treatment to the tobacco industry.

(8) Treat State-owned tobacco industry in the same way as any other tobacco industry.

18. Agreed measures for protecting public health policies with respect to tobacco control from commercial and other vested interests of the tobacco industry are listed below. Parties are encouraged to implement measures beyond those provided for by these guidelines, and nothing in these guidelines shall prevent a Party from imposing stricter requirements that are consistent with these recommendations.

(1) Raise awareness about the addictive and harmful nature of tobacco products and about tobacco industry interference with Parties' tobacco control policies.

19. All branches of government and the public need knowledge and awareness about past and present interference by the tobacco industry in setting and implementing public health policies with respect to tobacco control. Such interference requires specific action for successful implementation of the whole Framework Convention.

Recommendations

1.1 Parties should, in consideration of Article 12 of the Convention, inform and educate all branches of government and the public about the addictive and harmful nature of tobacco products, the need to protect public health policies for tobacco control from commercial and other vested interests of the tobacco industry and the strategies and tactics used by the tobacco industry to interfere with the setting and implementation of public health policies with respect to tobacco control.

1.2 Parties should, in addition, raise awareness about the tobacco industry's practice of using individuals, front groups and affiliated organizations to act, openly or covertly, on their behalf or to take action to further the interests of the tobacco industry.

(2) Establish measures to limit interactions with the tobacco industry and ensure the transparency of those interactions that occur.

20. In setting and implementing public health policies with respect to tobacco control, any necessary interaction with the tobacco industry should be carried out by Parties in such a way as to avoid the creation of any perception of a real or potential partnership or cooperation resulting from or on account of such interaction. In the event the tobacco industry engages in any conduct that may create such a perception, Parties should act to prevent or correct this perception.

Recommendations

2.1 Parties should interact with the tobacco industry only when and to the extent strictly necessary to enable them to effectively regulate the tobacco industry and tobacco products.

2.2 Where interactions with the tobacco industry are necessary, Parties should ensure that such interactions are conducted transparently. Whenever possible, interactions should be conducted in public, for example through public hearings, public notice of interactions, disclosure of records of such interactions to the public.

(3) Reject partnerships and non-binding or non-enforceable agreements with the tobacco industry.

21. The tobacco industry should not be a partner in any initiative linked to setting or implementing public health policies, given that its interests are in direct conflict with the goals of public health.

Recommendations

3.1 Parties should not accept, support or endorse partnerships and non-binding or non-enforceable agreements as well as any voluntary arrangement with the tobacco industry or any entity or person working to further its interests.

3.2 Parties should not accept, support or endorse the tobacco industry organizing, promoting, participating in, or performing, youth, public education or any initiatives that are directly or indirectly related to tobacco control.

3.3 Parties should not accept, support or endorse any voluntary code of conduct or instrument drafted by the tobacco industry that is offered as a substitute for legally enforceable tobacco control measures.

3.4 Parties should not accept, support or endorse any offer for assistance or proposed tobacco control legislation or policy drafted by or in collaboration with the tobacco industry.

(4) Avoid conflicts of interest for government officials and employees.

22. The involvement of organizations or individuals with commercial or vested interests in the tobacco industry in public health policies with respect to tobacco control is most likely to have a negative effect. Clear rules regarding conflicts of interest for government officials and employees working in tobacco control are important means for protecting such policies from interference by the tobacco industry.

23. Payments, gifts and services, monetary or in-kind, and research funding offered by the tobacco industry to government institutions, officials or employees can create conflicts of interest. Conflicting interests are created even if a promise of favourable consideration is not given in exchange, as the potential exists for personal interest to influence official responsibilities as recognized in the International Code of Conduct for Public Officials adopted by the United Nations General Assembly and by several governmental and regional economic integration organizations.

Recommendations

4.1 Parties should mandate a policy on the disclosure and management of conflicts of interest that applies to all persons involved in setting and implementing public health policies with respect to tobacco control, including government officials, employees, consultants and contractors.

4.2 Parties should formulate, adopt and implement a code of conduct for public officials, prescribing the standards with which they should comply in their dealings with the tobacco industry.

4.3 Parties should not award contracts for carrying out any work related to setting and implementing public health policies with respect to tobacco control to candidates or tenderers who have conflicts of interest with established tobacco control policies.

4.4 Parties should develop clear policies that require public office holders who have or have had a role in setting and implementing public health policies with respect to tobacco control to inform their institutions about any intention to engage in an

occupational activity within the tobacco industry, whether gainful or not, within a specified period of time after leaving service.

4.5 Parties should develop clear policies that require applicants for public office positions which have a role in setting and implementing public health policies with respect to tobacco control to declare any current or previous occupational activity with any tobacco industry whether gainful or not.

4.6 Parties should require government officials to declare and divest themselves of direct interests in the tobacco industry.

4.7 Government institutions and their bodies should not have any financial interest in the tobacco industry, unless they are responsible for managing a Party's ownership interest in a State-owned tobacco industry.

4.8 Parties should not allow any person employed by the tobacco industry or any entity working to further its interests to be a member of any government body, committee or advisory group that sets or implements tobacco control or public health policy.

4.9 Parties should not nominate any person employed by the tobacco industry or any entity working to further its interests to serve on delegations to meetings of the Conference of the Parties, its subsidiary bodies or any other bodies established pursuant to decisions of the Conference of the Parties.

4.10 Parties should not allow any official or employee of government or of any semi/quasi-governmental body to accept payments, gifts or services, monetary or in-kind, from the tobacco industry.

4.11 Taking into account national law and constitutional principles, Parties should have effective measures to prohibit contributions from the tobacco industry or any entity working to further its interests to political parties, candidates or campaigns, or to require full disclosure of such contributions.

(5) Require that information provided by the tobacco industry be transparent and accurate.

24. To take effective measures preventing interference of the tobacco industry with public health policies, Parties need information about its activities and practices, thus ensuring that the industry operates in a transparent manner. Article 12 of the Convention requires Parties to promote public access to such information in accordance with national law.

25. Article 20.4 of the Convention requires, inter alia, Parties to promote and facilitate exchanges of information about tobacco industry practices and the cultivation of tobacco. In accordance with Article 20.4(c) of the Convention, each Party should endeavour to cooperate with competent international organizations to establish progressively and maintain a global system to regularly collect and disseminate information on tobacco production and manufacture and activities of the tobacco industry which have an impact on the Convention or national tobacco control activities.

Recommendations

5.1 Parties should introduce and apply measures to ensure that all operations and activities of the tobacco industry are transparent.[3]

5.2 Parties should require the tobacco industry and those working to further its interests to periodically submit information on tobacco production, manufacture, market share, marketing expenditures, revenues and any other activity, including lobbying, philanthropy, political contributions and all other activities not prohibited or not yet prohibited under Article 13 of the Convention.[1]

5.3 Parties should require rules for the disclosure or registration of the tobacco industry entities, affiliated organizations and individuals acting on their behalf, including lobbyists.

5.4 Parties should impose mandatory penalties on the tobacco industry in case of the provision of false or misleading information in accordance with national law.

5.5 Parties should adopt and implement effective legislative, executive, administrative and other measures to ensure public access, in accordance with Article 12(c) of the Convention, to a wide range of information on tobacco industry activities as relevant to the objectives of the Convention, such as in a public repository.

(6) Denormalize and, to the extent possible, regulate activities described as "socially responsible" by the tobacco industry, including but not limited to activities described as "corporate social responsibility".

26. The tobacco industry conducts activities described as socially responsible to distance its image from the lethal nature of the product it produces and sells or to interfere with the setting and implementation of public health policies. Activities that are described as "socially responsible" by the tobacco industry, aiming at the promotion of tobacco consumption, is a marketing as well as a public relations strategy that falls within the Convention's definition of advertising, promotion and sponsorship.

27. The corporate social responsibility of the tobacco industry is, according to WHO,[4] an inherent contradiction, as industry's core functions are in conflict with the goals of public health policies with respect to tobacco control.

Recommendations

6.1 Parties should ensure that all branches of government and the public are informed and made aware of the true purpose and scope of activities described as socially responsible performed by the tobacco industry.

6.2 Parties should not endorse, support, form partnerships with or participate in activities of the tobacco industry described as socially responsible.

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[3] Without prejudice to trade secrets or confidential information protected by law.

[4] WHO. *Tobacco industry and corporate social responsibility – an inherent contradiction*. Geneva, World Health Organization, 2004.

6.3 Parties should not allow public disclosure by the tobacco industry or any other person acting on its behalf of activities described as socially responsible or of the expenditures made for these activities, except when legally required to report on such expenditures, such as in an annual report.[5]

6.4 Parties should not allow acceptance by any branch of government or the public sector of political, social, financial, educational, community or other contributions from the tobacco industry or from those working to further its interests, except for compensations due to legal settlements or mandated by law or legally binding and enforceable agreements.

(7) Do not give preferential treatment to the tobacco industry.

28. Some governments encourage investments by the tobacco industry, even to the extent of subsidizing them with financial incentives, such as providing partial or complete exemption from taxes otherwise mandated by law.

29. Without prejudice to their sovereign right to determine and establish their economic, financial and taxation policies, Parties should respect their commitments for tobacco control.

Recommendations

7.1 Parties should not grant incentives, privileges or benefits to the tobacco industry to establish or run their businesses.

7.2 Parties that do not have a State-owned tobacco industry should not invest in the tobacco industry and related ventures. Parties with a State-owned tobacco industry should ensure that any investment in the tobacco industry does not prevent them from fully implementing the WHO Framework Convention on Tobacco Control.

7.3 Parties should not provide any preferential tax exemption to the tobacco industry.

(8) Treat State-owned tobacco industry in the same way as any other tobacco industry.

30. Tobacco industry can be government-owned, non-government-owned or a combination thereof. These guidelines apply to all tobacco industry, regardless of its ownership.

Recommendations

8.1 Parties should ensure that State-owned tobacco industry is treated in the same way as any other member of the tobacco industry in respect of setting and implementing tobacco control policy.

8.2 Parties should ensure that the setting and implementing of tobacco control policy are separated from overseeing or managing tobacco industry.

[5] The guidelines for implementation of Article 13 of the WHO Framework Convention on Tobacco Control address this subject from the perspective of tobacco advertising, promotion and sponsorship.

8.3 Parties should ensure that representatives of State-owned tobacco industry does not form part of delegations to any meetings of the Conference of the Parties, its subsidiary bodies or any other bodies established pursuant to decisions of the Conference of the Parties.

Enforcement and monitoring

Enforcement

31. Parties should put in place enforcement mechanisms or, to the extent possible, use existing enforcement mechanisms to meet their obligations under Article 5.3 of the Convention and these guidelines.

Monitoring implementation of Article 5.3 of the Convention and of these guidelines

32. Monitoring implementation of Article 5.3 of the Convention and of these guidelines is essential for ensuring the introduction and implementation of efficient tobacco control policies. This should also involve monitoring the tobacco industry, for which existing models and resources should be used, such as the database on tobacco industry monitoring of the WHO Tobacco Free Initiative.

33. Nongovernmental organizations and other members of civil society not affiliated with the tobacco industry could play an essential role in monitoring the activities of the tobacco industry.

34. Codes of conduct or staff regulations for all branches of governments should include a "whistleblower function", with adequate protection of whistleblowers. In addition, Parties should be encouraged to use and enforce mechanisms to ensure compliance with these guidelines, such as the possibility of bringing an action to court, and to use complaint procedures such as an ombudsman system.

INTERNATIONAL COLLABORATION AND UPDATING AND REVISION OF THE GUIDELINES

35. International cooperation is essential for making progress in preventing interference by the tobacco industry with the formulation of public health policies on tobacco control. Article 20.4 of the Convention provides the basis for collecting and exchanging knowledge and experience with respect to tobacco industry practices, taking into account and addressing the special needs of developing country Parties and Parties with economies in transition.

36. Efforts have already been made to coordinate the collection and dissemination of national and international experience with regard to the strategies and tactics used by the tobacco industry and to the monitoring of tobacco industry activities. Parties would benefit from sharing legal and strategic expertise for countering tobacco industry strategies. Article 21.4 of the Convention provides that information exchange should be subject to national laws regarding confidentiality and privacy.

Recommendations

37. As the strategies and tactics used by the tobacco industry evolve constantly, these guidelines should be reviewed and revised periodically to ensure that they continue to provide

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Electronic nicotine delivery systems

Report by WHO

INTRODUCTION

1. This document was prepared in response to the request made by the Conference of the Parties (COP) at its fifth session (Seoul, Republic of Korea, 12–17 November 2012) to the Convention Secretariat to invite WHO to examine emerging evidence on the health impacts of electronic nicotine delivery systems (ENDS) use and to identify options for their prevention and control, for consideration at the sixth session of the COP.[1] This report incorporates the December 2013 deliberations and scientific recommendations on ENDS by the WHO Study Group on Tobacco Product Regulation (TobReg), and analysis from a recent WHO survey on tobacco products.[2]

2. ENDS are the subject of a public health dispute among bona fide tobacco-control advocates that has become more divisive as their use has increased. Whereas some experts welcome ENDS as a pathway to the reduction of tobacco smoking, others characterize them as products that could undermine efforts to denormalize tobacco use. ENDS, therefore, represent an evolving frontier, filled

[1] See decision FCTC/COP5(10).

[2] The WHO tobacco products survey on smokeless, electronic nicotine delivery systems, reduced ignition propensity cigarettes, and novel tobacco products was sent to all WHO Member States. A total of 90 WHO Member States, including 86 Parties to the WHO FCTC, had responded to the survey as at 9 April 2014. These countries are: Australia, Austria, Bahrain, Bangladesh, Barbados, Belarus, Belgium, Belize, Bhutan, Bolivia (Plurinational State of), Botswana, Brazil, Brunei Darussalam, Cambodia, Canada, Chile, China, Colombia, Congo, Costa Rica, Croatia, Czech Republic, Djibouti, Dominica, Ecuador, Egypt, Estonia, Fiji, Finland, France, Gabon, Georgia, Ghana, Guatemala, Honduras, Hungary, Iceland, India, Indonesia, Iran (Islamic Republic of), Iraq, Jamaica, Japan, Jordan, Kenya, Kuwait, Lao People's Democratic Republic, Latvia, Lebanon, Lithuania, Malaysia, Maldives, Mali, Mauritania, Mongolia, Morocco, Myanmar, Netherlands, New Zealand, Nicaragua, Norway, Oman, Pakistan, Palau, Panama, Paraguay, Peru, Philippines, Poland, Qatar, Republic of Korea, Russian Federation, Slovakia, South Sudan, Spain, Sudan, Suriname, Sweden, Syrian Arab Republic, Thailand, Tonga, Tunisia, Turkey, Tuvalu, United Arab Emirates, United States of America, Uruguay, Uzbekistan, Viet Nam, and Zambia.

with promise and threat for tobacco control. Whether ENDS fulfil the promise or the threat depends on a complex and dynamic interplay among the industries marketing ENDS (independent makers and tobacco companies), consumers, regulators, policy-makers, practitioners, scientists, and advocates. The evidence and recommendations presented in this report are therefore subject to rapid change.

PRODUCT DESIGN AND CONTENTS

3. ENDS, of which electronic cigarettes are the most common prototype, deliver an aerosol by heating a solution that users inhale. The main constituents of the solution by volume, in addition to nicotine when nicotine is present, are propylene glycol, with or without glycerol and flavouring agents.

4. Although some ENDS are shaped to look like their conventional tobacco counterparts (e.g. cigarettes, cigars, cigarillos, pipes, or hookahs), they also take the form of everyday items such as pens, USB memory sticks, and larger cylindrical or rectangular devices.

5. Battery voltage and unit circuitry differences can result in considerable variability in the products' ability to heat the solution to an aerosol and, consequently, may affect delivery of nicotine and other constituents, and may contribute to the formation of toxicants in the emissions.

6. User behaviour may affect nicotine absorption – length of puffs, depth of inhalation and frequency of use may be factors. However, while a faster, deeper puff increases nicotine delivery from a conventional cigarette, it might diminish it from ENDS due to cooling of the heating element.

7. In addition to manufacturer differences, some users modify products at home to alter delivery of nicotine and/or other drugs. Products vary widely in the ease with which they can be modified and the ease with which they can be filled with substances other than nicotine solutions.

THE ENDS MARKET

8. The use of ENDS is apparently booming. It is estimated that in 2014 there were 466 brands[1] and that in 2013 US$ 3 billion was spent on ENDS globally. Sales are forecasted to increase by a factor of 17 by 2030.[2] Despite this projection, transnational tobacco companies are divided about the prospects of the growth of ENDS sales and some companies have reported a slowdown in sales in some markets.[3,4,5] There are no data on ENDS use at the global level and for many countries. However, data mainly from North America, the European Union (EU) and Republic of Korea indicate that ENDS use at least doubled among both adults and adolescents from 2008 to 2012.[6] In 2012, 7% of EU citizens aged 15 years and over had tried electronic cigarettes. However, only 1% of the total population used them regularly.[7] In 2013, 47% of smokers and ex-smokers in the United States of

[1] Zhu S-H, Sun JY, Bonnevie E, Cummins SE, Gamst A, Yin L, Lee M. Four hundred and sixty brands of e-cigarettes and counting: implications for product regulation. Tobacco Control. 2014;23:iii3–iii9. doi:10.1136/tobaccocontrol-2014-051670.

[2] The tobacco industry at a crossroads: cigarettes growth falters as focus falls on alternatives. Euromonitor international. July 2013

[3] Evans P. E-cigarettes are the future? Not so fast, says BAT's boss. Wall Street Journal. 30 July 2014 (http://blogs.wsj.com/corporate-intelligence/2014/07/30/e-cigs-are-the-future-not-so-fast-says-bats-boss/)

[4] Prior A. Lorillard profit down as e-cigarette sales drop: electronic cigarette sales tumble 35%, offsetting slight increase in traditional cigarettes. Wall Street Journal. 30 July 2014 (http://online.wsj.com/articles/lorillard-profit-down-as-e-cigarette-sales-drop-1406720447).

[5] Wile R. Citi e-cigarettes: the e-cigarette boom is over. Business Insider. 15 May 2014 (http://www.businessinsider.com/citi-ecigarette-growth-slows-2014-5).

[6] Grana R, Benowitz N, Glantz SA. E-cigarettes: a scientific review. Circulation. 2014;129: e490–e492. doi:10.1161/CIRCULATIONAHA.114.008545.

[7] Attitudes of Europeans towards tobacco (Special Eurobarometer 385). European Commission, May 2012.

America had tried e-cigarettes, but prevalence of established use was 4% in this group.[1] Users report that the main reasons for using ENDS are to reduce or stop smoking and because they can be used in smoke-free places.[2]

9. According to the recent WHO survey, ENDS availability is widespread. Slightly over half of the world's population live in 62 countries that report the availability of ENDS in their jurisdictions, 4% live in countries reporting that ENDS are not available, while the rest live in countries that did not respond concerning the availability of ENDS.

10. Recently, the transnational tobacco companies have entered the ENDS market. Some of them are aggressively competing with the independent companies to gain market share. Given the economic power of the tobacco industry, recent moves to sue other companies alleging patent infringement may be an indicator of how difficult it will be for ENDS to remain a business niche dominated by independent companies.

QUESTIONS RELATED THE USE OF ENDS

11. Questions have been articulated in three groups:

(a) health risks to users and non-users;

(b) efficacy in helping smokers to quit smoking and ultimately nicotine dependence; and

(c) interference with existing tobacco-control efforts and implementation of the WHO FCTC.

Health risks to users and non-users

12. Most ENDS products have not been tested by independent scientists but the limited testing has revealed wide variations in the nature of the toxicity of contents and emissions.

13. Health risks from nicotine inhalation are affected by several factors.

(a) The capacity of ENDS to deliver nicotine to the user varies widely, ranging from very low to levels similar to that of cigarettes, depending on product characteristics, user puffing behaviour and nicotine solution concentration.

(b) Nicotine is the addictive component of tobacco. It can have adverse effects during pregnancy and may contribute to cardiovascular disease. Although nicotine itself is not a carcinogen, it may function as a "tumour promoter".[3] Nicotine seems involved in fundamental aspects of the biology of malignant diseases, as well as of neurodegeneration.

[1] Giovenco DP, Lewis MJ, Delnevo CD. Factors associated with e-cigarette use. American Journal of Preventive Medicine. Published online, 27 May 2014. doi: http://dx.doi.org/10.1016/j.amepre.2014.04.009.

[2] Grana R, Benowitz N, Glantz SA. E-cigarettes: a scientific review. Circulation. 2014;129: e490–e492. doi:10.1161/CIRCULATIONAHA.114.008545.

[3] Nicotine alters essential biological processes like regulation of cell proliferation, apoptosis, migration, invasion, angiogenesis, inflammation and cell-mediated immunity in a wide variety of cells including fetal, embryonic and adult stem cells, adult tissues as well as cancer cells.

(c) The evidence is sufficient to caution children and adolescents, pregnant women, and women of reproductive age about ENDS use because of the potential for fetal and adolescent nicotine exposure to have long-term consequences for brain development.[1]

14. The main health risk from nicotine exposure other than through inhalation is nicotine overdose by ingestion or through dermal contact. Since most countries do not monitor these incidents the information is very scarce. Reports from the United States and the United Kingdom nonetheless indicate that the number of reported incidents involving nicotine poisoning has risen substantially as the use of ENDS has increased. The actual number of cases is probably much higher than those reported.

15. Evidence concerning the health risks resulting from chronic inhalation of toxicants in aerosol to ENDS users are described below.

(a) Short-term effects of ENDS use include eye and respiratory irritation caused by exposure to propylene glycol. Serious short-term health problems may occur but are very rare.

(b) Given the relatively recent entry of ENDS into the market and the lengthy lag time for onset of many diseases of interest,[2] such as cancer, conclusive evidence about the association of ENDS use with such diseases will not be available for years or even decades.

(c) However, evidence based on the assessment of the chemical compounds in the liquids used in and aerosol produced by ENDS indicate:

(i) potential cytotoxicity of some solutions that have raised concerns about pregnant women who use ENDS or are exposed to second-hand ENDS aerosol.[3] Cytotoxicity was related to the concentration and number of flavourings used in the e-liquid;

(ii) the aerosol usually contains some carcinogenic compounds and other toxicants found in tobacco smoke at average levels of 1–2 orders of magnitude lower than in tobacco smoke, but higher than in a nicotine inhaler. For some brands, the level of some of these cancer causing agents, such as formaldehyde and other toxicants like acrolein have been found to be as high as in the smoke produced by some cigarettes;[4]

(iii) the range of size of particles delivered by ENDS is similar to that of conventional cigarettes, with most particles in the ultrafine range (modes around 100–200 nm) compared to the bigger size found in cigarette smoke. However, ENDS generate lower level of particles than cigarettes.[5]

(d) Therefore, it is very likely that average ENDS use produces lower exposures to toxicants that combustible products.

16. Evidence concerning the health risks resulting from inhalation of second-hand ENDS aerosol by non-users are described below.

[1] The health consequences of smoking – 50 years of progress. A report of the Surgeon General. Rockville (MD); US Department of Health and Human Services: 2014 (p.126).

[2] Including the lack of agreed early biomarker changes to assess potential harms.

[3] Bahl V, Lin S, Xu N, Davis B, Wang Y. Comparison of electronic cigarette refill fluid cytotoxicity using embryonic and adult models. Reproductive Toxicology. 2012;34:529–37.

[4] Goniewicz ML, Knysak J, Gawron M, Kosmider L, Sobczak A, Kurek J et al. Levels of selected carcinogens and toxicants in vapour from electronic cigarettes. Tobacco Control. 2014;23(2):133–139. doi:10.1136/tobaccocontrol-2012-050859.

[5] Schripp T., D. Markewitz, E. Uhde, and T. Salthammer. Does e-cigarette consumption cause passive vaping? Indoor Air. 2013;23(1):25–31.

(a) Bystanders are exposed to the aerosol exhaled by ENDS users, which increases the background level of some toxicants,[1,2] nicotine[3] as well as fine and ultrafine particles in the air. Nevertheless the level of toxicants, nicotine and particles emitted from one ENDS is lower than that of conventional cigarette emissions.[4] It is not clear if these lower levels in exhaled aerosol translate into lower exposure, as demonstrated in the case of nicotine. Despite having a lower levels of nicotine than in second-hand smoke, the exhaled ENDS aerosol results in similar uptake as shown by similar serum cotinine levels.[5]

(b) It is unknown if the increased exposure to toxicants and particles in exhaled aerosol will lead to an increased risk of disease and death among bystanders as does the exposure to tobacco smoke. However, epidemiological evidence from environmental studies shows adverse effects of particulate matter from any source following both short-term and long-term exposures. The low end of the range of concentrations at which adverse health effects has been demonstrated is not greatly above the background concentration, which for particles smaller than 2.5 μm has been estimated to be 3–5 μg/m3 and increases with dose, which means that there is no threshold for harm and that public health measures should aim at achieving the lowest concentrations possible.[6]

17. In summary, the existing evidence shows that ENDS aerosol is not merely "water vapour" as is often claimed in the marketing for these products. ENDS use poses serious threats to adolescents and fetuses. In addition, it increases exposure of non-smokers and bystanders to nicotine and a number of toxicants. Nevertheless, the reduced exposure to toxicants of well-regulated ENDS used by established adult smokers as a complete substitution for cigarettes is likely to be less toxic for the smoker than conventional cigarettes or other combusted tobacco products. The amount of risk reduction, however, is presently unknown. The 2014 Surgeon General's Report concluded that non-combustible products such as ENDS are much more likely to provide public health benefits only in an environment where the appeal, accessibility, promotion, and use of cigarettes and other combusted tobacco products are being rapidly reduced.[7]

Efficacy in helping smokers to quit smoking and ultimately nicotine dependence

18. Although anecdotal reports indicate that an undetermined proportion of ENDS users have quit smoking using these products their efficacy has not been systematically evaluated yet. Only a few studies have examined whether the use of ENDS is an effective method for quitting tobacco smoking.

[1] Under near real-use conditions, e-cigarettes increased indoor air levels of polycyclic aromatic hydrocarbons, 1,2-propanediol, 1,2,3-propanetriol, glycerine, and aluminium.

[2] Schober W, Szendrei K, Matzen W, Osiander-Fuchs H, Heitmann D, Schettgen T et al. Use of electronic cigarettes (e-cigarettes) impairs indoor air quality and increases FeNO levels of e-cigarette consumers. International Journal of Hygiene and Environmental Health. 2014;217(6):628–37. doi:10.1016/j.ijheh.2013.11.003.

[3] Czogala J1, Goniewicz ML, Fidelus B, Zielinska-Danch W, Travers MJ, Sobczak A. Secondhand exposure to vapors from electronic cigarettes. Nicotine and Tobacco Research. 2014;16(6):655–62. doi: 10.1093/ntr/ntt203.

[4] McAuley TR, Hopke PK, Zhao J, Babaian S. Comparison of the effects of e-cigarette vapor and cigarette smoke on indoor air quality. Inhalation Toxicology. 2012;24(12):850-7.

[5] Flouris AD, Chorti MS, Poulianiti KP, Jamurtas AZ, Kostikas K, Tzatzarakis MN et al. Acute impact of active and passive electronic cigarette smoking on serum cotinine and lung function. Inhalation Toxicology. 2013;25(2):91–101. doi: 10.3109/08958378.2012.758197.

[6] WHO air quality guidelines for particulate matter, ozone, nitrogen dioxide and sulfur dioxide: summary of risk assessment. Geneva: World Health Organization; 2006.

[7] The health consequences of smoking – 50 years of progress: a report of the Surgeon General. Atlanta (GA): US Department of Health and Human Services; 2014 (p. 874).

19. The evidence for the effectiveness of ENDS as a method for quitting tobacco smoking is limited and does not allow conclusions to be reached. However, the results of the only randomized control trial that compared use of ENDS, with or without nicotine, to use of nicotine patches without medical assistance in the general population, showed similar, although low, efficacy for quitting smoking.[1] A recent study also shows some, although limited, effectiveness in real-world conditions.[2]

20. At this level of efficacy, the use of ENDS is likely to help some smokers to switch completely from cigarettes to ENDS. However, for a sizeable number of smokers ENDS use will result in the reduction of cigarette use rather than in quitting. This will lead to dual use of ENDS and cigarettes. Given the likely greater importance of duration of smoking (number of years smoking) over intensity (number of cigarettes smoked per day) in generating negative health consequences, dual use will have much smaller beneficial effects on overall survival compared with quitting smoking completely.[3]

21. No ENDS product has yet been evaluated and approved for smoking cessation by a governmental agency, although the United Kingdom's Medicines and Healthcare Products Regulatory Agency is in the process of reviewing some of these products.

22. In considering ENDS as a potential cessation aid, smokers should first be encouraged to quit smoking and nicotine addiction using a combination of already approved treatments. However, at the individual level, experts suggest that in some smokers who have failed treatment, have been intolerant to it or who refuse to use conventional smoking cessation medication, the use of appropriately-regulated ENDS may have a role to play in supporting attempts to quit.[4,5]

Impact on existing tobacco-control efforts

23. Although ENDS present a range of potential benefits to smokers, there is an extensive and often heated debate about whether ENDS will prove to have a positive or negative impact on population health and particularly tobacco control. Areas of legitimate concern include avoiding nicotine initiation among non-smokers and particularly youth while maximizing potential benefits for smokers. Such concerns are referred to as the gateway and renormalization effects.

24. Gateway and renormalization concerns.

(a) The gateway effect refers to two potential circumstances:

(i) the possibility that children (and generally non-smokers) will initiate nicotine use with ENDS at a rate greater than expected if ENDS did not exist;[6] and

(ii) the possibility that once addicted to nicotine through ENDS children will switch to cigarette smoking.

[1] Bullen CB, Howe C, Laugesen M, McRobbie H, Parag V, Williman J et al. Electronic cigarettes for smoking cessation: a randomised controlled trial. Lancet. 2013;382(9905):1629–37.

[2] Brown J, Beard E, Kotz D, Michie S, West R. Real-world effectiveness of e-cigarettes when used to aid smoking cessation: a cross-sectional population study. Addiction. Published online, 20 May 2014. doi:10.1111/add.12623.

[3] The health consequences of smoking – 50 years of progress: a report of the Surgeon General. Atlanta (GA): US Department of Health and Human Services; 2014.

[4] Fiore MC, Schroeder SA, Baker TB. Smoke, the chief killer – strategies for targeting combustible tobacco use. New England Journal of Medicine. 2014;370(4):297–9. doi: 10.1056/NEJMp1314942.

[5] Grana R, Benowitz N, Glantz SA. E-cigarettes: a scientific review. Circulation. 2014;129: e490–e492. doi:10.1161/CIRCULATIONAHA.114.008545.

[6] this This does not mean that use of ENDS by children in not a concern in itself.

(b) The renormalization effect refers to the possibility that everything that makes ENDS attractive to smokers may enhance the attractiveness of smoking itself and perpetuate the smoking epidemic. ENDS mimic the personal experience and public performance of smoking and their market growth requires marketing that is challenging commercial communication barriers erected to prevent the promotion of tobacco products.

(c) The likelihood and significance of these two effects occurring will be the result of a complex interplay of individual, market and regulatory factors and is difficult to predict. They can only be assessed with empirical data, which at present are virtually non-existent.

(d) The limited existing survey data from a handful of countries show that experimentation with ENDS is increasing rapidly among adolescents and that in itself is of great concern even if most of the young ENDS users also smoke. In fact, except in one case, the surveys show that there are few exclusive ENDS users who have never smoked (mostly around 1% of the population).[1,2,3] These data do not allow the conclusions to be drawn as to whether this is a sign of adolescent smokers switching to ENDS, an established pattern of dual use, or a temporary experimentation fashion. Therefore, in the absence of longitudinal data, existing evidence does not allow an affirmation or rejection of the role of ENDS in increasing nicotine addiction among adolescents above existing uptake rates, much less as to whether ENDS lead to smoking in these countries. Among adults the pattern of dual use seems also the predominant one, resulting in a reduction of smoked cigarettes and with few never smokers starting to use ENDS (below 1% of the population).[4,5]

(e) There are also very limited data from very few countries about the evolution of the smoking epidemic in the presence of the ENDS boom. In one country (United Kingdom), where tobacco-control measures are very strong and ENDS use is popular and growing, it seems that smoking prevalence, cigarette consumption as well as overall nicotine use continues to decrease gradually.[6] Whether these contrasting trends are causally related cannot be concluded from these data. At least for the United Kingdom, renormalization as measured by prevalence of smoking is not occurring currently. Whether this would be the case for other countries cannot be generalized from the existing data and needs to be proven empirically.

25. More specific public health questions related to the interaction between ENDS and tobacco-control efforts are discussed below.

26. Positioning the tobacco-control message: The entry of ENDS in the market has created challenges to the core message of tobacco control, which until now has been that tobacco use should

[1] Calculations based on Centers for Disease Control and Prevention reported data from the United States National Youth Tobacco Survey, contained in: Corey C, Wang B, Johnson SE, Apelberg B, Husten C, King BA et al. Notes from the field: electronic cigarette use among middle and high school students – United States, 2011–2012. Morbidity and Mortality Weekly Report;62(35):729–30.

[2] Lee S, Grana RA, Glantz SA, Electronic cigarette use among Korean adolescents: a cross-sectional study of market penetration, dual use, and relationship to quit attempts and former smoking. Journal of Adolescent Health. Published online, 22 November 2013. doi: http://dx.doi.org/10.1016/j.jadohealth.2013.11.003.

[3] Lukasz Goniewicz M, Zielinska-Danch W. Electronic cigarette use among teenagers and young adults in Poland. Pediatrics. Published online, 17 September 2012. doi:10.1542/peds.2011-3448.

[4] Sutfina EL, McCoy TP, Morrell HER, Hoeppner BB, Wolfson M. Electronic cigarette use by college students. Drug and Alcohol Dependence. 2013;131(3):214–221. http://dx.doi.org/10.1016/j.drugalcdep.2013.05.001.

[5] ASH UK fact sheet. Use of electronic cigarettes in Great Britain. April 2014. Available from: http://www.ash.org.uk/files/documents/ASH_891.pdf.

[6] West R, Brown J, Beard E. Smoking toolkit study. Trends in electronic cigarette use in England. Updated 4th April 2014. Available from: http://www.smokinginengland.info/latest-statistics/.

not be started and if started it should be stopped.[1] The promotion of ENDS comes with at least one of the following messages or a combination of them: (a) try to quit smoking and if everything fails use ENDS as the last resort; (b) you do not need to quit nicotine addiction, just smoking; and (c) you do not need to quit smoking, use ENDS where you cannot smoke. Some of these messages are difficult to harmonize with the core tobacco-control message and others are simply incompatible.

27. The role of the tobacco industry: The future role of ENDS is strongly determined by the commercial interests of the industry that manufactures and sells ENDS. While there are "independent" ENDS companies that have reported no interest in perpetuating tobacco use, the tobacco industry involved in the production and sale of ENDS certainly is.

(a) The ENDS market, initially dominated by companies with no links to the tobacco industry, is increasingly owned by the tobacco industry. All main transnational tobacco companies sell ENDS and one of them is launching legal proceedings over patents against its rivals as they become increasingly aggressive in the battle for the fast-growing e-cigarette market. The increasing concentration of the ENDS market in the hands of the transnational tobacco companies is of grave concern in light of the history of the corporations that dominate that industry.

(b) It is unclear yet what this means for the ENDS market. However, if prior interest of the tobacco industry in reduced-risk products serves as a precedent, their interest lies in maintaining the status quo in favour of cigarettes for as long as possible, while simultaneously providing a longer-term source of profit should the cigarette model prove unsustainable. In addition, selling these products is intended to bring reputational benefits to these companies, as they can pretend to be part of the solution to the smoking epidemic.[2] ENDS may follow the trend of smokeless tobacco wherein the industry's historic interest in smokeless tobacco products outside some Nordic countries was both because they could be used in smoke-free environments and because they could be promoted to young, non-tobacco users to create a new form of tobacco use.[3]

28. Potential interference with smoke-free policies.

(a) Smoke-free policies are designed not only to protect non-smokers from second-hand smoke, but also to provide incentives to quit smoking and to denormalize smoking as adolescents are particularly vulnerable to visual cues and social norms.[4]

(b) The use of ENDS in places where smoking is not allowed

(i) increases the exposure to exhaled aerosol toxicants of potential harm to bystanders,
(ii) reduces quitting incentives, and
(iii) may conflict with the smoking denormalizing effect.

(c) Many ENDS look like smoking products and even if they do not resemble them, the exhaled vapour looks like tobacco smoke. ENDS are marketed to be used where smoking is

[1] de Andrade M, Hastings G, Angus K, Dixon D, Purves R. The marketing of electronic cigarettes in the UK. London: Cancer Research UK; November 2013.

[2] Peeters S, Gilmore AB. Understanding the emergence of the tobacco industry's use of the term tobacco harm reduction in order to inform public health policy. Tobacco Control. Published online, 22 January 2014. doi:10.1136/tobaccocontrol-2013-051502.

[3] Mejia AB, Ling PM. Tobacco industry consumer research on smokeless tobacco users and product development. American Journal of Public Health. 2010;100(1):78–87. doi: 10.2105/AJPH.2008.152603.

[4] Preventing tobacco use among youth and young adults. A report of the Surgeon General. Rockville (MD); US Department of Health and Human Services: 2012.

prohibited and given the resemblance to tobacco products it is likely that their use where smoking is banned will make enforcing smoke-free policies more difficult.

(d) The fact that ENDS exhaled aerosol contains on average lower levels of toxicants than the emissions from combusted tobacco does not mean that these levels are acceptable to involuntarily exposed bystanders. In fact, exhaled aerosol is likely to increase above background levels the risk of disease to bystanders, especially in the case of some ENDS that produce toxicant levels in the range of that produced by some cigarettes.

29. The role of ENDS marketing (which falls into two categories: consumer marketing aimed at the general public, and stakeholder marketing aimed at policy-makers and public health bodies):

(a) ENDS are being marketed to consumers in many media and forms, including television commercials, sports and cultural sponsorship, celebrity endorsement, social networking, online advertising, point-of-sale displays, pricing strategies, and product innovation. Some marketing clearly emulates the very successful tobacco advertising asserting an independent identity and a lifestyle choice, aligning oneself with celebrities, fashionable and youthful places and activities. Some ENDS are marketed not only as socially acceptable but as socially superior. Unsubstantiated or overstated claims of safety and cessation are frequent marketing themes aimed at smokers. Some ENDS marketing also promotes long-term use as a permanent alternative to tobacco, and a temporary one in public places where smoking is banned. ENDS marketing activities have the potential to glamorize smoking and attracting children and non-smokers even if those are unintentional results. However, no empirical studies have been conducted to show whether the negative prospects of ENDS marketing are actually directly associated with attitudinal and behavioural changes among children and non-smokers consistent with the realization of such potential. Concerns have also been raised over the use of flavours in the marketing of ENDS. One recent study indicates that ENDS are marketed in 7764 unique flavours.[3] Although the role of ENDS flavours potential attractiveness has not been studied yet, expert opinion indicates that candy-like flavours could entice youths to experiment with ENDS and could also facilitate the development of tobacco dependence by enhancing the sensory rewards of ENDS use.[1] The tobacco industry's internal documents suggest that flavouring agents have played an important role in the industry's targeting of children and youth, and there is a concern that they could play the same role in the uptake of ENDS in these age groups.

(b) The marketing message to tobacco-control stakeholders is one of alignment of industry and public health interests based on the harm reduction potential of ENDS. This leads to a proposal of partnership between government and industry because industry claims a meaningful seat at the table in the so-called harm reduction debate.

CURRENT REGULATION AND POLICY: RESULTS OF THE WHO SURVEY

30. **Table 1** reflects the results of the 2014 WHO survey, showing the distribution of countries according to the regulatory approach taken to ENDS.

Type of ENDS	ENDS regulated as					Not regulated or unknown
	consumer product	therapeutic product	tobacco product	other	total	
With nicotine	14 (27%)*	12 (6%)	22 (10%)	11 (6%)	59 (49%)	135 (51%)
Without nicotine	23 (35%)	0 (0%)	18 (7%)	12 (2%)	53 (44%)	141 (56%)

[1] The scientific basis of tobacco product regulation: a WHO Study Group on Tobacco Product Regulation report. Candy-flavoured tobacco products: research needs and regulatory recommendations. Geneva; World Health Organization: 2007 (WHO Technical Report Series 945).

* The figure in parentheses after the number of countries indicates the percentage of the world population living in these countries.

31. The sale of ENDS with nicotine is banned in 13 of the 59 countries that regulate them. However, the majority of these 13 countries report that ENDS are available to the public, probably through illicit trade and cross-border Internet sales.

32. The survey also shows that:

(a) comprehensive advertising, promotion and sponsorship bans on ENDS are in place in 39 countries (in which 31% of the world's population live);

(b) use of ENDS in enclosed public places is banned in 30 countries (35%);

(c) premarket review is required by 19 countries (5%);

(d) vendor licences are required by nine countries (4%);

(e) policies on ENDS sales to minors were confirmed by 29 countries (8%). Where specified, minimum required age for purchase ranged from 18 to 21 years.

GENERAL CONSIDERATIONS

33. Smokers will obtain the maximum health benefit if they completely quit both tobacco and nicotine use. In fact, Article 5.2(b) of the Convention commits Parties not only to preventing and reducing tobacco consumption and exposure to tobacco smoke but also to preventing and reducing nicotine addiction independently from its source. Therefore, while medicinal use of nicotine is a public health option under the treaty, recreational use is not.

34. The rapid growth of ENDS use globally can neither be dismissed nor accepted without efforts to appropriately regulate these products, so as to minimize consequences that may contribute to the tobacco epidemic and to optimize the potential benefits to public health. Thus it is important to identify public health concerns and to consider these concerns when undertaking regulation and surveillance.

35. Regulation of ENDS is a necessary precondition for establishing a scientific basis on which to judge the effects of their use, and for ensuring that adequate research is conducted, that the public has current, reliable information as to the potential risks and benefits of ENDS, and that the health of the public is protected. Public health authorities need to prioritize research and invest adequately to elucidate evidentiary uncertainties as soon as possible. However, the greater responsibility to prove claims about ENDS scientifically should remain with the industry.

36. When designing a regulatory strategy for ENDS, governments should bear in mind the following general regulatory objectives:

(a) impede ENDS promotion to and uptake by non-smokers, pregnant women and youth;

(b) minimize potential health risks to ENDS users and non-users;

(c) prohibit unproven health claims from being made about ENDS; and

(d) protect existing tobacco-control efforts from commercial and other vested interests of the tobacco industry.

37. Because the product, the market and the associated scientific evidence surrounding ENDS are all evolving rapidly, all legislation and regulations related to ENDS should be adaptable in response to

new scientific evidence, including evaluation of different models for ENDS regulation, as evidence accumulates.

38. Governments should consider that if their country has already achieved a very low prevalence of smoking and that prevalence continues to decrease steadily, use of ENDS will not significantly decrease smoking-attributable disease and mortality even if the full theoretical risk reduction potential of ENDS were to be realized.

SPECIFIC REGULATORY OPTIONS

39. In order to achieve the general regulatory objectives mentioned above, Parties that have not banned the sale of ENDS could consider the following non-exhaustive list of regulatory options, on the understanding that the advisability and feasibility at country level of each of these options will depend on a complex set of country-specific factors, including the existing regulatory frameworks and the legal exigencies of the regulatory process.

40. **Health claims.** Prohibit manufacturers and third parties from making health claims for ENDS, including that ENDS are smoking cessation aids, until manufacturers provide convincing supporting scientific evidence and obtain regulatory approval. The regulatory standard for cessation claims and approval as cessation aids should remain an appropriate body of evidence, based on well-controlled clinical trials. For ENDS products to be approved for smoking cessation by the suitable regulatory agency, the appropriate balance should be reached between providing accurate scientific information to the public about the risks of ENDS use and its potential benefits as compared with smoking. This balance can only be determined through scientifically tested audience messaging.

41. **Use of ENDS in public places**. Since the reasonable expectation of bystanders is not a diminished risk in comparison to exposure to second-hand smoke but no risk increase from any product in the air they breathe, ENDS users should be legally requested not to use ENDS indoors, especially where smoking is banned until exhaled vapour is proven to be not harmful to bystanders and reasonable evidence exists that smoke-free policy enforcement is not undermined. If smoke-free legislation is not fully developed according to Article 8 of the WHO FCTC and the guidelines for its implementation, this should be done as soon as possible.

42. **Advertising, promotion and sponsorship**. Given that the same promotional elements that make ENDS attractive to adult smokers could also make them attractive to children and non-smokers, Parties should contemplate putting in place an effective restriction on ENDS advertising, promotion and sponsorship. Some forms of ENDS promotion, however, may be considered acceptable by Parties if empirical evidence shows that ENDS might play a role in helping some smokers to quit without leading to increased ENDS use by minors and non-smokers who otherwise would not have used nicotine.

43. Any form of ENDS advertising, promotion and sponsorship must be regulated by an appropriate governmental body. If this is not possible, an outright ban on ENDS advertising, promotion and sponsorship is preferable to the implementation of voluntary codes on ENDS marketing, given the overwhelming evidence that similar codes for tobacco and alcohol products have failed to protect young people from such advertising.

44. Advertising, promotion and sponsorship of ENDS with or without nicotine, must, at a minimum:

(a) state clearly whether the product contains nicotine or may be used with nicotine solutions;

(b) not make them appealing to or target, either explicitly or implicitly, non-smokers or non-nicotine users, and must therefore indicate that ENDS are not suitable for use by people who do not currently consume tobacco products;

(c) not make them appealing to or target, either explicitly or implicitly, minors, including through the selection of media, location or the context in which they appear or through imagery that promotes sexual or sporting prowess;

(d) never promote ENDS for non-smokers, and their use should not be portrayed as a desirable activity in its own right;

(e) encourage smoking cessation and provide a quitline number if one exists;

(f) contain nothing that could reasonably be expected to promote the use of tobacco products, such as:

(i) the appearance or/and use of tobacco products;
(ii) the use of any brand name, design, colour, emblem, trademark, logo or trade insignia or any other distinctive feature that might be associated by the audience with a tobacco product;
(iii) the use of the words e-cigarette, electronic cigarette, or any other descriptor that might reasonably be expected to create confusion with the promotion of cigarettes and other combustible tobacco products;
(iv) showing ENDS products in ways that could reasonably be expected to promote tobacco products, including images of tobacco-like products;

(g) not contain health or medicinal claims, unless the product is licensed for those purposes by the appropriate regulatory agency. Electronic cigarettes and other nicotine-containing products should be presented only as an alternative to tobacco, and should include warnings that dual use will not substantially reduce the dangers of smoking;

(h) not undermine any tobacco-control measure, including by not promoting the use of ENDS in places where smoking is banned;

(i) include factual information about product ingredients other than nicotine and in a way that does not distort evidence of risks;

(j) not link these products with gambling, alcohol, illicit drugs or with activities or locations in which using them would be unsafe or unwise.

45. Advertising, promotion and sponsorship of ENDS that contain nicotine or may be used with nicotine solutions must:

(a) clearly state the addictive nature of nicotine and that these products are intended to deliver nicotine;

(b) Prohibit suggestions that ENDS have positive qualities as a consequence of the addictive nature of the product.

46. All authorized forms of ENDS advertising, promotion and sponsorship must be cleared by the appropriate authority prior to publication/transmission in order to proactively prevent inappropriate marketing, and then be monitored to assess compliance.

47. **Protection from vested commercial interests.** Transparency should be required from ENDS and tobacco companies advocating for and against legislation and regulation, both directly and through third parties. No matter what role the tobacco industry plays in the production, distribution and sale of ENDS, this industry, its allies and front-groups can never be considered to be a legitimate public health partner or stakeholder while it continues to profit from tobacco and its products or represents the interests of the industry. Article 5.3 of the WHO FCTC should be respected when developing and implementing ENDS legislation and regulations.

48. **Product design and information**. ENDS should be regulated to:

(a) minimize content and emissions of toxicants;

(b) ensure use of nicotine of pharmacological quality, when nicotine use is intended;

(c) standardize nicotine delivery at levels known to the consumers;

(d) minimize acute nicotine toxicity;

(e) impede product alteration to use of other drugs;

(f) ban ENDS solutions with fruit, candy-like and alcohol-drinks flavours until empirical evidence shows that they are not attractive to minors;

(g) require manufacturers and importers to disclose to governmental authorities information about the contents and emissions of ENDS; and

(h) require registration of manufacturers and importers with governmental authorities.

49. **Health warnings.** ENDS health warnings should be commensurate with proven health risks. In this regard, the following risk warnings could be considered: potential nicotine addiction; potential respiratory, eyes, nose and throat irritant effect; potential adverse effect on pregnancy (due to nicotine exposure).

50. **Surveillance and monitoring**. Governments are recommended to use or strengthen their existing tobacco surveillance and monitoring systems to assess developments in ENDS and nicotine use by sex and age.

51. **Sale to minors.** Retailers should be prohibited from selling ENDS products to minors, and vending machines should be eliminated in almost all locations.

REGULATORY FRAMEWORK

52. In order to implement the suggested general regulatory objectives as well as the specific regulatory options, Parties will need to consider the available national regulatory frameworks that could best provide solid regulatory grounds. Nevertheless, it is likely that a two-pronged regulatory strategy – regulating ENDS as both a tobacco product, in accordance with the provisions of the WHO FCTC, and as a medical product – would be necessary.

53. The applicability of many of the WHO FCTC provisions to the regulation of ENDS was reviewed in a report by the Convention Secretariat on this topic[1] presented at the fifth session of the COP.

ACTION BY THE CONFERENCE OF THE PARTIES

54. The COP is invited to note this report and to provide further guidance.

[1] Document FCTC/COP/5/13 (available at www.who.int/fctc/publications).

Having reviewed the operation of proceedings conducted under Chapter Eleven of the North American Free Trade Agreement, the Free Trade Commission hereby adopts the following interpretations of Chapter Eleven in order to clarify and reaffirm the meaning of certain of its provisions:

A. Access to documents

1. Nothing in the NAFTA imposes a general duty of confidentiality on the disputing parties to a Chapter Eleven arbitration, and, subject to the application of Article 1137(4), nothing in the NAFTA precludes the Parties from providing public access to documents submitted to, or issued by, a Chapter Eleven tribunal.

2. In the application of the foregoing:

   (a) In accordance with Article 1120(2), the NAFTA Parties agree that nothing in the relevant arbitral rules imposes a general duty of confidentiality or precludes the Parties from providing public access to documents submitted to, or issued by, Chapter Eleven tribunals, apart from the limited specific exceptions set forth expressly in those rules.

   (b) Each Party agrees to make available to the public in a timely manner all documents submitted to, or issued by, a Chapter Eleven tribunal, subject to redaction of:

      (i) confidential business information;

      (ii) information which is privileged or otherwise protected from disclosure under the Party's domestic law; and

      (iii) information which the Party must withhold pursuant to the relevant arbitral rules, as applied.

   (c) The Parties reaffirm that disputing parties may disclose to other persons in connection with the arbitral proceedings such unredacted documents as they consider necessary for the preparation of their cases, but they shall ensure that those persons protect the confidential information in such documents.

   (d) The Parties further reaffirm that the Government of Canada, the United Mexican States and the United States of America may share with officials of their respective federal, state or provincial governments all relevant documents in the course of dispute settlement under Chapter Eleven of NAFTA, including confidential information.

3. The Parties confirm that nothing in this interpretation shall be construed to require any Party to furnish or allow access to information that it may withhold in accordance with Articles 2102 or 2105.

B. 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).

Closing Provision

The adoption by the Free Trade Commission of this or any future interpretation shall not be construed as indicating an absence of agreement among the NAFTA Parties about other matters of interpretation of the Agreement.

Done in triplicate at Washington, D.C., on the 31st day of July, 2001, in the English, French and Spanish languages, each text being equally authentic.

For the Government of the United States of America	For the Government of the United Mexican State	For the Government of Canada
[SIGNATURE]	[SIGNATURE]	[SIGNATURE]
Robert B. Zoellick Representative	Luis Ernesto Derbes Bautista Secretary of Economy	Pierre S. Pettigrew Minister for International Trade

ARBITRAL AWARD

In the matter of a NAFTA arbitration under the
UNCITRAL Arbitration Rules
between:

International Thunderbird Gaming Corporation
Claimant

and

The United Mexican States
Respondent

Before the Arbitral Tribunal constituted under Chapter Eleven of
the North American Free Trade Agreement, and comprised of:

Lic. Agustín Portal Ariosa
Professor Thomas W. Wälde
Professor Dr. Albert Jan van den Berg (President)

Washington D.C., January 26, 2006

Mexican nationals) who have attempted to operate facilities with so-called "skill" machines, and it has proceeded with the closure of every similar facility of which it became aware of and defended its actions in every court of appeal initiated by the operators of machines similar or identical to those of EDM.

174. Mexico contends that Thunderbird has not succeeded in proving any discrimination against EDM, whether based on nationality or otherwise. In this regard, Mexico disputes Thunderbird's three-part test Article 1102. According to Mexico, Article 1102 is directed only to nationality-based discrimination and proscribes only demonstrable and significant indications of bias and prejudice on the basis on nationality, which are to be proven by Thunderbird, "the like circumstances" of Article 1102 requiring an adequate comparison on the basis of the facts, thereby taking into account, in particular, compliance with local law relating to illegal conduct. Mexico adds that EDM is not "in like circumstances" with the operators of facilities that have been able to continue operating under temporary injunctive relief while their legal challenges were pending, as even if EDM filed "*juicio de amparo*" proceedings, it was not granted injunctive relief and moreover withdrew its appeals.

(iii)The Tribunal's findings

175. In construing Article 1102 of the NAFTA, the Tribunal gives effect to the plain wording of the text. The obligation of the host NAFTA Party under Article 1102 of the NAFTA is to accord non-discriminatory treatment towards the investment or investor of other NAFTA Parties. It must therefore be established that discriminatory treatment was accorded to the foreign investment or investor.

176. The burden of proof lies with Thunderbird, pursuant to Article 24(1) of the UNCITRAL Rules. In this respect, Thunderbird must show that its investment received treatment less favourable than Mexico has accorded, in like circumstances, to investments of Mexican nationals.

177. It is not expected from Thunderbird that it show separately that the less favourable treatment was motivated because of nationality. The text of Article 1102 of the NAFTA does not require such showing. Rather, the text contemplates the case where a foreign investor is treated less favourably than a national investor. That case is to be proven by a foreign investor, and, additionally, the reason why there was a less favourable treatment.[9]

178. In the Tribunal's view, Thunderbird has not sufficiently established – not even on a *prima facie* basis – that the EDM investments were treated, in like circumstances, worse than those of Mexican nationals (or any other nationals for that matter).

179. The record shows that SEGOB has sought to enforce Mexican legislation on gambling by pursuing the closure of numerous gambling facilities (most of which have been closed definitely), and that the official closure of Mexican gambling facilities was in fact pursued at the very same time SEGOB proceeded to the official closure of the EDM facilities in Nuevo Laredo and Matamoros (*see* Exh. R-9). The Tribunal notes that SEGOB met resistance from the gaming facilities in question, including those of EDM, before the Mexican courts. As a result, it appears that some of the facilities closed by SEGOB were able to continue to operate under temporary injunctive relief, but the record also shows that SEGOB legally challenged the court decisions granting injunctive relief in connection with SEGOB's official closure orders and that appeals are pending.

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[9] *See S.D. Myers Inc. v. Canada*, First Partial Award, 13 November 2000, UNCITRAL (NAFTA), http://ita.law.uvic.ca/documents/SDMeyers-1stPartialAward.pdf; *Pope & Talbot Inc. v. Canada*, Award on the Merits of Phase 2, 10 April 2001, UNCITRAL (NAFTA), http://ita.law.uvic.ca/documents/PopeandTalbot-Merit.pdf; *Feldman v. Mexico*, Award, 16 December 2002, ICSID Case No. ARB(AF)/99/1, http://www.worldbank.org/icsid/cases/feldman_mexico-award-en.PDF, *Occidental Exploration and Production Company v. Ecuador*, Final Award, 1 July 2004, LCIA Case No. UN3467, http://ita.law.uvic.ca/documents/Oxy-EcuadorFinalAward_001.pdf.

188. According to Mexico, Thunderbird's complaints about the SEGOB administrative proceedings are factually incorrect and in any event pertain to issues of pure domestic law; and Thunderbird has not presented any evidence of failures of the Mexican judicial system that it argues prejudiced it and constituted the principal reason why it withdrew its judicial appeals.

189. Mexico contends that it has adopted a uniform and consistent line of conduct with respect to illegal gaming operations. In particular, Mexico argues that it has, to its knowledge, closed down all facilities where so-called slot machines were operating and has legally challenged all court decisions granting injunctive relief regarding SEGOB official closure orders.

190. With respect to any alleged detrimental reliance on the *Oficio*, Mexico contends that SEGOB's determination that it would consider the machines to be prohibited games cannot be considered arbitrary, given that Thunderbird itself knew the nature of the machines and knew of the existing risk that they would be inspected by SEGOB and it would reach that conclusion.

191. As to the SEGOB administrative proceedings, Mexico denies that they were illegal, arbitrary or unfair, arguing that the decision itself indicates that EDM's evidence was taken into account even when not in strict accordance with the applicable domestic legal requirements and the decision set out a reasoned basis for its conclusions; that the procedure was transparent and in compliance with Mexican laws, validated by EDM's lawyers who were experts in Mexican law; and that if there had been a violation during the proceedings, there were appropriate judicial remedies available to challenge it.

(iii)The Tribunal's findings

192. The Tribunal shall interpret Article 1105(1) of the NAFTA in accordance with the NAFTA Free Trade Commission's Notes of Interpretation of certain Chapter

Eleven Provisions ("Minimum Standard of Treatment in Accordance with International Law") dated 31 July 2001[10], which provides as follows:

> 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).

193. The Tribunal shall accordingly measure the Article 1105(1) of the NAFTA minimum standard of treatment against the customary international law minimum standard, according to which foreign investors are entitled to a certain level of treatment, failing which the host State's international responsibility may be engaged.

194. The content of the minimum standard should not be rigidly interpreted and it should reflect evolving international customary law.[11] Notwithstanding the

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10 http://www.dfait-maeci.gc.ca/tna-nac/Nafta-interpr-en.asp.

11 *See* in particular *Mondev International Ltd. v. USA*, Award, 11 October 2002, ICSID Case No. ARB(AF)/99/2, http://www.state.gov/documents/organization/14442.pdf.; *ADF Group Inc. v. USA*, Award, 9 January 2003, ICSID Case No. ARB(AF)/00/1, http://www.worldbank.org/icsid/cases/ADF-award.pdf; *Waste Management Inc. v. Mexico*, Arbitral Award, 2 June 2002, ICSID Case No. ARB(AF)/98/2, http://www.worldbank.org/icsid/cases/waste_award.pdf; Final Award, 30 April 2004, ICSID Case No. ARB(AF)/00/3, http://ita.law.uvic.ca/documents/laudo_ingles.pdf.

evolution of customary law since decisions such as *Neer Claim* in 1926[12], the threshold for finding a violation of the minimum standard of treatment still remains high, as illustrated by recent international jurisprudence[13]. For the purposes of the present case, the Tribunal views acts that would give rise to a breach of the minimum standard of treatment prescribed by the NAFTA and customary international law as those that, weighed against the given factual context, amount to a gross denial of justice or manifest arbitrariness falling below acceptable international standards[14].

195. In the present case, the Tribunal is not convinced that Thunderbird has demonstrated that Mexico's conduct violated the minimum standard of treatment, for the following reasons.

196. The Tribunal has already found that Thunderbird could not reasonably rely on the *Oficio* to its detriment (*see* the Tribunal's findings under Issue 7 above).

197. As to the alleged failure to provide due process (constituting an administrative denial of justice) and the alleged manifest arbitrariness in administration (constituting proof of an abuse of right) in the SEGOB proceedings, the Tribunal

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12 *USA (L.F. Neer) v. Mexico* (1926), 4 R.I.A.A. 60 (Gen. Cl. Comm'n 1926).

13 *See* in this regard *Alex Genin et al. v. Estonia*, Award, 25 June 2001, ICSID Case No. ARB/99/2), http://www.worldbank.org/icsid/cases/genin.pdf; *Waste Management Inc. v. Mexico*, Final Award, 30 April 2004, ICSID Case No. ARB(AF)/00/3, http://ita.law.uvic.ca/documents/laudo_ingles.pdf.

14 *See* in this regard *Alex Genin et al. v. Estonia*, Award, 25 June 2001, ICSID Case No. ARB/99/2, http://www.worldbank.org/icsid/cases/genin.pdf; *S.D. Myers Inc. v. Canada*, First Partial Award, 13 November 2000, UNCITRAL (NAFTA), http://ita.law.uvic.ca/documents/SDMeyers-1stPartialAward.pdf; *Mondev International Ltd. v. USA*, Award, 11 October 2002, ICSID Case No. ARB(AF)/99/2, http://www.state.gov/documents/organization/14442.pdf.; *ADF Group Inc. v. USA*, Award, 9 January 2003, ICSID Case No. ARB(AF)/00/1, http://www.worldbank.org/icsid/cases/ADF-award.pdf; *Azinian v. Mexico*, Arbitral Award, 1 November 1999; ICSID Case No. ARB(AF)/97/2, http://www.worldbank.org/icsid/cases/robert_award.pdf; *Loewen v. USA*, Award, 26 June 2003, ICSID Case No. ARB(AF)/98/3, http://ita.law.uvic.ca/documents/Loewen-Award-2.pdf; *Case concerning Elettronica Sicula SpA (ELSI) (United States v. Italy*), 20 July 1989, 1989 I.C.J. 15.

cannot find sufficient evidence on the record establishing that the SEGOB proceedings were arbitrary or unfair, let alone so manifestly arbitrary or unfair as to violate the minimum standard of treatment.

198. In particular, the Tribunal notes that Thunderbird was given a full opportunity to be heard and to present evidence at the Administrative Hearing, and that it made use of this opportunity. The Tribunal does not find anything reproachable about the Administrative Order. The 31-page document appears, in the Tribunal's view, to be adequately detailed and reasoned; it reviews the evidence presented by Thunderbird at the hearing; and discusses at length the legal grounds on which SEGOB based its determination that the EDM machines were prohibited gambling equipment (*see* Exh. R-93).

199. As to the official closures of the EDM facilities, the Tribunal does not find that the manner in which SEGOB proceeded for the official closure was arbitrary. In fact, the record shows that on one occasion, SEGOB itself recognized that the official closure order for Nuevo Laredo was irregular and accordingly rectified its error by lifting the seals of the Nuevo Laredo facility.

200. The Tribunal does not exclude that the SEGOB proceedings may have been affected by certain irregularities. Rather, the Tribunal cannot find on the record any administrative irregularities that were grave enough to shock a sense of judicial propriety and thus give rise to a breach of the minimum standard of treatment. As acknowledged by Thunderbird, the SEGOB proceedings should be tested against the standards of due process and procedural fairness applicable to administrative officials. The administrative due process requirement is lower than that of a judicial process. Hence, for instance, even if one views the absence of Lic. Aguilar Coronado (who signed the Administrative Order) at the 10 July hearing as an administrative irregularity, it does not attain the minimum level of gravity required under Article 1105 of the NAFTA under the circumstances.

201. Finally, the SEGOB proceedings (including the Administrative Resolution) were subject to judicial review before the Mexican courts. The Tribunal notes in this

VII. DECISIONS

222. FOR THE FOREGOING REASONS, the Arbitral Tribunal renders the following decisions:

1) FINDS that Mexico did not breach Articles 1102, 1105 or 1110 of the NAFTA or otherwise;

2) DISMISSES Thunderbird's claims in their entirety;

3) DETERMINES the costs of the arbitration referred to in ¶ 221 above at US$505,252.08, and further DETERMINES that these costs are to be shared by the Thunderbird and Mexico on a 3/4-1/4 basis, and are to be paid out of the deposits made by the Parties;

4) DETERMINES that Thunderbird shall reimburse Mexico in the amount of US$ 1,126,549.38 in respect of the costs of legal representation and US$126,313.02 in respect of the deposits made by Mexico for the fees and disbursements of the Arbitral Tribunal.

INTERNATIONAL CENTRE FOR THE SETTLEMENT OF INVESTMENT DISPUTES (ADDITIONAL FACILITY)

Washington D.C.

Case N° ARB(AF)/00/3

Waste Management, Inc.

(Claimant)

versus

United Mexican States

(Respondent)

AWARD

Before the Arbitral Tribunal
constituted under Chapter Eleven
of the North American Free Trade
Agreement, and comprised of:

Professor James Crawford, President
Mr. Benjamin R. Civiletti
Mr. Eduardo Magallón Gómez

Secretary of the Tribunal

Ms. Gabriela Alvarez Avila

Date of dispatch to the parties: April 30, 2004

legal issues in turn, dealing with the facts (and with any factual disputes) as far as necessary for the purpose.

(2) The status of the Claimant as an "investor"

77. At the time it was incorporated, Acaverde was owned, through a holding company called AcaVerde Holdings Ltd, by Sun Investment Co., a Cayman Islands company. AcaVerde Holdings Ltd., also a Cayman Islands company, was purchased by Sanifill Inc., a U.S. company ("Sanifill"), at about the time the City initially approved the concession. The sale agreement of 21 December 1994 was contingent upon conclusion of the Concession Agreement and the Line of Credit Agreement. In fact the sale was completed on 27 June 1995. The price paid, in instalments, was US$5 million, plus the right to certain royalties based on Acaverde's operations. Subsequently, in August 1996, Sanifill merged with USA Waste Services Inc.; the merged company later adopted the name Waste Management Inc.

78. A number of witnesses presented by the Respondent asserted that the City was not aware at the time the Concession Agreement was negotiated that Acaverde was not owned by Sanifill. The Claimant's witnesses asserted that they had informed the City of this fact. The Tribunal does not need to resolve the discrepancy. Although the City may not have been aware of the specific financial arrangements between Sun Investments and Sanifill, it was certainly aware that United States interests were involved in the proposed arrangement,[26] as was reported in the local press at the time.[27] The Concession Agreement was signed by Mr. Proto, a senior employee of Sanifill, under a power of attorney granted by Acaverde. As noted, the actual purchase of Acaverde's stock was contingent upon the conclusion of the Line of Credit Agreement, without which the project would not have gone ahead. By the time Acaverde commenced operations on 15 August 1995, almost all its shares were owned, through Cayman Islands companies, by Sanifill.[28]

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[26] Mr. Walton, transcript, 7 April 2003, 233.

[27] *Novedades* (Acapulco), 30 October 1994, identifying Sanifill Inc. as the prospective concessionaire.

[28] On 30 November 1995, a merger agreement left Sanifill de Mexico, S.A. de C.V., a Mexican company, as the sole successor of the various intermediate holding companies of Aceverde, the ultimate controlling interest of which was in Sanifill.

action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency".[41]

94. The discussion of Article 1105 by the tribunal in *S.D. Myers*, even though before the FTC interpretation, may also be noted. The tribunal considered that a breach of Article 1105 occurs

> "only when it is shown that an investor has been treated in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective. That determination must be made in the light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders. The determination must also take into account any specific rules of international law that are applicable to the case."[42]

95. In the context of denial of justice arising from decisions of domestic courts, the *Mondev* tribunal formulated the test of the applicable "customary international law minimum standard" under Article 1105(1) in the following terms:

> "The test is not whether a particular result is surprising, but whether the shock or surprise occasioned to an impartial tribunal leads, on reflection, to justified concerns as to the judicial propriety of the outcome, bearing in mind on the one hand that international tribunals are not courts of appeal, and on the other hand that Chapter 11 of NAFTA (like other treaties for the protection of investments) is intended to provide a real measure of protection. In the end the question is whether, at an international level and having regard to generally accepted standards of the administration of justice, a tribunal can conclude in the light of all the available facts that the impugned decision was clearly improper and discreditable, with the result that the investment has been subjected to unfair and inequitable treatment."[43]

96. The *ADF* tribunal, citing *Mondev v. United States*, said of Article 1105 as interpreted by the FTC[44] that "any general requirement to accord 'fair and equitable treatment' and 'full protection and security' must be disciplined by being based on State

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41 *USA (L.F. Neer) v. United Mexican States*, 1927, AJIL 555, at 556, cited in *Mondev*, 221 (para. 114).

42 *S.D. Myers, Inc. v. Government of Canada*, Partial Award, 13 November 2000, para. 263. The majority (Arbitrator Chiasson dissenting) considered that the facts which supported a finding of breach of Article 1102 also established a breach of Article 1105, para. 266.

43 *Mondev v. United States*, 225-6 (para. 127).

44 Ibid., 528-31 (paras. 180, 183-4).

practice and judicial or arbitral caselaw or other sources of customary or general international law."[45] Considering the "general customary international law standard of treatment", the Tribunal found that:

- the argument that the government procurement provisions were unfair was unconvincing. Performance requirements in governmental procurement were common to all three NAFTA Parties as well as to other States. Thus "the US measures cannot be characterized as idiosyncratic or aberrant and arbitrary"; [46]
- the actions of a government authority in refusing to follow and apply earlier case-law was not in the circumstances of the case "grossly unfair or unreasonable", nor were ADF's assumptions about the applicability of that case-law induced by the misrepresentations by authorised officials of government;[47]
- the government agency in question had not acted *ultra vires*, but, in any case, showing an act is *ultra vires* under the internal law of a state "by itself does not necessarily render the measures grossly unfair or inequitable under the customary international law standard of treatment embodied in Article 1105(1)… something more than simple illegality or lack of authority under the domestic law of a State is necessary";[48]
- the investor's claim that the United States had breached its duty under customary international law to perform its obligations in good faith in breach of Article 1105 added "only negligible assistance in the task of determining or giving content to a standard of fair and equitable treatment."[49] However the Tribunal noted in this respect that the investor had not tried to show government actions refusing the request for a waiver of the procurement requirements were "flawed by arbitrariness". There was no evidence that other companies had been granted the same waivers. The investor did not allege that the contract specifications were tailored so that only a specific US company could comply; nor did the investor show that extraordinary costs or other burdens had been imposed that were not also imposed on other contractors involved in the same project.

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45 Ibid., 531 (para. 184).

46 Ibid., 531 (para. 188).

47 Ibid., 531-2 (para. 189).

48 Ibid., 532-3 (para. 190).

49 Ibid., 533 (para. 191).

97. The content of Article 1105 in light of the FTC interpretation was also discussed in *Loewen v. United States* in the specific context of denial of justice.[50] The tribunal said:

> "Neither State practice, the decisions of international tribunals nor the opinion of commentators support the view that bad faith or malicious intention is an essential element of unfair and inequitable treatment or denial of justice amounting to a breach of international justice. Manifest injustice in the sense of a lack of due process leading to an outcome which offends a sense of judicial propriety is enough, even if one applies the Interpretation according to its terms."[51]

The *Loewen* Tribunal also noted that discriminatory violations of municipal law would amount to a manifest injustice according to international law.[52] However, the tribunal held that, where the minimum standards of international law in question in a particular case are raised in respect of a claim of judicial action—that is, a denial of justice—what matters is the *system* of justice and not any individual decision in the course of proceedings. The system must be tried and have failed, and thus in this context the notion of exhaustion of local remedies is incorporated into the substantive standard and is not only a procedural prerequisite to an international claim.[53] For this reason, although the *Loewen* tribunal found that the first instance trial and its verdict were "clearly improper and discreditable" and a breach of the minimum standards of fair and equitable treatment, that did not dispose of the case.[54]

98. The search here is for the Article 1105 standard of review, and it is not necessary to consider the specific results reached in the cases discussed above. But as this survey shows, despite certain differences of emphasis a general standard for Article 1105 is emerging. Taken together, the *S.D. Myers*, *Mondev*, *ADF* and *Loewen* cases suggest that the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary,

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50 *The Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, Award of 26 June 2003 (Case No. ARB(AF)/98/3). For the Tribunal's discussion of the Article 1105 and the FTC interpretation see ibid., paras. 124-8.

51 Ibid., para. 132.

52 Ibid., para. 135.

53 Ibid., para. 168.

54 Ibid., para. 137.

grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.

99. Evidently the standard is to some extent a flexible one which must be adapted to the circumstances of each case. Accordingly it is to the facts of the present case that the Tribunal turns.

(ii) The allegations of breach of Article 1105(1)

100. The Claimant asserted that the failure of Acaverde's enterprise arose from a combination of conduct of local, provincial and federal authorities, together with the failure of Mexican courts and tribunals to provide it any relief. In the first place the Tribunal will consider separately the conduct of each of the various Mexican authorities concerned. Subsequently it will deal with the claim that there was collusion or conspiracy between these authorities.

101. Before turning to the specific facts, the Tribunal notes that an important part of the background to the case was the Mexican financial crisis, which started in December 1994 with a substantial devaluation of the currency and continued for several years. During that period the value of the peso was approximately halved, the rate of inflation reached 38%, and federal revenues to the States and municipalities were greatly affected.[55] The effects on the City were numerous: tourist numbers declined, its financial obligations under the Concession Agreement (which were indexed to inflation) were substantially increased[56] and the federal revenues it received were substantially reduced.

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55 See William A. Lovett, "Lessons from the Recent Peso Crisis in Mexico", (1996) 4 *Tulane JICL* 143.

56 The monthly fee increased from NP1 million to NP1.6 million in January 1996.

143. It may be noted that Article 1110(1) distinguishes between direct or indirect expropriation on the one hand and measures tantamount to an expropriation on the other. An indirect expropriation is still a taking of property. By contrast where a measure tantamount to an expropriation is alleged, there may have been no actual transfer, taking or loss of property by any person or entity, but rather an effect on property which makes formal distinctions of ownership irrelevant. This is of particular significance in the present case, at least as concerns the enterprise of Acaverde as a whole.

144. Evidently the phrase "take a measure tantamount to nationalization or expropriation of such an investment" in Article 1110(1) was intended to add to the meaning of the prohibition, over and above the reference to indirect expropriation. Indeed there is some indication that it was intended to have a broad meaning, otherwise it is difficult to see why Article 1110(8) was necessary. As a matter of international law a "non-discriminatory measure of general application" in relation to a debt security or loan which imposed costs on the debtor causing it to default would not be considered expropriatory or even potentially so. It is true that paragraph (8) is stated to be "for greater certainty", but if it was necessary even for certainty's sake to deal with such a case this suggests that the drafters entertained a broad view of what might be "tantamount to an expropriation".

145. Thus there is some textual basis for the Claimant's submission that "the modern definition of 'expropriation' must be broad enough to encompass every course of sovereign conduct that unfairly destroys a foreign investor's contractual rights as an asset".[96] The Claimant relied on a number of decisions in support of this proposition, and a review of these is first called for.

146. *LETCO v. Liberia*[97] concerned a 1970 concession agreement between LETCO and the Liberian government which gave LETCO, a Liberian company owned by French nationals, the exclusive right to harvest, process, transport and market forest products and to conduct other timber operations within an exclusive exploitation area, in

[96] Reply, para. 4.23.

[97] *Liberian Eastern Timber Corporation [LETCO] v. Government of the Republic of Liberia* (1986) 2 ICSID Reports 343.

[185]

AWARD

For the foregoing reasons, the Tribunal unanimously DECIDES:

(a) That the claim is admissible under Chapter 11 of NAFTA;

(b) That the conduct of the Respondent which is the subject of the claim did not involve any breach of Article 1105 or 1110 of NAFTA;

(c) That Waste Management's claim is accordingly dismissed in its entirety;

(d) That each Party shall bear its own costs and half of the costs and expenses of these proceedings.

Done at Washington, D.C. in English and Spanish, both versions being equally authoritative.

Professor James Crawford
President of the Tribunal

Mr. Benjamin R. Civiletti
Member

Mr. Eduardo Magallón Gómez
Member

INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
Washington, D.C.

In accordance with the
United Nations Commission on International Trade Law (UNCITRAL)
Arbitration Rules

Glamis Gold, Ltd.
(Claimant)

- AND -

United States of America
(Respondent)

AWARD

Before the Arbitral Tribunal constituted under Chapter 11
of the North American Free Trade Agreement, and comprised of:

Michael K. Young
Professor David D. Caron
Kenneth D. Hubbard

Secretary of the Tribunal
Ms. Eloïse Obadia

Legal Assistant to the Tribunal
Ms. Leah D. Harhay

Date of dispatch to the parties: June 8, 2009

of custom involves not only questions of law but also questions of fact, where custom is found in the practice of States regarded as legally required by them.[20] The content of a particular custom may be clear; but where a custom is not clear, or is disputed, then it is for the party asserting the custom to establish the content of that custom.[21]

21. In the case of the customary international law standard of "fair and equitable treatment," the Parties in this case and the other two NAFTA State Parties agree that the customary international law standard is at least that set forth in the 1926 *Neer* arbitration.[22] The Parties disagree, however, as to how that customary standard has in fact, if at all, evolved since that time. As an evidentiary matter, the evolution of a custom is a proposition to be established. The Tribunal acknowledges that the proof of change in a custom is not an easy matter to establish. In some cases, the evolution of custom may be so clear as to be found by the tribunal itself. In most cases, however, the burden of doing so falls clearly on the party asserting the change.[23]

22. In the instant case, the Tribunal finds that Glamis fails to establish the evolution in custom it asserts to have occurred. It thus appears that, although situations presented to tribunals are more varied and complicated today than in the 1920s, the level of scrutiny required under *Neer* is the same. Given the absence of sufficient evidence to establish a change in the custom, the fundamentals of the *Neer* standard thus still apply today: to violate the customary international law minimum standard of treatment codified in Article 1105 of the NAFTA, an act must be sufficiently egregious and shocking—a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination, or a manifest lack of reasons—so as to fall below accepted international standards and constitute a breach of Article 1105(1). Such a breach may be exhibited by a "gross denial of justice or manifest arbitrariness falling below acceptable international standards;" or the creation by the State of objective expectations *in order to induce* investment and the subsequent repudiation of those

[20] *See infra* ¶¶ 607-11.
[21] *See infra* ¶¶ 601-05.
[22] *See infra* ¶ 612.
[23] *See infra* ¶¶ 601-05.

expectations.[24] The Tribunal emphasizes that, although bad faith may often be present in such a determination and its presence will certainly be determinative of a violation, a finding of bad faith is not a requirement for a breach of Article 1105(1).[25] The Tribunal further finds that although the standard for finding a breach of the customary international law minimum standard of treatment therefore remains as stringent as it was under *Neer*; it is entirely possible that, as an international community, we may be shocked by State actions now that did not offend us previously.[26]

23. Respondent additionally argues that, in reviewing State agency or departmental decisions and actions, international tribunals, as well as domestic judiciaries, should defer to the agency so as not to second guess the primary decision-makers. The Tribunal disagrees that domestic deference in national court systems is necessarily applicable to international tribunals particularly where a measure of deference is already present in the standard to be applied.[27]

24. With this standard (as elaborated in this Award) in mind, the Tribunal finds that the acts of the federal government and the State of California complained of by Glamis do not, either individually or collectively, violate the Article 1105 obligations of the United States. Specifically, the Tribunal finds the following measures did not violate Respondent's international obligations under Article 1105:

- A legal opinion by the Department of the Interior did not breach Respondent's obligations under Article 1105, because it was not arbitrary or manifestly without reasons; was not blatantly unfair or evidently discriminatory; nor did it repudiate expectations formed by a quasi-contractual relationship or evidence a complete lack of due process.[28]

[24] *See infra* ¶¶ 616, 627. The Tribunal takes no position on the type or nature of repudiation measures that would be necessary to violate international obligations. As the Tribunal holds below, Claimant has not proved governmental actions that would have legitimately created such expectations; the Tribunal therefore need not and does not reach the latter half of the inquiry. *See infra,* ¶ 622.
[25] *Id.*
[26] *Id.*
[27] *See infra* ¶ 617.
[28] *See infra* ¶¶ 758-72.

- The Record of Decision denying Claimant's Plan of Operations did not breach international obligations as it was based upon the above-mentioned legal opinion which was in compliance with Respondent's international obligations.[29]

- With respect to the asserted delay in the federal government's review of Claimant's Plan of Operations, the Tribunal finds that, prior to Claimant's submission to arbitration, there was no delay in the processing; and Respondent's subsequent failure to diligently pursue administrative review while also defending an arbitration with respect to the same review is not manifestly arbitrary, completely lacking in due process, exhibiting evident discrimination, or manifestly lacking in reasons.[30]

- The cultural review of Claimant's Plan of Operations did not breach Article 1105, as it was undertaken by qualified professionals who provided their reasoned and substantiated opinions upon which Respondent was justified in relying, and was not harmed by bias or prejudice. In addition, the conclusion of the cultural review culminating in direct recommendation to the secretary of Interior was not manifestly arbitrary, a gross denial of justice, or exhibiting a manifest lack of reasons.[31]

- The complained of California legislation was of general application and did not target Claimant's investment, though it is likely that the investment served as a triggering event.[32] The legislation also did not breach Respondent's obligations to protect investor expectations, as such expectations were not created by specific assurances;[33] nor was it arbitrary in that it is clear from the record that the legislation addressed some, if not all, of the harms at issue.[34]

- The California regulations, and the emergency regulations that preceded them, did not upset reasonable investor expectations as such expectations were not created

[29] *See infra* ¶ 772.
[30] *See infra* ¶¶ 773-77.
[31] *See infra* ¶¶ 778-88.
[32] *See infra* ¶¶ 791-97.
[33] *See infra* ¶¶ 798-802.
[34] *See infra* ¶¶ 803-06.

by specific assurances.[35] The Tribunal also finds that there was a rational relationship between the regulations and their purpose and sufficient scientific study to support the Board's conclusions.[36]

- With respect to Claimant's contention that the California measures were closely related acts with the same goal of halting its investment, the Tribunal holds that, even if it were to view the measures as "working together," Claimant has not met its burden of proving to the Tribunal that either measure unfairly targeted its investment.[37]

25. Finally, the Tribunal views the measures of both the federal and state governments together, to see whether the entirety of the conduct breaches international obligations when the individual events do not. The Tribunal determines that, for acts that do not individually violate Article 1105 to nonetheless breach that Article when taken together, there must be some additional quality that exists only when the acts are viewed as a whole, as opposed to individually. It is not clear, in general terms, what such quality would be in all circumstances though, in this factual situation, the Tribunal holds that it cannot see that the conduct as a whole is a violation of the fair and equitable treatment standard.[38]

26. The Tribunal thus dismisses both of the claims by Glamis Gold against the United States. The Tribunal holds that, with respect to the costs of this proceeding, Glamis shall bear two-thirds of the costs and the United States one-third, and each Party should bear its own individual costs of representation.

[35] *See infra* ¶¶ 809-15.
[36] *See infra* ¶¶ 816-18.
[37] *See infra* ¶¶ 819-23.
[38] *See infra* ¶¶ 824-29.

3. DECISION OF THE TRIBUNAL WITH RESPECT TO THE ARTICLE 1105(1) LEGAL STANDARD

598. As noted above, Article 1105(1) of the NAFTA provides 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."

599. There is no disagreement among the State Parties to the NAFTA, nor the Parties to this arbitration, that the requirement of fair and equitable treatment in Article 1105 is to be understood by reference to the customary international law minimum standard of treatment of aliens.[1243] Indeed, the Free Trade Commission ("FTC") clearly states, in its binding Notes of Interpretation on July 31, 2001, that "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."[1244]

600. The question thus becomes: what does this customary international law minimum standard of treatment require of a State Party vis-à-vis investors of another State Party? Is it the same as that established in 1926 in *Neer v. Mexico*?[1245] Or has Claimant proven that the standard has "evolved"? If it has evolved, what evidence of custom has Claimant provided to the Tribunal to determine its current scope?

601. As a threshold issue, the Tribunal notes that it is Claimant's burden to sufficiently answer each of these questions. The State Parties to the NAFTA (at least Canada and Mexico) agree that "the test in *Neer* does continue to apply," though Mexico "also agrees that the standard is relative and that conduct which may not have violated international law [in] the 1920's might very well be seen to offend internationally accepted principles today."[1246] If, as Claimant argues, the customary international law

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[1243] Counsel for Claimant, Tr. 36:15-18; Counsel for Respondent, Tr. 1390:11-14; Free Trade Commission, *Notes of Interpretation of Certain Chapter 11 Provisions*, § B(2) (July 31, 2001) ("FTC Notes").

[1244] *FTC Notes*, § B(1). For further discussion of the binding nature of the FTC Notes, *see* NAFTA Article 1131(2): "An interpretation by the Commission of a provision of this Agreement shall be binding on a Tribunal established under this Section."

[1245] Neer v. Mexico, 4 R. Int'l Arb. Awards, 60 (Oct. 15, 1926).

[1246] *ADF Group*, Second Article 1128 Submission of the United Mexican States, p. 15 (July 22, 2002), quoting *Pope & Talbot*, Post-Hearing Article 1128 Submission of the United Mexican States (Damages Phase), ¶ 8 (Dec. 3, 2001), quoting *Pope & Talbot*, Respondent Canada's Counter-Memorial (Phase 2), ¶ 309 (Aug. 18, 2001) (Mexico's Post-Hearing Article 1128 Submission in *Pope & Talbot* quotes with approval Canada's submission as respondent in *Pope & Talbot*, which states in paragraph 8:

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.

602. The Tribunal acknowledges that it is difficult to establish a change in customary international law. As Respondent explains, establishment of a rule of customary international law requires: (1) "a concordant practice of a number of States acquiesced in by others," and (2) "a conception that the practice is required by or consistent with the prevailing law (*opinio juris*)."[1247]

603. The evidence of such "concordant practice" undertaken out of a sense of legal obligation is exhibited in very few authoritative sources: treaty ratification language, statements of governments, treaty practice (e.g., Model BITs), and sometimes pleadings.[1248] Although one can readily identify the practice of States, it is usually very difficult to determine the intent behind those actions. Looking to a claimant to ascertain custom requires it to ascertain such intent, a complicated and particularly difficult task. In the context of arbitration, however, it is necessarily Claimant's place to establish a change in custom.

604. The Tribunal notes that, although an examination of custom is indeed necessary to determine the scope and bounds of current customary international law, this requirement—repeatedly argued by various State Parties—because of the difficulty in proving a change in custom, effectively freezes the protections provided for in this provision at the 1926 conception of egregiousness.

605. Claimant did provide numerous arbitral decisions in support of its conclusion that fair and equitable treatment encompasses a universe of "fundamental" principles common throughout the world that include "the duty to act in good faith, due process, transparency and candor, and fairness and protection from arbitrariness."[1249] Arbitral awards, Respondent rightly notes, do not constitute State practice and thus cannot create or prove

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"The conduct of government toward the investment must amount to gross misconduct, manifest injustice or, in the classic words of the *Neer* claim, an outrage, bad faith or the willful neglect of duty.").

[1247] Respondent's Counter-Memorial, at 219 (citations omitted).

[1248] In the NAFTA context, there is the addition of Article 1128 submissions through which the State Parties can express directly their views on and interpretations of the provisions of the NAFTA.

[1249] Counsel for Claimant, Tr. 40:1-8.

customary international law.[1250] They can, however, serve as illustrations of customary international law if they involve an examination of customary international law, as opposed to a treaty-based, or autonomous, interpretation.

606. This brings the Tribunal to its first task: ascertaining which of the sources argued by Claimant are properly available to instruct the Tribunal on the bounds of "fair and equitable treatment." As briefly mentioned above, the Tribunal notes that it finds two categories of arbitral awards that examine a fair and equitable treatment standard: those that look to define customary international law and those that examine the autonomous language and nuances of the underlying treaty language. Fundamental to this divide is the treaty underlying the dispute: those treaties and free trade agreements, like the NAFTA, that are to be understood by reference to the customary international law minimum standard of treatment necessarily lead their tribunals to analyze custom; while those treaties with fair and equitable treatment clauses that expand upon, or move beyond, customary international law, lead their reviewing tribunals into an analysis of the treaty language and its meaning, as guided by Article 31(1) of the Vienna Convention.

607. Ascertaining custom is necessarily a factual inquiry, looking to the actions of States and the motives for and consistency of these actions. By applying an autonomous standard, on the other hand, a tribunal may focus solely on the language and nuances of the treaty language itself and, applying the rules of treaty interpretation, require no party proof of State action or *opinio juris*. This latter practice fails to assist in the ascertainment of custom.

608. As Article 1105's fair and equitable treatment standard is, as Respondent phrases it, simply "a shorthand reference to customary international law,"[1251] the Tribunal finds that arbitral decisions that apply an autonomous standard provide no guidance inasmuch as the entire method of reasoning does not bear on an inquiry into custom. The various BITs cited by Claimant may or may not illuminate customary international law; they will prove helpful to this Tribunal's analysis when they seek to provide the same base floor of

[1250] Respondent's Rejoinder, at 151, quoting Robert Cryer, *Of Custom, Treaties, Scholars, and the Gavel: The Influence of the International Criminal Tribunals on the ICRC Customary Law Study*, 11 J. CONFLICT & SECURITY L. 239, 252 (2006) (additional citation omitted).

[1251] Counsel for Respondent, Tr. 1934:9-20.

conduct as the minimum standard of treatment under customary international law; but they will not be of assistance if they include different protections than those provided for in customary international law.

609. Claimant has agreed with this distinction between customary international law and autonomous treaty standards but argues that, with respect to this particular standard, BIT jurisprudence has "converged with customary international law in this area."[1252] The Tribunal finds this to be an over-statement. Certainly, it is possible that some BITs converge with the requirements established by customary international law; there are, however, numerous BITs that have been interpreted as going beyond customary international law, and thereby requiring more than that to which the NAFTA State Parties have agreed. It is thus necessary to look to the underlying fair and equitable treatment clause of each treaty, and the reviewing tribunal's analysis of that treaty, to determine whether or not they are drafted with an intent to refer to customary international law.

610. Looking, for instance, to Claimant's reliance on *Tecmed v. Mexico* for various of its arguments, the Tribunal finds that Claimant has not proven that this award, based on a BIT between Spain and Mexico,[1253] defines anything other than an autonomous standard and thus an award from which this Tribunal will not find guidance. Article 4(1) of the Spain-Mexico BIT involved in the *Tecmed* proceeding provides that each contracting party guarantees just and equitable treatment conforming with "International Law" to the investments of investors of the other contracting party in its territory.[1254] Article 4(2) proceeds to explain that this treatment will not be less favorable than that granted in similar circumstances by each contracting party to the investments in its territory by an investor of a third State.[1255] Several interpretations of the requirement espoused in Article 4(2) are indeed possible, but the *Tecmed* tribunal itself states that it "understands that the scope of the undertaking of fair and equitable treatment under Article 4(1) of the Agreement described ... is that resulting from *an autonomous interpretation* ...."[1256]

[1252] Counsel for Claimant, Tr. 1710:20-22.

[1253] *See Tecmed*, Award, ¶ 4 (May 29, 2003), citing Agreement on the Reciprocal Promotion and Protection of Investments signed by the Kingdom of Spain and the United Mexican States, (Dec. 18, 1996).

[1254] Claimant's Memorial, ¶ 533, footnote 1033, quoting *Tecmed*, Award, ¶ 154 (May 29, 2003).

[1255] Agreement on the Reciprocal Promotion and Protection of Investments signed by the Kingdom of Spain and the United Mexican States, Article 4(2) (Dec. 18, 1996).

[1256] *Tecmed*, Award, ¶ 155 (May 29, 2003) (emphasis added).

Thus, this Tribunal finds that the language or analysis of the *Tecmed* award is not relevant to the Tribunal's consideration.

611. The Tribunal therefore holds that it may look solely to arbitral awards—including BIT awards—that seek to be understood by reference to the customary international law minimum standard of treatment, as opposed to any autonomous standard. The Tribunal thus turns to its second task: determining the scope of the current customary international law minimum standard of treatment, as proven by Claimant.

612. It appears to this Tribunal that the NAFTA State Parties agree that, at a minimum, the fair and equitable treatment standard is that as articulated in *Neer*:[1257] "the treatment of an alien, in order to constitute an international delinquency, should amount to an outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency."[1258] Whether this standard has evolved since 1926, however, has not been definitively agreed upon. The Tribunal considers two possible types of evolution: (1) that what the international community views as "outrageous" may change over time; and (2) that the minimum standard of treatment has moved beyond what it was in 1926.

613. The Tribunal finds apparent agreement that the fair and equitable treatment standard is subject to the first type of evolution: a change in the international view of what is shocking and outrageous. As the *Mondev* tribunal held:

> *Neer* and like arbitral awards were decided in the 1920s, when the status of the individual in international law, and the international protection of foreign investments, were far less developed than they have since come to be. In particular, both the substantive and procedural rights of the individual in international law have undergone considerable development. In light of these developments it is unconvincing to confine the meaning of 'fair and equitable treatment' and 'full protection and security' of foreign investments to what those

[1257] *ADF Group*, Second Article 1128 Submission of the United Mexican States, p. 15 (July 22, 2002), quoting *Pope & Talbot*, Post-Hearing Article 1128 Submission of the United Mexican States (Damages Phase), ¶ 8 (Dec. 3, 2001), quoting *Pope & Talbot*, Respondent Canada's Counter-Memorial (Phase 2), ¶ 309 (Aug. 18, 2001).

[1258] *Neer v. Mexico*, 4 R. Int'l Arb. Awards, ¶ 4 (Oct. 15, 1926). The *Neer* tribunal continued to explain that its inquiry was limited to "whether there [was] convincing evidence either (1) that the authorities administering the Mexican law acted in an outrageous way, in bad faith, in wilful neglect of their duties, or in a pronounced degree of improper action, or (2) that Mexican law rendered it impossible for them properly to fulfil their task." *Id.* ¶ 5.

> terms—had they been current at the time—might have meant in the 1920s when applied to the physical security of an alien. To the modern eye, what is unfair or inequitable need not equate with the outrageous or the egregious. In particular, a State may treat foreign investment unfairly and inequitably without necessarily acting in bad faith.[1259]

Similarly, this Tribunal holds that the *Neer* standard, when applied with current sentiments and to modern situations, may find shocking and egregious events not considered to reach this level in the past.

614. As regards the second form of evolution—the proposition that customary international law has moved beyond the minimum standard of treatment of aliens as defined in *Neer*—the Tribunal finds that the evidence provided by Claimant does not establish such evolution. This is evident in the abundant and continued use of adjective modifiers throughout arbitral awards, evidencing a strict standard. *International Thunderbird* used the terms "*gross* denial of justice" and "*manifest* arbitrariness" to describe the acts that it viewed would breach the minimum standard of treatment.[1260] *S.D. Myers* would find a breach of Article 1105 when an investor was treated "in *such an unjust or arbitrary* manner."[1261] The *Mondev* tribunal held: "The test is not whether a particular result is surprising, but whether the *shock or surprise* occasioned to an impartial tribunal leads, on reflection, to justified concerns as to the judicial propriety of the outcome ...."[1262]

615. The customary international law minimum standard of treatment is just that, a minimum standard. It is meant to serve as a floor, an absolute bottom, below which conduct is not accepted by the international community. Although the circumstances of the case are of course relevant, the standard is not meant to vary from state to state or investor to investor. The protection afforded by Article 1105 must be distinguished from that provided for in Article 1102 on National Treatment. Article 1102(1) states: "Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors ...." The treatment of investors under Article 1102 is compared to the treatment the State's own investors receive and thus can

[1259] *Mondev*, Award, ¶ 116 (Oct. 11, 2002).
[1260] *International Thunderbird*, Award, ¶ 194 (Jan. 26, 2006) (emphasis added).
[1261] *S.D. Myers*, Partial Award, ¶ 263 (Nov. 13, 2000) (emphasis added).
[1262] *Mondev,* Award, ¶ 127 (Oct. 11, 2002) (emphasis added).

vary greatly depending on each State and its practices. The fair and equitable treatment promised by Article 1105 is not dynamic; it cannot vary between nations as thus the protection afforded would have no minimum.

616. It therefore appears that, although situations may be more varied and complicated today than in the 1920s, the level of scrutiny is the same. The fundamentals of the *Neer* standard thus still apply today: to violate the customary international law minimum standard of treatment codified in Article 1105 of the NAFTA, an act must be sufficiently egregious and shocking—a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination, or a manifest lack of reasons—so as to fall below accepted international standards and constitute a breach of Article 1105(1). The Tribunal notes that one aspect of evolution from *Neer* that is generally agreed upon is that bad faith is not required to find a violation of the fair and equitable treatment standard, but its presence is conclusive evidence of such. Thus, an act that is egregious or shocking may also evidence bad faith, but such bad faith is not necessary for the finding of a violation. The standard for finding a breach of the customary international law minimum standard of treatment therefore remains as stringent as it was under *Neer*; it is entirely possible, however that, as an international community, we may be shocked by State actions now that did not offend us previously.

617. Respondent argues below that, in reviewing State agency or departmental decisions and actions, international tribunals as well as domestic judiciaries favor deference to the agency so as not to second guess the primary decision-makers or become "science courts." The Tribunal disagrees that domestic deference in national court systems is necessarily applicable to international tribunals. In the present case, the Tribunal finds the standard of deference to already be present in the standard as stated, rather than being additive to that standard. The idea of deference is found in the modifiers "manifest" and "gross" that make this standard a stringent one; it is found in the idea that a breach requires something greater than mere arbitrariness, something that is surprising, shocking, or exhibits a manifest lack of reasoning.

618. With this thought in mind, the Tribunal turns to the duties that Claimant argues are part of the requirements of a host State per Article 1105: (1) an obligation to protect

legitimate expectations through establishment of a transparent and predictable business and legal framework, and (2) an obligation to provide protection from arbitrary measures. As the United States explained in its 1128 submission in *Pope & Talbot*, and as Mexico adopted in its 1128 submission to the *ADF* tribunal: "'fair and equitable treatment' and 'full protection and security' are provided as examples of the customary international law standards incorporated into Article 1105(1). … The international law minimum standard [of treatment] is an umbrella concept incorporating a set of rules that has crystallized over the centuries into customary international law in specific contexts."[1263] The Tribunal therefore finds it appropriate to address, in turn, each of the State obligations Claimant asserts are potential parts of the protection afforded by fair and equitable treatment.

a. Asserted Obligation to Protect Legitimate Expectations Through Establishment of a Transparent and Predictable Legal and Business Framework

619. As explained above, the minimum standard of treatment of aliens established by customary international law, and by reference to which the fair and equitable treatment standard of Article 1105(1) is to be understood, is an absolute minimum, a floor below which the international community will not condone conduct. To maintain fair and equitable treatment as an absolute floor, a breach must be based upon objective criteria that apply equally among States and between investors.

620. The Tribunal notes Respondent's argument that even those expectations that manifest in a contract are insufficient to provide a basis for a breach of the minimum standard of treatment.[1264] The Tribunal agrees that mere contract breach, without something further such as denial of justice or discrimination, normally will not suffice to establish a breach of Article 1105.[1265] Merely not living up to expectations cannot be sufficient to find a breach of Article 1105 of the NAFTA. Instead, Article 1105(1)

[1263] *ADF Group*, Second Article 1128 Submission of the United Mexican States, p. 8 (July 22, 2002), quoting *Pope & Talbot*, Fourth Article 1128 Submission of the United States, ¶¶ 3, 8 (Nov. 1, 2000).

[1264] Counsel for Respondent, Tr. 1397:15-18; Respondent's Rejoinder, at 180.

[1265] *See* Azinian v. United Mexican States ("*Azinian*"), NAFTA/ICSID Case No. ARB/(AF)/97/2, Award, ¶ 87 (Nov. 1, 1999) (holding, "NAFTA does not, however, allow investors to seek international arbitration for mere contractual breaches. Indeed, NAFTA cannot possibly be read to create such a regime, which would have elevated a multitude of ordinary transactions with public authorities into potential international disputes.").

requires the evaluation of whether the State made any specific assurance or commitment to the investor so as to induce its expectations.[1266]

621. The Tribunal therefore agrees with *International Thunderbird* that legitimate expectations relate to an examination under Article 1105(1) in such situations "where a Contracting Party's conduct creates reasonable and justifiable expectations on the part of an investor (or investment) to act in reliance on said conduct …."[1267] In this way, a State may be tied to the objective expectations that it creates *in order to induce* investment.

622. As the Tribunal determines below that no specific assurances were made to induce Claimant's "reasonable and justifiable expectations," the Tribunal need not determine the level, or characteristics, of state action in contradiction of those expectations that would be necessary to constitute a violation of Article 1105.

b. Asserted Obligation to Provide Protection from Arbitrary Measures

623. With respect to the asserted duty to protect investors from arbitrariness, the Tribunal notes Claimant's citations to several NAFTA arbitrations that have found a violation of Article 1105 in arbitrary state action. Claimant cites to *S.D. Myers* for its holding that "a breach of Article 1105 occurs only when it is shown that an investor has been treated in such an unjust and arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective."[1268] Similarly, it quotes *International Thunderbird*'s holding that "manifest arbitrariness falling below acceptable international standards" is prohibited under Article 1105.[1269]

624. The Tribunal also notes, however, Respondent's argument that no Chapter 11 tribunal has found that decision-making that appears arbitrary to some parties is sufficient to constitute an Article 1105 violation.[1270] In *Mondev*, for instance, the tribunal held: "The test is not whether a particular result is surprising, but whether the shock or surprise occasioned to an impartial tribunal leads, on reflection, to justified concerns as to the

[1266] *Methanex*, Final Award, Part IV, Ch. D, ¶ 7 (Aug. 3, 2005).
[1267] *International Thunderbird*, Award, ¶ 147 (Jan. 26, 2006) (internal citation omitted).
[1268] Claimant's Reply Memorial, ¶ 239, quoting *S.D. Myers*, Partial Award, ¶ 263 (Nov. 13, 2000).
[1269] *Id.*, citing *International Thunderbird*, Award, ¶ 194 (Jan. 26, 2006).
[1270] Respondent's Counter-Memorial, at 227.

judicial propriety of the outcome ….”[1271] Respondent understands this to be the case because tribunals consistently afford administrative decision-making a high level of deference.[1272] Respondent quotes *S.D. Myers* to illustrate this deference: “determination [that Article 1105 has been breached] must be made in light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders.”[1273] This, Respondent argues, leads to the result that merely imperfect legislation or regulation does not give rise to State responsibility under customary international law.[1274]

625. The Tribunal finds that, in this situation, both Parties are correct. Previous tribunals have indeed found a certain level of arbitrariness to violate the obligations of a State under the fair and equitable treatment standard. Indeed, arbitrariness that contravenes *the* rule of law, rather than *a* rule of law, would occasion surprise not only from investors, but also from tribunals.[1275] This is not a mere appearance of arbitrariness, however—a tribunal’s determination that an agency acted in a way with which the tribunal disagrees or that a state passed legislation that the tribunal does not find curative of all of the ills presented; rather, this is a level of arbitrariness that, as *International Thunderbird* put it, amounts to a “gross denial of justice or manifest arbitrariness falling below acceptable international standards.”[1276]

626. The Tribunal therefore holds that there is an obligation of each of the NAFTA State Parties inherent in the fair and equitable treatment standard of Article 1105 that they do not treat investors of another State in a *manifestly* arbitrary manner. The Tribunal thus determines that Claimant has sufficiently substantiated its arguments that a duty to protect investors from arbitrary measures exists in the customary international law minimum standard of treatment of aliens; though Claimant has not sufficiently rebutted Respondent’s assertions that a finding of arbitrariness requires a determination of some act far beyond the measure’s mere illegality, an act so manifestly arbitrary, so unjust and surprising as to be unacceptable from the international perspective.

[1271] *Mondev*, Award, ¶ 127 (Oct. 11, 2002).
[1272] Respondent’s Counter-Memorial, at 227.
[1273] *Id.* at 230, quoting *S.D. Myers*, Partial Award, ¶ 263 (Nov. 13, 2000).
[1274] Respondent’s Rejoinder, at 188.
[1275] *ELSI*, Judgment, ¶ 128 (July 28, 1989).
[1276] *International Thunderbird*, Award, ¶ 194 (Jan. 26, 2006).

4. FINAL DISPOSITION OF THE TRIBUNAL WITH RESPECT TO THE SCOPE OF THE FAIR AND EQUITABLE LEGAL STANDARD

627. The Tribunal holds that Claimant has not met its burden of proving that something other than the fundamentals of the *Neer* standard apply today. The Tribunal therefore holds that a violation of the customary international law minimum standard of treatment, as codified in Article 1105 of the NAFTA, requires an act that is sufficiently egregious and shocking—a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination, or a manifest lack of reasons—so as to fall below accepted international standards and constitute a breach of Article 1105. Such a breach may be exhibited by a "gross denial of justice or manifest arbitrariness falling below acceptable international standards;"[1277] or the creation by the State of objective expectations *in order to induce* investment and the subsequent repudiation of those expectations.[1278] The Tribunal emphasizes that, although bad faith may often be present in such a determination and its presence certainly will be determinative of a violation, a finding of bad faith is not a requirement for a breach of Article 1105(1).

B. DETERMINATION OF WHETHER THE FACTS ALLEGED VIOLATE THE ARTICULATED LEGAL STANDARD OF ARTICLE 1105(1)

628. Claimant argues, as part of its claim under Article 1105 of the NAFTA, that in "determining whether the Respondent's conduct rises to the level of a breach of Article 1105, the Tribunal should consider the entirety of its conduct rather than focusing on individual aspects of that conduct."[1279] Quoting *GAMI*, Claimant asserts that "[t]he record as a whole—not isolated events—determines whether there has been a breach of international law."[1280] To support its claim that the entirety of the United States federal and California State actions worked together to violate Claimant's rights under Article 1105, however, Claimant discusses the individual federal and State actions—and their

[1277] *Id.*

[1278] The Tribunal takes no position on the type or nature of repudiation measures that would be necessary to violate international obligations. As the Tribunal held above, Claimant has not proved governmental actions that would have legitimately created such expectations; the Tribunal therefore need not and does not reach the latter half of the inquiry.

[1279] Claimant's Memorial, ¶ 556.

[1280] *Id.*, quoting *GAMI Investments,* Final Award, ¶ 97 (Nov. 15, 2004).

VIII. AWARD AND ORDER

834. For the foregoing reasons, the Tribunal awards and orders as follows:

835. Denies Claimant's claim under Article 1110 of the NAFTA;

836. Denies Claimant's claim under Article 1105 of the NAFTA;

837. Orders Claimant to pay 2/3 of the arbitral costs and Respondent to pay 1/3 of the arbitral costs; this results in a reimbursement of funds expended by Respondent to ICSID to be determined by ICSID and paid by Claimant; and each Party to bear to its own costs of representation;

838. Denies all other claims for compensation.

Done in Washington, D.C.

Michael K. Young
President
Date: May 14, 2009

Professor David D. Caron
Arbitrator
Date: May 7, 2009

Kenneth D. Hubbard
Arbitrator
Date: May 7, 2009

Subject to the Separate Statement Included in the Award (Footnote 1044)

INTERNATIONAL CENTRE FOR THE SETTLEMENT OF

INVESTMENT DISPUTES

(ADDITIONAL FACILITY)

Washington, D.C.

(ICSID Case No. ARB(AF)/05/2)

Cargill, Incorporated

(Claimant)

- AND -

United Mexican States

(Respondent)

AWARD

Before the Arbitral Tribunal
constituted under Chapter 11
of the North American Free Trade
Agreement, and comprised of:

Dr. Michael C. Pryles
Professor David D. Caron
Professor Donald M. McRae

Secretary of the Tribunal
Mr. Gonzalo Flores

Legal Assistant to the Tribunal
Ms. Leah D. Harhay

Date of dispatch to the parties: 18 September 2009

claim. The Tribunal does not consider this to be so. The Notice of Intent to Submit a Claim to Arbitration served by Claimant specifically complains of the import permit measure (*see* paragraph 171 above).

Conclusion of the Tribunal with respect to Jurisdiction

184. For all the foregoing reasons the Tribunal decides that it possesses jurisdiction to hear the dispute.

VII. ARTICLE 1102 – NATIONAL TREATMENT

Issue Presented

185. Claimant argues that Mexico's measures violate NAFTA Article 1102. Specifically, the IEPS Tax was imposed on "all soft drinks containing HFCS, all of which was supplied by U.S.-owned companies" and not imposed on soft drinks sweetened with cane sugar, all of which was supplied by domestic sugar producers. In addition, Claimant argues that Mexico's import permit requirement and the failure to issue a permit to Cargill "disadvantaged Cargill to the benefit of Mexican domestic sugar producers." Claimant also points out that the fact that the IEPS Tax neither names HFCS nor singles out foreign investors is irrelevant, as the obligation under Article 1102 relates to *de facto* as well as *de jure* discrimination.

186. Respondent counters that there has been no violation of Article 1102. Claimant, it says, is confusing obligations under Article 1102 with obligations under NAFTA Article 301, incorporating GATT Article III, which deals with national treatment in relation to goods and which, Respondent argues, requires an analysis that is different from that required under NAFTA Article 1102. Further, Respondent claims, the IEPS Tax did not discriminate on the basis of nationality, a requirement for discrimination under Article 1102; nor, Respondent asserts, was Cargill de Mexico in "like circumstances" with Mexican sugar producers.

187. The relevant paragraphs of NAFTA Article 1102 provide:

> 1. Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.

> 2. Each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords, in like circumstances, to investments of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.

188. Article 1102 mandates non-discrimination in respect of both "investors" (paragraph 1) and their "investments" (paragraph 2). Claimant takes the view that Respondent has failed to comply with both paragraphs of Article 1102. That is to say, the IEPS Tax and the import permit requirement constituted less favourable treatment both for the investor Cargill and its investment Cargill de Mexico.

189. In the case of both the investor and the investment, there are two basic requirements for a successful claim to be brought under Article 1102: that the investor or the investment be in "like circumstances" with domestic investors or their investments, and that the treatment accorded to the investor or the investment be less favourable than the treatment accorded to domestic investors or their investments. A further requirement of Article 1102 is that the treatment must be "with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments." The Tribunal will deal first with the "like circumstances" requirement. It will then address each of the two further requirements, in turn.

"Like Circumstances"

Contentions of the Parties with respect to "Like Circumstances"

190. Claimant argues that Cargill and its investment Cargill de Mexico are in "like circumstances" with Mexican domestic sugar producers because they operate "in the same business or economic sector." They were, in Claimant's view, supplying a "functionally interchangeable product to the same customers in the same sector of the economy for the same business purpose." Claimant points to the decision of the WTO panel in *Mexico-Tax Measures on Soft Drinks and Other Beverages*, which found HFCS and sugar to be "directly competitive or substitutable" products within the meaning of GATT Article III.

191. Respondent's response is that Claimant has confused the notion of "like products" in respect of goods under GATT Article III with the notion of "like circumstances" in

NAFTA Article 1102. Relying on the award in the *Methanex* case, in which the tribunal stated that Article 1102 must be read on its own terms and not as if the notion of "like, directly competitive or substitutable goods" was incorporated into it, Respondent argues that, just because the products sugar and HFCS compete in the same market, does not mean that the distributors of sugar and the distributors of HFCS are in "like circumstances". Respondent cites in particular to the decisions in *GAMI* and *Pope & Talbot* to show that, even though investors and domestic producers are producing the same product, they may still not be in "like circumstances".

192. In its Reply, Claimant rejects Respondent's view that there is no relationship between "like circumstances" in Article 1102 and "like goods" or "like services" found elsewhere in the NAFTA and GATT, citing cases under the NAFTA (*SD Myers* and *Cross Border Trucking Services*) where the concepts of "like goods" and "like services" were referred to in the interpretation of Article 1102. "Like goods", Claimant argues, is an important component of "like circumstances".

Conclusion of the Tribunal with respect to "Like Circumstances"

193. The Tribunal accepts that "like circumstances" in Article 1102 has to be interpreted on its own terms. Article 1102 requires that no less favourable treatment be provided when foreign investors and domestic investors are in "like circumstances". It does not refer to "like products" and there cannot be an automatic transfer of GATT law relating to "like products" to the Article 1102 term "like circumstances". If the drafters of NAFTA Chapter 11 had intended to equate "like circumstances" with "like products" they could have done so. In this respect, this Tribunal agrees with the tribunal in *Methanex.*[18] The Tribunal thus concludes that the State Parties did not intend that "like circumstances" have a special meaning in the sense of Article 31(4) of the Vienna Convention on the Law of Treaties, but rather that it should be interpreted in accordance with Article 31(1) of the Vienna Convention, that is, the "ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

[18] *Methanex*, Final Award on Jurisdiction and Merits, Final Award on Jurisdiction and Merits, Part IV, Ch. B, ¶¶ 33-34 (3 Aug. 2005).

194. It thus follows that, although as Claimant suggests "like goods" or "like products" can be an important component of "like circumstances", the fact that an investor is producing a good that is "like" a domestically produced good does not necessarily mean that the investor is in "like circumstances" with the domestic producer of that good. Thus, the fact that a WTO panel in *Mexico-Tax on Soft Drinks* concluded that cane sugar and HFCS are "directly competitive or substitutable" products is relevant but not determinative of whether the producers of these products are in "like circumstances" for the purposes of Article 1102.

195. In this regard, the approach of the Tribunal is in accord with that in *GAMI* and *Pope & Talbot*. In each of these cases, the investor and domestic producers were not in "like circumstances" even though they produced the same product and competed in the same market. Thus, something more than the likeness of goods being produced has to be shown in order to establish that the investor and domestic producers are in "like circumstances", particularly where there are other factors that potentially differentiate the situation of the investor or its investment from that of domestic producers of the "like goods" in question.

196. The Tribunal also notes that the IEPS Tax was applied to soft drinks containing HFCS, not to HFCS directly. Although the Tax had an impact on Claimant as a producer of HFCS in the United States and an exporter of HFCS to Mexico, as pointed out above, that effect is not something that can be the subject of a NAFTA Chapter 11 claim. The relevant impact of the Tax on Cargill as an investor was through its investment, Cargill de Mexico, which supplied HFCS to soft drink bottlers in Mexico. Hence, the question under the Article 1102 claim is whether Claimant's investment, Cargill de Mexico, was in "like circumstances" with domestic investments. More particularly, was Cargill de Mexico, as a supplier of HFCS to the soft drink industry, in "like circumstances" with domestic suppliers of cane sugar to the soft drink industry?

197. Respondent cites three reasons for its contention that Cargill de Mexico and domestic sugar suppliers were not in "like circumstances". First, Cargill de Mexico is a distributor of diverse products whereas Mexican sugar producers are limited to one product. Second, the market for sugar is highly regulated, but the market for HFCS is not. Third, the sugar industry was devastated economically, but the HFCS industry was not.

198. Claimant rejects each of these arguments. First, the fact that Cargill de Mexico distributes a variety of products is irrelevant because this case is about one product owned by Mexican nationals and one product owned by U.S. nationals. Second, the claim that the market for sugar is more highly regulated is neither pertinent nor proved. Third, the claim that sugar was more vulnerable "misses the point" because both products competed for the business of soft drink bottlers.

199. With respect to the first reason advanced by Respondent, the Tribunal fails to see the relevance of the diversity of Cargill de Mexico's business. The question is whether, *in respect of its HFCS business*, Cargill de Mexico was in "like circumstances" with domestic sugar producers. The fact that Cargill de Mexico engaged in business other than the distribution of HFCS to the soft drink industry, or the fact that domestic suppliers of cane sugar engaged in businesses other than the supply of sugar to the soft drinks industry, does not appear to the Tribunal to prevent Cargill de Mexico, as a supplier of HFCS to the soft drinks industry, from being in "like circumstances" with domestic suppliers of cane sugar to the soft drinks industry.

200. Equally, the Tribunal does not find the fact that sugar operates in a highly regulated market in comparison to the HFCS market to be a relevant consideration. In fact, Respondent does not elaborate on how this factor is relevant. Rather, Respondent's arguments on this point were largely a reiteration of its claim that the United States had failed to live up to its NAFTA obligations.

201. Respondent's third argument to support its position that Cargill de Mexico and domestic sugar producers were not in "like circumstances" deserves closer attention. Respondent claims that the sugar industry and the HFCS industry were in different economic circumstances. The former was "economically devastated" while the latter was not. This argument about the difference in economic circumstances bears some resemblance to the approach taken in *GAMI*. There, the tribunal concluded that the Mexican government had expropriated certain mills on the basis of its perception that it was in the interest of the national economy to have public participation in mills operating at near insolvency. On that basis, the tribunal was not convinced that the mills that had not been expropriated were so like the expropriated mills as to constitute

a violation of Article 1102.[19] Thus, under *GAMI*, difference in economic circumstances appeared to be the basis for the tribunal concluding that the expropriated and non-expropriated mills were not in "like circumstances".

202. In order to avoid the consequences of *GAMI*, Claimant argues that the decision in that case was based on a finding that the foreign investors could not show that they were less favourably treated than similarly situated domestic investors. However, an examination of the *GAMI* award shows that the tribunal concluded that the less favourable treatment that the Claimant received (being expropriated) was not a violation of Article 1102 because the expropriated investments were not in "like circumstances" with the investments that were not expropriated. And, they were not in "like circumstances" because of the perception of the difference in their economic situations.

203. In the present case, the essence of the Respondent's argument is that an industry that is in dire economic straits (Mexican suppliers of cane sugar) is not in "like circumstances" with an industry that is economically healthy (U.S. suppliers of HFCS), even though they supply products that are "directly competitive or substitutable." While it is true that this difference in economic circumstances existed, the question is whether the difference is relevant in the present case. In the Tribunal's view, the fact that a difference in circumstances exists in the abstract is not enough; the difference has to be relevant in the context of the particular measure being imposed.

204. In *GAMI*, the difference in economic circumstances was directly related to the rationale for the measure. The measure—expropriation—was taken *because of* economic circumstances. Mills that were in dire economic circumstances were expropriated and those that were in different economic circumstances were not. Thus, it was not an abstract difference that prevented the mills from being in "like circumstances"; it was a difference that was relevant to the very rationale for the measure. In relation to the measure, mills that were in different economic circumstances were not in "like circumstances".

[19] GAMI Investments, Inc. v. Mexico ("*GAMI*"), NAFTA/UNCITRAL, Final Award, ¶ 114 (15 Nov. 2004).

205. A similar approach appears to underlie the decision in *Pope & Talbot v. Canada*. There, the tribunal took the view that a determination of "like circumstances" had to take account of the surrounding facts and that "[a]n important element of the surrounding facts will be the character of the measure under challenge."[20] The tribunal then looked at the rationale for the measure and its policy objective, which was to replace the countervailing (anti-subsidy) duty ("CVD") imposed on Canadian lumber producers, and came to the conclusion that, in relation to that measure, lumber producers in "covered provinces" (provinces whose producers had been subject to the CVD) and lumber producers in non-covered provinces (provinces whose producers were not subject to the CVD) were not in "like circumstances".

206. Thus, in both *GAMI* and *Pope & Talbot*, "like circumstances" was determined by reference to the rationale for the measure that was being challenged. It was not a determination of "like circumstances" in the abstract. The distinction between those affected by the measure and those who were not affected by the measure could be understood in light of the rationale for the measure and its policy objective. Indeed, it is possible that in respect of other, different measures, the mills in *GAMI* and the lumber producers in *Pope & Talbot* could have been found to be in "like circumstances".

207. Thus, the question in this case is whether the difference in economic circumstances of the sugar industry and the HFCS industry in Mexico is relevant to the measure taken, the IEPS Tax imposed on soft drinks sweetened with HFCS. If the measure was one taken to benefit the sugar industry because of its economic condition in comparison with that of the HFCS industry then, on the basis of *GAMI*, the two industries would not have been in "like circumstances".

208. This case, however, is different. It is not a case of a measure providing an advantage to an industry in dire economic circumstances that is not available to a more economically healthy industry. It is a measure taken to disadvantage an industry that was in healthy economic circumstances, and which had the effect of driving the industry out of the market. Undoubtedly, the measure did benefit sugar producers, but

[20] Pope & Talbot Inc. v. Canada ("*Pope & Talbot*"), NAFTA/UNCITRAL, Award on the Merits of Phase 2, ¶ 76 (10 Apr. 2001).

Mexico did not claim that it took the measure simply to allow sugar producers to capture the sweetener market for soft drinks. Its rationale for the measure was to bring pressure on the United States government to live up to its NAFTA obligations.

209. Are, then, sugar producers and producers of HFCS in "like circumstances" in relation to the IEPS Tax, a measure designed to bring pressure on the United States? In the Tribunal's view, a measure affecting a particular industry designed to put pressure on the United States government will focus on those who are likely to be able to influence the United States government and, in this, there is no necessary relationship with economic circumstances. In other words, unlike the *GAMI* and *Pope & Talbot* cases, there is no link here between the alleged difference—a difference in economic circumstances—and the rationale and objective of the measure in question. In the Tribunal's view, a difference in economic circumstances is simply not relevant to determining whether the suppliers of HFCS and the suppliers of cane sugar are in "like circumstances" in relation to a measure designed to put pressure on the United States government.

210. Further, in the Tribunal's view, even the fact that the IEPS Tax indirectly benefited the sugar cane industry does not make the difference in economic circumstances relevant for determining whether the industries in question are in "like circumstances". In *GAMI*, reliance on a difference in economic circumstances to show that the Claimant's mills were not in like circumstances with other mills was related to the fact that the measure was taken to benefit the economically disadvantaged industry. The Claimant's mills were certainly treated differently, but they were not the target of a measure to drive them out of business. But, here, the measure and the effect are different from *GAMI*. If the *GAMI* principle could be used to justify a measure that destroys an economically viable foreign investment in order to benefit a domestic competitor, the national treatment protection in Article 1102 would be meaningless.

Final Disposition of the Tribunal with respect to "Like Circumstances"

211. In light of the above, the Tribunal concludes that, with respect to the IEPS Tax, suppliers of HFCS to the soft drink industry were in like circumstances with suppliers of cane sugar to the soft drink industry.

212. Although this conclusion relates to the IEPS Tax, in the Tribunal's view, the same reasoning must apply to the claim of "like circumstances" in relation to the import permit requirement. Since the import permit was a requirement that affected Cargill de Mexico as an investment of Cargill in Mexico, and not just Cargill as an exporter into Mexico, Claimant would have to show that Cargill de Mexico was in "like circumstances" with domestic suppliers of cane sugar for whom no such requirement existed.

213. Once again, the rationale for the measure—the import permit requirement—is relevant. Like the IEPS Tax, the rationale for the import permit requirement was to put pressure on the United States government to live up to its NAFTA obligations; indeed, it was perceived as a substitute for the IEPS Tax. The question, then, is whether a difference in economic circumstances is relevant to the determination of "like circumstances" in relation to a measure whose primary objective was to put pressure on the United States government. In the Tribunal's view, the answer to the import permit requirement is precisely the same as the answer for the IEPS Tax: difference in economic circumstances does not mean that the suppliers of HFCS and suppliers of cane sugar are not in "like circumstances" in relation to the import permit requirement.

214. In the light of the above, the Tribunal concludes that, in relation to both the IEPS Tax and the import permit requirement, Cargill de Mexico was in "like circumstances" with domestic suppliers of cane sugar to the soft drink industry.

"Treatment No Less Favorable"

Issue Presented

215. In view of the Tribunal's conclusion that suppliers of cane sugar and suppliers of HFCS were in "like circumstances", it is necessary to consider whether Cargill de Mexico, as a supplier of HFCS, received "less favorable treatment" than the suppliers of cane sugar.

Contentions of the Parties with respect to "Treatment No Less Favorable"

216. Claimant argues that the treatment accorded it by Respondent was less favourable in that the "difference in tax treatment made HFCS a far more expensive input into soft drinks than sugar." In respect of the IEPS Tax, Claimant draws support from the

decision of the WTO panel in *Mexico-Tax on Soft Drinks*, which concluded that HFCS, as a product, received less favourable treatment than sugar in relation to the soft drinks industry. Equally, Claimant argues that "Mexico's new import requirement and its refusal to issue such a permit to Cargill" disadvantaged Claimant to the benefit of domestic sugar producers in the competition for sweetener orders from the soft drinks industry.

217. Respondent does not challenge the claim that, under the IEPS Tax, HFCS was treated less favourably than cane sugar, but instead argues that, in order to comply with Article 1102, differential treatment has to be received on the basis of nationality. Respondent claims that this requirement is the consistent position taken by the three NAFTA State Parties and that the Tribunal should give this due weight in interpreting Article 1102. Thus, Respondent argues, since there was some Mexican investment in the HFCS industry and there was foreign investment (including that of Cargill) in the cane sugar industry, the discrimination as between suppliers of HFCS and cane sugar to the soft drinks industry could not have been on the basis of nationality.

218. Claimant counters that Article 1102 applies to *de facto* as well as *de jure* discrimination. It contends as well that Article 1102 applies when the treatment received by foreign investors is "materially less favorable" as compared with the treatment received by domestic investors.

Conclusion of the Tribunal with respect to "Treatment No Less Favorable"

219. In the Tribunal's view, there is no question but that, as a result of the IEPS Tax, the treatment received by suppliers of HFCS to the Mexican soft drinks industry was less favourable than the treatment received by suppliers of cane sugar. HFCS suppliers could no longer compete as a result of the IEPS Tax, whereas cane sugar suppliers were not affected.

220. Moreover, the Tribunal also concludes that the discrimination was based on nationality both in intent and effect. The IEPS Tax was taken avowedly to bring pressure on the United States government. By its very design, then, it was directed at United States producers of HFCS because only in that way would pressure be brought to bear on the United States government. The import permit requirement, which was intended by the

Mexican government to be a substitute for the IEPS Tax, was even more directly targeted at United States producers, even though it may have affected other nationals as well. The whole history of this case, as set out by both Claimant and Respondent, indicates that it is about measures directed at United States producers and suppliers of HFCS.

Final Disposition of the Tribunal with respect to "Treatment No Less Favorable"

221. In light of the above, the Tribunal concludes that the IEPS Tax and the import permit requirement resulted in Claimant receiving less favourable treatment within the meaning of Article 1102.

Treatment "with respect to the Establishment, Acquisition, Expansion, Management, Conduct, Operation, and Sale or Other Disposition of Investments"

222. The final requirement of Article 1102—that the treatment must be "with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments"—is clearly met in this case. Indeed, Respondent does not challenge this.

Final Disposition of the Tribunal with respect to Claim Arising under Article 1102

223. The Tribunal, accordingly, concludes that the IEPS Tax and the export permit requirement violate Mexico's obligations under Article 1102.

VIII. ARTICLE 1103 – MOST FAVOURED NATION ("MFN") TREATMENT

Issue Presented

224. Claimant argues that, as the import permit requirement applied only to HFCS imported from the United States and not to HFCS imported from Canada, Mexico violated its obligations under NAFTA Article 1103 to provide to Claimant, and its investment, Cargill de Mexico, treatment no less favourable than it provides in like circumstances to investors or investments of another Party or a non-Party.

225. Respondent's response is that Claimant has not identified any measure that constituted a violation of Article 1103. For Respondent, this is a jurisdictional issue. In order to establish a violation of Article 1103, Claimant has to show that an investor, or the

and "overthr[ow] the prior tax and import regimes on which [Claimant] reasonably relied when making its investments."

251. According to Claimant, predictability and stability were of "paramount importance" to it when it decided to invest in the Mexican sweetener industry and, for the first several years under the NAFTA, Respondent provided a stable business framework. Claimant argues, however, that then the HFCS measures "pulled the rug out from under that framework," defeating stability, predictability and Claimant's reasonable expectations. Claimant asserts that the antidumping duties, the IEPS Tax, the unobtainable permit requirement and the "governmental determination to remove the competitive threat of HFCS at all costs" "breached its obligation of fair and equitable treatment by evisceration of the arrangements in reliance upon which the foreign investor was induced to invest."[31]

252. Claimant concludes that "[t]his transformation of the investment landscape" cannot be considered a legitimate business risk as it arose not from natural economic factors, but from "hostile measures taken by the host government." Claimant argues that the unpredictability of the measures is proven by their timing: when the antidumping duties were about to be revoked, Respondent instituted the IEPS Tax; and when bottlers began to win *amparos* against the Tax, Respondent withheld criteria for issuance of the import permits.

253. Respondent, on the other hand, points to Claimant's internal feasibility studies and memoranda as proof that Claimant was not only not taken by surprise by the import licensing requirement, but was previously aware of the possibility of such an action. Respondent quotes, for instance, from Claimant's "Mexico HFCS Plant Feasibility Study: Tula, Hidalgo," (4 Nov. 1999), Executive Summary, p. 2, in which Claimant wrote under Section V, titled, "Mexico Government/Political Section" at p. 21:

> The key factors are:
>
> (A) Potential risk of government-imposed quota limiting quantities of HFCS imports, or the potential risk of elimination of HFCS imports because of domestically produced HFCS (longer term).

[31]CME Czech Rep. B.V. (Netherlands) v. The Czech Republic ("*CME v. Czech Republic*"), UNCITRAL, Partial Award, ¶ 611 (13 Sept. 2001).

> By Cargill not building in Mexico, we take the risk of our competitors and the sugar mills petitioning the Mexican government for protection of a now, local industry (HFCS). ... Cargill would be the only major wet miller without HFCS capacity in Mexico. As the HFCS duty declines to 0 over the next 9 years, our competitors would have a strong argument for local support of their investment employing Mexican workers, paying Mexican taxes. I believe it is safe to say that if there is a quota imposed on HFCS, the wet miller without local HFCS production would be at the most risk.

In further support, Respondent also quotes from an internal Cargill memorandum of 6 August 1996, a 17 July 2000 draft letter from Claimant to USTR Charlene Barshefsky, and a memorandum from the Corn Refiners Association regarding the status of NAFTA Chapter 19 litigation addressing the antidumping order sent to the board of directors (including Claimant's representative) on 28 August 2000. As final support for its contention that Claimant was aware of the possibility of such import restrictions, Respondent raises a 23 August 2001 meeting, at which Undersecretary de la Calle allegedly informed Claimant's representatives that such restrictions would occur unless the sugar market dispute was resolved expeditiously.

254. In response to Respondent's raising of these various documents in an effort to prove Claimant's anticipation of the permit requirement, Claimant counters that, "[o]f course, no company would consider an investment in a foreign country without assessing risks." Claimant asserts, however, that this does not mean that it should have reasonably expected Respondent to announce a permit requirement only for HFCS where such permits would be issued automatically, but where in fact Respondent would refuse to issue to Claimant such a permit on the basis that no criteria had been established for their issuance.

Contentions of the Parties as to the Application in this Instance of the Asserted Prohibition of "Arbitrariness, Ambiguity and Inconsistency"

255. Claimant next argues that Respondent's HFCS measures were arbitrary, ambiguous and inconsistent as illustrated by three alleged facts: (1) the IEPS Tax was imposed solely in response to domestic political and protectionist pressure, rather than an attempt to raise revenue; (2) the permit requirement was not reasonably related to any purpose other than excluding HFCS imported from the United States, as illustrated by Respondent's failure to announce criteria for obtaining the permits; and (3) the IEPS

Conclusion of the Tribunal with respect to Claim Arising under Article 1105

The Fair and Equitable Treatment Standard

266. Article 1105(1) of the NAFTA provides: "Each 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." The content of this obligation has been difficult to define with precision and the statements of various NAFTA tribunals are difficult to apply to particular facts.

267. The Tribunal first observes that it is beyond cavil that the reference to "fair and equitable treatment" in Article 1105(1) is to be understood by reference to customary international law. On 31 July 2001, in response to the concern of State Parties that tribunals were reading this provision over-broadly, the NAFTA Free Trade Commission issued an FTC Note providing, *inter alia*, that:

> 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).

268. In light of the FTC's interpretation and the binding force of that interpretation on this Tribunal by virtue of Article 1132(2),[39] the Tribunal joins all previous NAFTA tribunals in the view that Article 1105 requires no more, nor less, than the minimum standard of treatment demanded by customary international law. As stated by the *Mondev* tribunal, the FTC Note made "clear that Article 1105(1) refers to a standard existing under customary international law, and not to standards established by other treaties of the three NAFTA Parties."[40] Likewise, as explained by Mexico in its 1128

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[39] Article 1131, titled "Governing Law," in its second paragraph provides: "An interpretation by the Commission of a provision of this Agreement shall be binding on a Tribunal established under this Section."

[40] Mondev Int'l Ltd. v. United States ("*Mondev*"), NAFTA/ICSID Case No. ARB(AF)/99/2, Award, ¶ 121 (11 Oct. 2002). *See also* ADF Group Inc. v. United States ("*ADF Group*"), NAFTA/ICSID Case No. ARB(AF)/00/1, Award, ¶ 178 (9 Jan. 2003) (holding that the FTC Note "clarifies that so far as the three NAFTA Parties are concerned, the

Submission to the *ADF* tribunal, "'fair and equitable treatment' and 'full protection and security' are provided as examples of the customary international law standards incorporated in Article 1105(1). … The international law minimum standard [of treatment] is an umbrella concept incorporating a set of rules that has crystallized over the centuries into customary international law in specific contexts."[41]

269. Although Claimant initially argued that the meaning of "fair and equitable treatment" should be approached as a question of treaty interpretation, both Claimant and Respondent agreed by the time of the hearing that Article 1105 is a codification of the customary international law minimum standard of treatment. The Parties, however, continue to disagree as to the content of that customary international law standard.

270. In approaching the task of ascertaining the customary international law standard of "fair and equitable treatment," the Tribunal emphasizes a foundational point to its mode of reasoning, which it simultaneously views as a point of weakness in some of the awards it has reviewed.

271. The shift in approach from seeking the meaning of "fair and equitable treatment" as a matter of treaty interpretation to seeking to ascertain the content of custom has fundamental implications for the legal reasoning of a tribunal. A tribunal confronted with a question of treaty interpretation can, with little input from the parties, provide a legal answer. It has the two necessary elements to do so; namely, the language at issue and rules of interpretation. A tribunal confronted with the task of ascertaining custom, on the other hand, has a quite different task because ascertainment of the content of custom involves not only questions of law but involves primarily a question of fact, where custom is found in the practice of States regarded as legally required by them. The content of a particular custom may be clear; but where a custom is not clear, or is disputed, then it is for the party asserting the custom to establish the content of that custom.

272. In the case of the customary international law standard of "fair and equitable treatment," the Parties in this case and the other two NAFTA State Parties agree that

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long-standing debate as to whether there exists such a thing as a minimum standard of treatment of non-nationals and their property prescribed in customary international law, is closed.").

[41] *ADF Group*, Second Article 1128 Submission of the United Mexican States, p. 8 (22 July 2002).

the customary international law standard is at least that set forth in the 1926 *Neer* arbitration. In that award it was held that "the treatment of an alien … should amount to an outrage, to bad faith, to willful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency."[42] The Parties and the other two NAFTA State Parties also agree that the standard may evolve and, indeed, may have evolved since 1926.

273. The Parties disagree, however, as to how that customary standard has in fact, if at all, evolved since that time. The burden of establishing any new elements of this custom is on Claimant. The Tribunal acknowledges that the proof of change in a custom is not an easy matter to establish. However, the burden of doing so falls clearly on Claimant. If Claimant does not provide the Tribunal with the proof of such evolution, it is not the place of the Tribunal to assume this task. Rather the Tribunal, in such an instance, should hold that Claimant fails to establish the particular standard asserted.

274. The initial issue before the Tribunal therefore is to evaluate Claimant's assertions as to the content of the customary international law standard of "fair and equitable treatment" in light of the sources placed before the Tribunal. Consistent and widespread State practice conducted out of a sense of legal obligation would establish the content of customary international law. The Tribunal acknowledges, however, that surveys of State practice are difficult to undertake and particularly difficult in the case of norms such as "fair and equitable treatment" where developed examples of State practice may not be many or readily accessible. Claimant has not provided the Tribunal with such a survey of recent State practice, nor is the Tribunal aware of such a survey.

275. In such instances, recourse may be made to other evidence of custom. The statements of States can—with care—serve as evidence of the content of custom. In the case of the NAFTA State Parties, they have made statements in the context of their position as respondents or as non-disputing State Parties in Chapter 11 arbitrations. Thus, Mexico has not only presented its view on the content of customary international law standard in this proceeding, but also as a non-disputing State Party in an Article 1128

[42] *Neer*, 4 I.R.A.A. 60 (15 Oct. 1926).

Submission in the *ADF* proceeding. In *ADF*, Mexico's Article 1128 Submission approvingly quotes Canada's submission as respondent in *Pope & Talbot*, which states: "The conduct of the government toward the investment must amount to gross misconduct, manifest injustice or, in the classic words of the *Neer* claim, an outrage, bad faith or the willful neglect of duty."[43] The Tribunal acknowledges that the weight of these statements needs to be assessed in light of their position as respondents at the time of the statement. However, the Tribunal also observes that, for example, the United States maintains a similar position as to the customary international law standard of fair and equitable treatment in its model bilateral investment treaty, a situation in which it is at least equally possible that the United States would be in the position of either respondent or the state of nationality of the claiming investor.

276. It also is widely accepted that extensive adoption of identical treaty language by many States may in and of itself serve—again with care—as evidence of customary international law. The Tribunal notes that Claimant has not attempted to establish such a circumstance to this Tribunal except in the most general terms. Even accepting that such clauses are widespread, the Tribunal views the evidentiary weight of this possibility cautiously. The Tribunal observes that the requirement to provide "fair and equitable treatment" is included in many bilateral investment treaties ("BITs"). The Tribunal notes first that some of these clauses involve a reference to customary international law, while others apparently involve autonomous treaty language. It is the Tribunal's view that significant evidentiary weight should not be afforded to autonomous clauses inasmuch as it could be assumed that such clauses were adopted precisely because they set a standard other than that required by custom. It may be that widespread adoption of a strict autonomous meaning to "fair and equitable treatment" may in time raise international expectations as to what constitutes good governance, but such a consequence is different than such clauses evidencing directly an evolution of custom. The Tribunal notes second that the explosion in the number of BITs is a recent phenomenon and that responses of States to the questions presented in terms, for example, of calls for renegotiation or statements of approval is only now

[43] *ADF Group*, Second Article 1128 Submission of the United Mexican States, p. 15 (22 July 2002), quoting *Pope & Talbot*, Post-Hearing Submission of the United Mexican States (Damages Phase), ¶ 8 (3 Dec. 2001), quoting *Pope & Talbot*, Respondent Canada's Counter-Memorial (Phase 2), ¶ 309 (10 Oct. 2000).

emerging. In such a fluid situation, the Tribunal does not believe it prudent to accord significant weight to even widespread adoption of such clauses.

277. Finally, the writings of scholars and the decisions of tribunals may serve as evidence of custom.[44] It is important to emphasize, however, as Mexico does in this instance, that the awards of international tribunals do not create customary international law but rather, at most, reflect customary international law. Moreover, in both the case of scholarly writings and arbitral decisions, the evidentiary weight to be afforded such sources is greater if the conclusions therein are supported by evidence and analysis of custom.

278. A substantial number of arbitral decisions have been rendered over the last decade in proceedings based on such BITs. In the Tribunal's view, these decisions are relevant to the issue presented in Article 1105(1) only if the fair and equitable treatment clause of the BIT in question was viewed by the Tribunal as involving, like Article 1105, an incorporation of the customary international law standard rather than autonomous treaty language.

279. The Tribunal observes that Claimant in the instant case has not offered a survey of all arbitral decisions bearing on the customary international law of fair and equitable treatment. Claimant's effort to establish the current customary content of "fair and equitable treatment" relies rather heavily on the award rendered in *Tecmed*, a reliance that Respondent contends is misplaced. The Tribunal agrees.

280. The Tribunal notes that the claim in *Tecmed* alleges violations of a BIT between Spain and Mexico.[45] Article 4(1) of the BIT involved in the *Tecmed* proceeding provides that each party guarantees in its territory just and equitable treatment, conforming with "International Law", to the investments of investors of the other contracting party. Article 4(2) explains further that this treatment will not be less favourable than that granted in similar circumstances by each contracting party to the investments in its territory by an investor of a third State. Although the language of Article 4(2) permits several interpretations, the *Tecmed* tribunal specifically states that it "understands that

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[44] *See, e.g.*, The Statute of the International Court of Justice, Article 38 (1)(d).
[45] *See* Agreement on the Reciprocal Promotion and Protection of Investments signed by the Kingdom of Spain and the United Mexican States (1996).

the scope of the undertaking of fair and equitable treatment under Article 4(1) of the Agreement described ... is that resulting from *an autonomous interpretation* ...."[46] The award and statements of the *Tecmed* tribunal thus do not bear on the customary international law minimum standard of treatment, but rather reflect an autonomous standard based on an interpretation of the text. Thus, the Tribunal determines that the holding in *Tecmed* is not instructive in this arbitration as to the scope and bounds of the fair and equitable treatment required by Article 1105 of the NAFTA.

281. The Tribunal observes that several NAFTA arbitrations, the significance of which was argued before this Tribunal, in contrast do analyze and elaborate upon the customary international law minimum standard of treatment as required by NAFTA Article 1105. These tribunals agree, for instance, that the customary international law minimum standard of treatment is dynamic and therefore evolves with the rights of individuals under international law. As the *ADF* tribunal wrote: the customary international law minimum standard of treatment is "constantly in a process of development."[47] The *Mondev* tribunal held similarly:

> [B]oth the substantive and procedural rights of the individual in international law have undergone considerable development. In the light of these developments it is unconvincing to confine the meaning of 'fair and equitable treatment' and 'full protection and security' of foreign investments to what those terms – had they been current at the time – might have meant in the 1920s when applied to the physical security of an alien.[48]

282. As stated above, the Parties in this proceeding and this Tribunal agree with the view that the customary international law minimum standard of treatment may evolve in accordance with changing State practice manifesting to some degree expectations within the international community. As the world and, in particular, the international business community become ever more intertwined and interdependent with global trade, foreign investment, BITs and free trade agreements, the idea of what is the minimum treatment a country must afford to aliens is arising in new situations simply not present at the time of the *Neer* award which dealt with the alleged failure to properly investigate the murder of a foreigner.

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[46] *Tecmed*, Award, ¶ 155 (29 May 2003) (emphasis added).
[47] *ADF Group*, Award, ¶ 179 (9 Jan. 2003).
[48] *Mondev*, Award, ¶ 116 (11 Oct. 2002).

283. The central inquiry therefore is: what does customary international law *currently* require in terms of the minimum standard of treatment to be accorded to foreigners? The *Waste Management II* tribunal concluded that a general interpretation was emerging from NAFTA awards:

> Taken together, the *S.D. Myers*, *Mondev*, *ADF* and *Loewen* cases suggest that the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety – as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.[49]

284. In reviewing the awards cited and, as importantly, the evidence of custom analyzed in those proceedings, this Tribunal agrees in part with the assessment cited above. The Tribunal observes a trend in previous NAFTA awards, not so much to make the holding of the *Neer* arbitration more exacting, but rather to adapt the principle underlying the holding of the *Neer* arbitration to the more complicated and varied economic positions held by foreign nationals today. Key to this adaptation is that, even as more situations are addressed, the required severity of the conduct as held in *Neer* is maintained. In this regard, the Tribunal finds particularly significant the statement of the standard found in the Article 1128 Submissions of Mexico and Canada in *ADF*. That standard is:

> [T]he conduct of the government toward the investment must amount to gross misconduct, manifest injustice or, in the classic words of the *Neer* claim, bad faith or the willful neglect of duty.[50]

285. As outlined in the *Waste Management II* award quote above, the violation may arise in many forms. It may relate to a lack of due process, discrimination, a lack of transparency, a denial of justice, or an unfair outcome. But in all of these various forms, the "lack" or "denial" of a quality or right is sufficiently at the margin of acceptable conduct and thus we find—in the words of the 1128 submissions and

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[49] Waste Management, Inc. v. United Mexican States ("*Waste Management II*"), NAFTA/ICSID Case No. ARB(AF)/00/3, Award, ¶ 98 (30 Apr. 2004).
[50] *ADF Group*, Second Article 1128 Submission of the United Mexican States, p. 15 (22 July 2002), quoting *Pope & Talbot*, Post-Hearing Submission of the United Mexican States (Damages Phase), ¶ 8 (3 Dec. 2001), quoting *Pope & Talbot*, Respondent Canada's Counter-Memorial (Phase 2), ¶ 309 (10 Oct. 2000).

previous NAFTA awards—that the lack or denial must be "gross," "manifest," "complete," or such as to "offend judicial propriety." The Tribunal grants that these words are imprecise and thus leave a measure of discretion to tribunals. But this is not unusual. The Tribunal simultaneously emphasizes, however, that this standard is significantly narrower than that present in the *Tecmed* award where the same requirement of severity is not present.

286. The Tribunal thus holds that Claimant has failed to establish that the standard present for example in the *Tecmed* award reflects the content of customary international law. The Tribunal holds that the current customary international law standard of "fair and equitable treatment" at least reflects the adaptation of the agreed *Neer* standard to current conditions, as outlined in the Article 1128 submissions of Mexico and Canada. If the conduct of the government toward the investment amounts to gross misconduct, manifest injustice or, in the classic words of the *Neer* claim, bad faith or the willful neglect of duty, whatever the particular context the actions take in regard to the investment, then such conduct will be a violation of the customary obligation of fair and equitable treatment.

287. In articulating the above standard, the Tribunal finds the four "implications" identified by the *GAMI* tribunal to be both helpful and consistent. The Tribunal therefore joins the *GAMI* tribunal in the adoption of these four implications: (1) "The failure to fulfill the objectives of administrative regulations without more does not necessarily rise to a breach of international law"; (2) "A failure to satisfy requirements of national law does not necessarily violate international law"; (3) "Proof of a good faith effort by the Government to achieve the objectives of its laws and regulations may counter-balance instances of disregard of legal or regulatory requirements"; and (4) "The record as a whole—not isolated events—determines whether there has been a breach of international law."[51]

288. As noted above, Claimant argues that fair and equitable treatment creates several specific obligations for each State Party: the provision of a stable and predictable environment that does not offend reasonable expectations; a general lack of arbitrariness, ambiguity and inconsistency; transparency; and a lack of discrimination.

[51] *GAMI Investments*, Final Award, at ¶ 97 (15 Nov. 2004).

As far as these particular requirements, the Tribunal examines each briefly as to how it is to be approached in light of the Tribunal's holding in the previous paragraph.

Stable and Predictable Environment that Does Not Frustrate Reasonable Expectations

289. Claimant provides the Preamble to the NAFTA as its sole legal or textual support for its contention that NAFTA State Parties are bound to provide a stable and predictable environment in which reasonable expectations are upheld.[52]

290. The Tribunal notes that there are at least two BIT awards, both involving a clause viewed as possessing autonomous meaning, that have found an obligation to provide a predictable investment environment that does not affect the reasonable expectations of the investor at the time of the investment.[53] No evidence, however, has been placed before the Tribunal that there is such a requirement in the NAFTA or in customary international law, at least where such expectations do not arise from a contract or quasi-contractual basis.

Arbitrariness, Ambiguity and Inconsistency

291. With respect to arbitrariness, the Tribunal agrees with the view expressed by a Chamber of the International Court of Justice in the *ELSI* case, where it is stated:

> Arbitrariness is not so much something opposed to a rule of law, as something opposed to the rule of law. This idea was expressed by the court in the *Asylum* case, when it spoke of 'arbitrary action' being 'substituted for the rule of law' … It is a wilful [*sic*] disregard of due process of law, an act which shocks, or at least surprises, a sense of juridical propriety.[54]

This holding, though not based on the NAFTA, has been accepted by at least two of the State Parties to the NAFTA as the "best expression" of arbitrariness.[55]

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[52] Claimant also cites to *Tecmed* to support its arguments with respect to the alleged requirement to provide a stable and predictable environment. However, as the Tribunal has determined that *Tecmed* arose from an autonomous interpretation of "fair and equitable treatment," as opposed to that drawn from the customary international law minimum standard of treatment, the Tribunal does not consider the *Tecmed* award a persuasive authority in evaluating these allegations.

[53] *See Tecmed*, Award, ¶ 154 (29 May 2003); Saluka Investments BV (Netherlands) v. Czech Republic ("*Saluka v. Czech Republic*"), UNCITRAL, Partial Award, ¶¶ 301-02 (17 Mar. 2006).

[54] *ELSI*, Judgment, ¶ 128 (1989) (internal citation omitted).

[55] *See ADF Group*, Award, ¶ 121 (9 Jan. 2003) (describing Canada's approval of the standard); *ADF Group*, Second Article 1128 Submission of the United Mexican States, pp. 16-18 (22 July 2002) (detailing Mexico's view of the standard as instructive).

292. The Tribunal also agrees with the view expressed in *S.D. Myers* that a tribunal, in assessing whether an action of a State is arbitrary, need recognize that governments "make many potentially controversial choices" and, in doing so, may "appear to have made mistakes, to have misjudged the facts, proceeded on the basis of a misguided economic or sociological theory, placed too much emphasis on some social values over others and adopted solutions that are ultimately ineffective or counterproductive."[56] Therefore, an actionable finding of arbitrariness must not be based simply on a tribunal's determination that a domestic agency or legislature incorrectly weighed the various factors, made legitimate compromises between disputing constituencies, or applied social or economic reasoning in a manner that the tribunal criticizes.

293. The Tribunal thus finds that arbitrariness may lead to a violation of a State's duties under Article 1105, but only when the State's actions move beyond a merely inconsistent or questionable application of administrative or legal policy or procedure to the point where the action constitutes an unexpected and shocking repudiation of a policy's very purpose and goals, or otherwise grossly subverts a domestic law or policy for an ulterior motive.

Transparency

294. The Tribunal holds that Claimant has not established that a general duty of transparency is included in the customary international law minimum standard of treatment owed to foreign investors per Article 1105's requirement to afford fair and equitable treatment. The principal authority relied on by the Claimant—*Tecmed*—involved the interpretation of a treaty-based autonomous standard for fair and equitable treatment and treated transparency as an element of the "basic expectations" of an investor rather than as an independent duty under customary international law.

Discrimination

295. The Tribunal finds that a discussion of whether a finding of discrimination will independently violate Article 1105 of the NAFTA is not called for at this time. In support of its contention that the customary international law minimum standard of

[56] *S.D. Myers*, Partial Award, ¶ 261 (13 Nov. 2000).

treatment precludes discrimination, Claimant merely incorporates its discussion from its arguments for finding a violation of Articles 1102 and 1103. The FTC Note clearly states that "[a] determination that there has been a breach of another provision of the NAFTA ... does not establish that there has been a breach of Article 1105(1)." Therefore, looking to the facts presented as proof of a violation of Articles 1102 and 1103 will not assist the Tribunal in assessing a violation of Article 1105.

Final Disposition of the Tribunal with respect to the Standard of Conduct Required by the Obligation of Fair and Equitable Treatment

296. In summation, the Tribunal finds that the obligations in Article 1105(1) of the NAFTA are to be understood by reference to the customary international law minimum standard of treatment of aliens. The requirement of fair and equitable treatment is one aspect of this minimum standard. To determine whether an action fails to meet the requirement of fair and equitable treatment, a tribunal must carefully examine whether the complained of measures were grossly unfair, unjust or idiosyncratic; arbitrary beyond a merely inconsistent or questionable application of administrative or legal policy or procedure so as to constitute an unexpected and shocking repudiation of a policy's very purpose and goals, or to otherwise grossly subvert a domestic law or policy for an ulterior motive; or involve an utter lack of due process so as to offend judicial propriety. The Tribunal observes that other NAFTA tribunals have expressed the view that the standard of fair and equitable treatment is not so strict as to require "bad faith" or "willful neglect of duty". The Tribunal agrees. However, the Tribunal emphasizes that although bad faith or willful neglect of duty is not required, the presence of such circumstances will certainly suffice.

Conclusion of the Tribunal with respect to whether the Mexican Measures at Issue in this Proceeding Breach the Fair and Equitable Treatment Requirement of Article 1105

297. In analyzing the facts as presented by the Parties, the Tribunal observes that the effects of the IEPS Tax, as well as the consequences of the antidumping duties, may not serve as the basis of a claim asserting a breach of Article 1105(1). In the case of the former, this is because the tax measures are excluded from consideration in the context of Article 1105; in the case of the latter, because the antidumping duties are outside of the temporal jurisdiction of this Tribunal. A measure excluded as a basis for a claim,

however, may nevertheless aid the Tribunal's understanding of the context of the acts legitimately within the Tribunal's purview.[57] The Tribunal, therefore, considers solely whether the import permit requirement instituted by Mexico breached the requirement of fair and equitable treatment in Article 1105(1). But, in doing so, the Tribunal is cognizant that the permit requirement was only one in a series of measures taken by Respondent.

298. The import permit requirement instituted by Mexico may be analyzed in several respects under the standard the Tribunal has determined to be applicable. By far, the Tribunal finds most determinative the fact that the import permit was put into effect by Mexico with the express intention of damaging Claimant's HFCS investment to the greatest extent possible. For this reason, the Tribunal finds this action to surpass the standard of gross misconduct and be more akin to an action in bad faith.

299. Reviewing closely the record of this case, the Tribunal finds ample support for the conclusion that the import permit was one of a series of measures expressly intended to injure United States HFCS producers and suppliers in Mexico in an effort to persuade the United States government to change its policy on sugar imports from Mexico. The Tribunal finds that the sole purpose of the import permit requirement was to change the trade policy of the United States; while the sole effect was to virtually remove Claimant from the Mexican HFCS market. There is no other relationship between the means and the end of this requirement. The Tribunal finds the institution of a permit requirement for a few foreign producers in an attempt to persuade another nation to alter its trade practices to be manifestly unjust.

300. The Tribunal finds that Respondent, in an attempt to further its goals regarding United States trade policy, targeted the few suppliers of HFCS that originated in the United States. These few suppliers thus were then forced to bear the entire burden of Respondent's effort to act on what it views as the United States' failure to comply with international obligations. Indeed, the import permit requirement all but annihilated a series of investments for the time that the permit requirement was in place. The Tribunal finds this willful targeting, by its nature, to be a manifest injustice. The fact that the targeted investors are corporations with U.S. nationality is of no significance

[57] *See GAMI*, Final Award, at ¶ 97 (15 Nov. 2004).

in the Tribunal's view. If the import permit requirement had been instituted to influence the trade policy of a country other than the country of the nationality of the investors, the manifest injustice is, in the Tribunal's view, patent. Given the Tribunal's holding within, rejecting Respondent's claim that its actions were justifiable as countermeasures,[58] it is equally clear that a targeted import permit requirement of this type is also manifestly unjust when the country sought to be influenced is also the country of nationality of the investor.

301. The Tribunal's finding that the import permit requirement surpasses the standard of gross misconduct and is more akin to an action in bad faith is supported by the fact that there was a complete lack of objective criteria put forth by the Mexican government by which a company could obtain a permit. The Tribunal finds Respondent's explanation that "the publication of the criteria for applying import permits will be established when 'the necessary conditions' exist" to be insufficient, given that the existence of such conditions depended entirely on the actions of an unrelated third party with respect to its trade policies.

302. The Tribunal recalls Respondent's argument that, as there has been no conclusion under domestic law that the import requirement was illegal, the "Tribunal cannot proceed to analyze if the conduct of the Mexican authorities rises to arbitrariness under international law." As proof of the lack of domestic resolution, Respondent points to a legal challenge filed by Claimant in 2006, that was "still pending" at the time of the Parties' submissions. The Tribunal likewise recalls Respondent's argument that tribunals have consistently held that poor administration of government programs (which Respondent claims is not at issue) does not amount to a violation of the minimum standard of treatment under customary international law. Finally, the Tribunal recalls Respondent's argument that Claimant was previously aware of the possibility of such an import permit requirement.

303. The Tribunal finds these arguments to be inapposite given the Tribunal's finding that the import permit intentionally targeted Claimant and therefore was manifestly unjust. Whether Claimant was previously aware or not of the possibility of an import permit requirement is not on point because such a line of argumentation suggests a public

[58] *See infra* ¶¶ 420-29.

purpose to the requirement, rather than, as the Tribunal's finds, the fact that the requirement was an intentional targeting of Claimant's investment that was designed specifically so that Claimant would not receive a permit. Likewise, the issue is not whether there was poor administration of government leading to arbitrary acts. In this instance, the administration by the government of the import permit requirement was quite effective. Finally, the Tribunal does not, and need not, rest its holding on the import permit requirement being domestically unlawful given its conclusion that the requirement is manifestly unjust and akin to an act in bad faith. The Tribunal agrees with Respondent that even the unlawfulness of a municipal law does not necessarily mean that the act is unlawful under international law. The converse must be true, however, in that the *lawfulness* of a domestic law does not presuppose its lawfulness under international law. Indeed, this is the very rationale for the customary international law minimum standard of treatment of aliens: regardless of the views of each State, there is a minimum, a floor below which a State will be held internationally responsible for its conduct.

304. Lastly, the Tribunal acknowledges the dire and difficult circumstances that faced Mexico at the time of the measures in terms of the crisis gripping its sugar industry and the many citizens employed in that industry. The Tribunal does not assert that Mexico could not enact any laws and regulations to aid this industry and its populace. Rather, the Tribunal finds that the import permit requirement simultaneously breached the requirement to provide fair and equitable treatment under Article 1105(1). Mexico may seek to attain its objective by the regulation chosen, but it may not under Article 1105(1) leave the Claimant to bear the costs of this choice.

Final Disposition of the Tribunal with respect to Claim Arising Under Article 1105

305. For the forgoing reasons, the Tribunal finds the import permit requirement instituted by Mexico, for the period it was in effect, to be a breach of the Article 1105(1) obligation to provide fair and equitable treatment to Claimant.

possible under Article 1110 to bring a claim for a "temporary" taking and denies the claim on that basis.

The Scope of Cargill's Investment under Article 1139

349. Respondent argues that Claimant's Article 1110 claim is not based on an "investment" as that term is defined by Article 1139. The Tribunal disagrees.

350. Under Article 1139, it is clear that Cargill de Mexico ("CdM") qualifies as an "investment" both because it satisfies the definition of an "enterprise," and because it qualifies as "real estate or other property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes" (including the Tula distribution facility).[80] This is argued by Claimant and not disputed by Respondent. Claimant's claim, however, is based on its "Mexican HFCS business" and not on a taking of CdM or the Tula Facility: "it is *Cargill's investment in HFCS* that is at issue here, including its investment in Cargill de Mexico's *HFCS business unit* and in the *HFCS terminal* at the Tula distribution center" (emphasis added). Claimant thus does not claim for the diminished value of the physical assets held by Cargill de Mexico, but rather for the damages that resulted from the alleged loss of their intended use.

351. Respondent argues that the issue before the Tribunal is whether this "HFCS business" is an investment in and of itself under Article 1139 that is subject to expropriation within the meaning of Article 1110. The Tribunal agrees broadly with Respondent's identification of the issue presented, but views the issue as involving two distinct questions: first, whether the "HFCS business" is an investment in and of itself under Article 1139; and second, whether the "HFCS business," as an investment under Article 1139, can be the subject of a claim for expropriation within the meaning of Article 1110.

352. As to the first question, the Tribunal recalls its conclusion in paragraph 153, *supra*, that there is no express or implied presumption that measures dealing with goods cannot *ipso facto* be alleged to be measures "relating to" investors or investments per

[80] *See supra* ¶ 167.

Article 1101. It likewise concluded in paragraph 147, *supra*, that although there are exclusions, the Article 1139 definition of "investment" is broad and inclusive.

353. The Tribunal thus has little difficulty in concluding that business income, particularly one associated with a physical asset in the host country and not merely trade in goods, is potentially an investment both as an element of a larger investment involving the physical asset and as an investment in and of itself.

354. This conclusion leads to the second question of whether the "HFCS business," as an investment under Article 1139, can be the subject of a claim for expropriation within the meaning of Article 1110. In other words, the scope of what may be the subject of a claim is delimited in part by the definition of investment in Article 1139, but also by the confines of the legal basis of the particular claim. It is the unusual character of Claimant's Article 1110 claim (namely that it is a claim based on a temporary taking and therefore a claim not for the physical asset but rather for the loss of business during the time of the interference) that is truly at the basis of Respondent's objection.

355. The issue of whether a loss of business may be the subject of an Article 1110 claim has been considered by other NAFTA tribunals.

356. In *Pope & Talbot*, the tribunal was presented with a similar situation in that the claimant's ability in that case to sell lumber in the U.S. market was impeded by a set of Canadian measures. Canada in that instance claimed, as in this case, that the claimant retained title to the investment and that loss of business was not the proper subject of an Article 1110 claim. The tribunal found that interference with the business had an impact on the property in the host country:

> While Canada suggests that the ability to sell softwood lumber from British Columbia to the U.S. is an abstraction, it is, in fact, a very important part of the 'business' of the Investment. Interference with that business would necessarily have an adverse effect on the property that the Investor has acquired in Canada, which, of course, constitutes the Investment. While Canada's focus on the 'access to the U.S. Market' may reflect only the Investor's own terminology, that terminology should not mask the fact that the true interests at stake are the Investment's asset base, the value of which is largely dependent on its export business.[81]

[81] *Pope & Talbot*, Interim Award, ¶ 98 (26 June 2000).

The Tribunal agrees with the *Pope & Talbot* tribunal that the business income of an investment is an integral part of the value of the underlying property. But in both *Pope & Talbot* and the present case, the Claimant has not claimed for the value of the entire investment but rather only for the loss of business income. Usually, in the case of a permanent expropriation of the entire investment, the loss of business income would be reflected in the value given to the entire investment.[82] In this sense, the *Pope & Talbot* tribunal did not address what this Tribunal considers to be the key question: whether an Article 1110 expropriation claim may be based on a temporary taking and thus only seek the loss of business income.

357. This situation was also considered by the tribunal in the *Methanex* arbitration. The claimant in *Methanex* claimed for reduced return on investments, increased cost of capital, reduced value of investments, and reduced market value (as evidenced by drop in stock price).[83] The *Methanex* tribunal agreed with the reasoning of *Pope & Talbot* but then expanded on its holding:

> Certainly, the restrictive notion of property as a material 'thing' is obsolete and has ceded its place to a contemporary conception which includes managerial control over components of a process that is wealth producing. In the view of the Tribunal, items such as good will and market share may, as Professor White wrote, 'constitute an element of the value of an enterprise and as such may have been covered by some of the compensation payments.' Hence, in a comprehensive taking, these items may figure in valuation. But it is difficult to see how they might stand alone, in a case like the one before the Tribunal.[84]

358. The Tribunal concludes that business income, particularly when it is associated with a physical asset in the host country, is an investment within the meaning of Article 1139 both as an element of a larger investment involving the physical asset and as an investment in and of itself. The separate question of whether an Article 1110 claim may be based on a temporary taking is considered *infra* at paragraphs 370-77.

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[82] In *Pope & Talbot*, given that "the true interests at stake are the Investment's asset base, the value of which is largely dependent on its export business," the tribunal found that the claimant had properly pled that measures affected its "investment", but that the "interference [was not] sufficiently restrictive to support a conclusion that the property [had] been 'taken' from the owner." *Pope & Talbot*, Interim Award, ¶¶ 98, 102, 104-05 (26 June 2000).

[83] *Methanex*, Final Award, Part II, Ch. D, p. 11, ¶ 31 (3 Aug. 2005), citing Second Amended Statement of Claim, ¶¶ 321-27.

[84] *Id.*, Part IV, Ch. D, p. 7, ¶ 17 (citations omitted). The *Methanex* tribunal therefore found no violation of Article 1110 in the claimant's claims that "a substantial portion of [its] investments, including its share of the California and larger U.S. oxygenate market were taken by facially discriminatory measures and handed over to the domestic ethanol industry." *Id.* ¶¶ 3, 15-18.

The Degree of Interference with the Investment

359. There are two prongs to an assessment of the degree of interference with Claimant's investment: the severity of the economic impact and the duration of that impact. The Tribunal considers each in turn.

The Severity of the Economic Impact

360. It is widely accepted that a finding of expropriation of property under customary international law requires a radical deprivation of a claimant's economic use and enjoyment of its investment. This is the consistent view of previous NAFTA tribunals. "[*T*]*he affected property* must be impaired to such an extent that it must be seen as 'taken'."[85] "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)."[86] It is a view also stated in numerous BIT arbitrations.[87] Therefore, putting to the side the question of sufficiency of the duration of the interference, the Tribunal must find a radical deprivation of the Claimant's economic use and enjoyment of its investment for the period of the interference.

361. The difference between the Parties' perspectives as to the severity of the economic impact in this case again is related to the question of whether it is permissible to raise an Article 1110 claim on the basis of a temporary taking and Claimant's formulation of its claim. To prove the severity of the economic impact of the Mexican measures, Claimant relies on data regarding lost profits as opposed to diminished value of the assets. Claimant explains the rationale behind this distinction: the temporary nature of the alleged expropriation. "The established valuation standard for temporary expropriations is the net loss from lost use of the expropriated property or investment during the expropriation period, which generally equates to the present value of the lost income stream during that period." Respondent, in contrast, both challenges the permissibility of a temporary taking claim and, if such a claim is accepted, focuses its analysis on all of the business streams conducted through the physical assets owned by Claimant in Mexico.

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[85] *GAMI*, Final Award, ¶ 126 (15 Nov. 2004).
[86] *Fireman's Fund*, Final Award, ¶ 176(c) (17 July 2006) (citations omitted).
[87] *See, e.g., Tecmed*, Award, ¶ 115 (29 May 2003).

362. At the outset, the Tribunal notes that the principal and growing aspect of the business of Cargill de Mexico and the Tula distribution centre was, at that time, the sale of HFCS.[88] The HFCS trade was clearly central to the business of CdM as Claimant reports, for instance, that it was forced to close the Tula distribution facility in 1998, when CdM was no longer able to sell HFCS, although it appears that at least some part of the facility was utilized by a Cargill oilseeds operation at different times within this period.[89] Likewise, it is not apparent that management could simply have replaced or sufficiently offset its loss of the sales in the HFCS market with different products. More importantly, it is not at all clear to the Tribunal that the good faith effort of a company to develop new outlets when it has lost business as a result of targeted governmental measures should lead to the loss of that company's claim based on those same measures.

363. The Tribunal also notes, however, that unlike the total cessation of business that one would expect to accompany a physical occupation of a business, Cargill de Mexico was not closed down, the Mexican government did not take control of its management, and CdM was not precluded from all business activity during the period in which the IEPS Tax and the special import permit program were in place. In addition, as the facilities and the overall business structure were still available and always under Claimant's control, there remained the opportunity for Claimant to utilize these assets for other products throughout the period in which trade in HFCS was not a viable option.

364. In fact, it appears to the Tribunal that HFCS, though an important component of the investment, was not the sole business of Cargill de Mexico. Claimant's own expert explains that Cargill de Mexico's Corn Milling division was established in 1993 in Mexico City, "along with the majority of CdM's other operations. Establishing a corn milling division rather than a separate company allowed CdM to take advantage of the synergies with existing CdM operations and to better leverage CdM's existing

[88] *See* Navigant Expert Report (21 Dec. 2006), p. 51, Tbl. 10, titled "Nominal Lost Cash Flows Earned by CdM and Cargill on CdM's HFCS Sales."
[89] *See* E-mail correspondence from Mike Coots to Larry Popp re: Tula Terminal Pics (18 Sept. 2000); E-mail correspondence from Jeff Cotter to Pat Bowe, et al. re: FW: Mexico Status update (26 Oct. 2004).

customer relationships to help drive HFCS sales in the market."[90] Respondent's expert points to an internal Cargill memorandum circulated on 6 September 1994, offering space at the soon-to-be-constructed Tula facility:

> North American Corn Milling (NACM) has recently inaugurated a corn sweetener terminal in McAllen, Texas, and has begun construction on a second terminal at Tula, Hidalgo, in the Mexico City area. Both sites were chosen for their strategic location to serve Cargill businesses, product lines, taking advantage of joint opportunities and synergies. The sites have land available for expansion by other Cargill product lines. In case of interest, please contact: Gordon Adkins ....[91]

In addition, Respondent raises a subsequent memorandum on 9 March 1996, entitled, "Mexico Corn Wet Milling Plant, Tula Hidalgo, Executive Summary," which suggests that other Cargill divisions had indeed moved into the facilities: "Our terminals in McAllen and Tula are today distributing HFCS, Glucose, Soybean oil, and Flour throughout Northern and Central Mexico."

365. Also strongly suggesting the presence of and contribution by other "businesses" administered by Cargill de Mexico and present at CdM's facilities, the Tribunal notes that indeed the gross receipts of Cargill de Mexico increased during the period of interference. Claimant's expert Navigant Consulting quantifies this increase as an annual revenue growth of [redacted]% between fiscal years 1990 and 2006; Cargill de Mexico's gross profits grew an average of [redacted]% during the same period.

366. It is thus clear that Cargill de Mexico retained some businesses and some value during the period in which the Mexican measures were in effect. Therefore, to determine whether or not Claimant's investment has suffered a radical deprivation, it is necessary to assess how greatly the alleged lost sales affected Claimant's investment in CdM, as a whole. In order to evaluate this, the Tribunal determined a "but for net income" that CdM would have earned with its actual income during the period of 2002-2006, combined with the alleged lost income. From here, the Tribunal was able to determine

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[90] Navigant Expert Report (21 Dec. 2006), ¶ 34, citing Witness Statement of Eduardo Ortega, ¶ 30. Claimant's witness, Eduardo Ortega, the individual responsible for development and growth in Latin America since 1999, and who began Claimant's business in Mexico "from the ground up," acknowledges that other Cargill business units operated out of the Tula industrial park. He alleges, however, that each business unit had to purchase and develop its own land at Tula to build its plants and that each division operated independently from both a financial and practical perspective. Rebuttal Witness Statement of Eduardo Ortega, Jr., ¶¶ 1, 10-12.

[91] Comments and Analysis of the *Expert Report of Brent C. Kaczmarek, CFA* dated 21 December 2006, prepared by Navigant Consulting, Inc., Pablo Rión and Associates, ¶ 137 (Apr. 2007), quoting Memorandum from Gordon Adkins to Cargill personnel (16 Sept. 1994).

what percentage the lost sales contributed to this "but for income" and thus what effect their loss would have had on the overall investment. Based solely on Claimant's data, the Tribunal determined that, between 2002 and 2006, the Mexican measures allegedly decreased CdM and Cargill's annual pre-tax earnings by between 33% and 79%.[92]

367. Respondent has raised strong evidence that Cargill de Mexico operated numerous other businesses, besides that of HFCS, some of which have been sufficiently profitable to fuel an increase in revenues during the period in which Claimant was excluded from Mexico's HFCS market. These businesses suggest not only that Claimant never lost control of or access to its investment, but also that although the overall investment of Cargill de Mexico appears to have been harmed by the temporary loss of one of its businesses—high fructose corn syrup—the economic impact of that loss was not so complete as to create an appearance that the investment, in its entirety, was expropriated.

368. On the one hand, under Claimant's analysis, Respondent's measures resulted in a near total loss of the business income stream from Claimant's Mexican HFCS business. On the other hand, adopting Respondent's focus on all business income streams of CdM and the Tula facility, the Tribunal concludes that, in light of the circumstances of this case and the evidence before it with respect to these exhibits and the entire record, Claimant has failed to prove that the damage done by the Mexican measures to its HFCS business resulted in such a substantial diminution of Cargill de Mexico so as to equate to a radical deprivation of Claimant's overall investment.

369. The Tribunal notes that the question of whether the severity of measures alleged to be a temporary taking should be valued in terms of the particular revenue stream affected, or in terms of all of the business streams of the underlying investment, need only be reached if the Tribunal finds that an Article 1110 claim may be based on a temporary taking. It is to this question the Tribunal now turns.

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[92] This percentage diminution was calculated by adding the actual "earnings before tax" derived from CdM's various businesses and Navigant's projected "nominal lost cash flows earned" (lost pre-tax income) and then dividing the lost income by this sum. (For these calculations, the Tribunal relied on Claimant Exhibit 248: "Cargill de Mexico 1991-2006 Financial Statements" for the actual earnings before tax; and Navigant Expert Report (21 Dec. 2006), p. 51, Tbl. 10: "Nominal Lost Cash Flows Earned by CdM and Cargill on CdM's HFCS Sales" for the pre-tax income losses attributed to the lost sales.). These figures are for both CdM and Cargill, Inc.

Duration of the Interference

370. It is accepted that there was not a permanent expropriation of Claimant's investment in Mexico. Given the respective contentions of the Parties, it is also accepted that Claimant was precluded from participating in its HFCS-related activities for at least three years and four months, and perhaps, as asserted by Claimant, for five years or more.

371. The Parties disagree as to whether a claim for damages arising from a temporary expropriation is permitted under NAFTA Article 1110 or under customary international law to the extent that it is assumed that Article 1110 incorporates custom in this regard.

372. "Expropriation" under customary international law involves the taking of property by a State. In the classic form of nationalization, title is transferred to the government. This *de jure* form of expropriation was extended over the decades to include *de facto* takings where, even though there was not a decree transferring title, the property was nonetheless deemed to have been taken. As the *S.D. Myers* tribunal wrote: "In general, the term 'expropriation' carries with it the connotation of a 'taking' by a governmental-type authority of a person's 'property' with a view to transferring ownership of that property to another person, usually the authority that exercised its *de jure* or *de facto* power to do the 'taking'".[93] In both the case of *de jure* and *de facto* takings, the investor was deprived permanently of the property. Article 1110, in using the terms "expropriation" and "tantamount to expropriation", incorporates this customary law of expropriation.

373. Claimant asserts that an expropriation claim may be based on a temporary rather than a permanent taking. In particular, Claimant argues that, if a government temporarily occupied an investor's facility preventing its intended use and later returned the facility to the control of the investor, then the government would be liable to the investor for a temporary taking where the measure of damages would not be the value of the property inasmuch as that which was returned, but rather damages that flow from that interference with the use of the property. Claimant argues that its situation in this case

[93] *S.D. Myers*, Partial Award, ¶ 280 (13 Nov. 2000).

is analogous. Although Respondent did not physically occupy Claimant's facility and deny its intended use, Claimant argues that the effect of Mexico's measures was the same. While Claimant asserts that several authorities support this proposition, the Tribunal does not find them on point.

374. The practice of the Iran-United States Claims Tribunal is not of assistance. The statement in *Tippetts, Abbett, McCarthy, Stratton v. TAMS-AFFA Consulting Eng'rs of Iran* cited by Claimant for the proposition that measures may be expropriatory so long as they are more than "merely ephemeral" does not support Claimant's proposition regarding temporary takings.[94] In *Tippetts*, the tribunal held that "the Claimant has been subjected to 'measures affecting property rights' by being deprived of its property interests in TAMS-AFFA since at least 1 March 1980." In making this holding, however, the tribunal concluded that the property interest in the partnership had been *de facto* permanently taken as of that date. That permanency is reflected in the fact that the tribunal proceeded to calculate damages by ascertaining claimant's interest in the dissolution value of the partnership as of 1 March 1980. The tribunal's reference to not "merely ephemeral" is a statement that the set of actions or measures alleged to give rise *de facto* to a permanent taking may not be merely ephemeral. Judge Brower writes of the *Tippetts* award, that the "merely ephemeral" standard "appears to reflect a realization by the Tribunal that a genuinely temporary assumption of management control would not, without more, constitute a compensable taking."[95]

375. One NAFTA tribunal, without explanation, reserves the possibility of a temporary taking. Contrary to Claimant's position, the tribunal in *S.D. Myers* stated that an expropriation "usually amounts to a lasting removal of the ability of an owner to make use of its economic rights ...." But Claimant relies on the *S.D. Myers* tribunal's immediate statement thereafter that "in some contexts and circumstances, it [is] appropriate to view a deprivation as amounting to an expropriation, even if it [is] partial or temporary."[96] This possibility is neither explained nor supported, however. The *S.D. Myers* tribunal observes that the 18-month period of the measure in that case "may have significance in assessing the compensation to be awarded in relation to

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[94] *Tippets*, 6 Iran-US CTR 219 (Award No. 141-7-2) (1984).
[95] CHARLES N. BROWER AND JASON D. BRUESCHKE, THE IRAN-UNITED STATES CLAIMS TRIBUNAL 399, fn. 1866 (1998). *See also Tippets*, at 414-17.
[96] *S.D. Myers*, Partial Award, ¶ 283 (13 Nov. 2000).

[Canada's] violations of Articles 1102 and 1105, but it does not support the proposition on the facts of this case that the measure should be characterized as an expropriation within the terms of Article 1110,"[97] and in this sense the possibility on which it reserved judgment was not present in the case before it.

376. Finally, the BIT arbitration awards cited to by Claimant appear to not be on point either. The *Wena Hotels* tribunal found a year-long seizure and occupation of, and stripping of property from, a hotel to constitute a *de facto* permanent taking.[98] This permanency is evident in the fact that the loss was not valued in terms of the damages arising as a result of the period of deprivation, but as "the market value of the investment immediately before the expropriation."[99] In *Middle East Cement*, the tribunal found that a conceded deprivation of a license for at least four months amounted to a *de facto* permanent taking of the property right in the license.[100] This permanency is evident in the fact that the loss was not valued in terms of the four month loss but rather the remaining life of the license.[101]

377. It is always possible that there is evidence of practice suggesting that customary international law is changing to address not only claims of expropriation, but also claims for interference with property rights or claims based on other measures affecting property. For this case, such evidence would need to clearly indicate that it establishes an expansion of the scope of expropriation rather than the creation of categories of claims not encompassed within Article 1110. Such evidence, however, has not been presented to this Tribunal.

Final Disposition of the Tribunal with respect to Claim Arising under Article 1110

378. For these reasons, the Tribunal finds that Claimant's Article 1110 claim fails inasmuch as it does not present an instance of expropriation within the scope of Article 1110.

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[97] *Id.* at ¶ 284.
[98] *Wena Hotels*, Award, ¶ 99 (8 Dec. 2000).
[99] *Id.* at ¶ 125.
[100] *Middle East Cement*, Award, ¶ 107 (12 Apr. 2002).
[101] *Id.* at ¶¶ 121-28.

directly on Cargill de Mexico, the Tax, by its very objective and design, involved a performance requirement within the meaning of Article 1106(3). It conditioned a tax advantage on the use of domestically produced cane sugar for the very purpose of affecting the sale of HFCS, and thus, it conditioned an advantage "in connection with" the operation of the Claimant's investment which supplied HFCS to the soft drink bottling industry.

553. The Tribunal finally holds that the wrongfulness of these breaches of Respondent's obligations under NAFTA Chapter 11 is not precluded by Respondent's assertion that its actions were lawful countermeasures. The Tribunal determines that countermeasures operate only to preclude the wrongfulness of an act that is not in conformity with an obligation owed to the offending state, not in regard to obligations owed to a third state nor those, as here, owed to the nationals of the offending state. The Tribunal further determines that, under the NAFTA, investors have both substantive and procedural rights, and investors are therefore protected under Chapter 11 from measures taken by a host state directly against them. This is true even if these same actions might constitute valid countermeasures if taken instead against the offending state, and even despite the fact that such valid countermeasures may in fact result in secondary effects on the nationals of the offending state.

XVI. AWARD AND ORDER

For the foregoing reasons, THE TRIBUNAL AWARDS AND ORDERS AS FOLLOWS:

554. Finds Respondent has acted inconsistently with respect to its obligations under Article 1102 of the NAFTA;

555. Denies Claimant's claim for damages for a breach of NAFTA Article 1103;

556. Finds Respondent has acted inconsistently with respect to its obligations under Article 1105 of the NAFTA;

557. Finds Respondent has acted inconsistently with respect to its obligations under Article 1106 of the NAFTA;

558. Denies Claimant's claim for damages under NAFTA Article 1110;

559. Orders Respondent to pay immediately to Claimant the sum of US $77,329,240;

560. Orders interest to be paid on this Award from 1 January 2008, until payment in full at a rate equal to the U.S. Monthly Bank Loan Prime Rate, compounded annually;

561. Orders Respondent to pay all of the costs of this arbitration and half of Claimant's costs of legal representation and assistance, in addition to its own costs of representation, a total of US $3,296,140; and Claimant to maintain responsibility for the remaining half of its legal representation and assistance costs, or US $1,675,473. Considering the sums already expended, this equates to a payment from Respondent to Claimant of US $2,085,473 for reimbursement of costs;

562. Denies all other claims for compensation.

Doctor Michael C. Pryles
President
Date: AUGUST 13, 2009

Professor David D. Caron
Arbitrator
Date: July 29, 2009

Professor Donald M. McRae
Arbitrator
Date: July 29, 2009

Ad Hoc NAFTA Arbitration under UNCITRAL Rules

CHEMTURA CORPORATION
(formerly Crompton Corporation)

CLAIMANT

V.

GOVERNMENT OF CANADA

RESPONDENT

AWARD

Rendered by an Arbitral Tribunal composed of:

Prof. Gabrielle Kaufmann-Kohler, Chairperson
The Honorable Charles N. Brower, Arbitrator
Prof. James R. Crawford, Arbitrator

Secretary to the Tribunal:
Dr. Jorge E. Viñuales

on the scope of Article 1105. The Claimant argues that the reference in the FTC Note to customary international law entails a standard of treatment that has evolved over time as a result *inter alia* of the conclusion of a large number of BITs providing for fair and equitable treatment of investments. The Respondent replies that the conclusion of BITs is not sufficient to build customary international law and that, in all events, the Claimant has failed to establish the content of the customary standards which it invokes. Both Parties have referred to the decisions of a number of NAFTA tribunals to buttress their respective positions.

121. At the outset, the Tribunal notes that it is not disputed that the scope of Article 1105 of NAFTA must be determined by reference to customary international law. Such determination cannot overlook the evolution of customary international law, nor the impact of BITs on this evolution. As noted by the tribunal in *Mondev v. United States*:

> [B]oth the substantive and procedural rights of the individual in international law have undergone considerable development. In the light of these developments it is unconvincing to confine the meaning of "fair and equitable treatment" and "full protection and security" of foreign investments to what those terms – had they been current at the time – might have meant in the 1920s when applied to the physical security of an alien. To the modern eye, what is unfair or inequitable need not equate with the outrageous or the egregious. In particular, a State may treat foreign investment unfairly and inequitably without necessarily acting in bad faith. [...]

And further:

> [T]he vast number of bilateral and regional investment treaties (more than 2000) almost uniformly provide for fair and equitable treatment of foreign investments, and largely provide for full security and protection of investments. [...] In the Tribunal's view, such a body of concordant practice will necessarily have influenced the content of rules governing the treatment of foreign investment in current international law. [...] It [the term "customary international law"] is not limited to the international law of the 19th century or even of the first half of the 20th century, although decisions from that period remain relevant. In holding that Article 1105(1) refers to customary international law, the FTC interpretations incorporate current international law, whose content is shaped by the conclusion of more than two thousand bilateral investment treaties and many treaties of friendship and commerce".[10]

122. In line with *Mondev*, the Tribunal will take account of the evolution of international customary law in ascertaining the content of the international minimum standard. Such inquiry will be conducted,

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[10] Mondev International Ltd. v. United States of America, ICSID Case No. ARB(AF)/99/2, Award of 11 October 2002, para. 116, 117, 125.

as necessary, in analyzing each specific measure allegedly in breach of Article 1105 of NAFTA.

123. Before undertaking such analysis, the Tribunal deems it necessary to address an additional question concerning the scope of Article 1105 on which the Parties disagree, i.e. whether the protection granted under this provision is lessened by a margin of appreciation granted to domestic regulatory agencies and, if so, to what extent. Having reviewed the arguments of the Parties, the Tribunal is of the opinion that the assessment of the facts is an integral part of its review under Article 1105 of NAFTA. In assessing whether the treatment afforded to the Claimant's investment was in accordance with the international minimum standard, the Tribunal must take into account all the circumstances, including the fact that certain agencies manage highly specialized domains involving scientific and public policy determinations. This is not an abstract assessment circumscribed by a legal doctrine about the margin of appreciation of specialized regulatory agencies. It is an assessment that must be conducted *in concreto*. The Tribunal will proceed to such assessment *in concreto* when reviewing the specific measures challenged by the Claimant.

b. The Review of Lindane

1. Claimant's position

124. In response to an invitation by a Tribunal, the Claimant identified in its Post-Hearing Brief the specific measures that it considers in breach of Article 1105(1) of NAFTA. For the purposes of the analysis, the first and sixth measures identified by the Claimant, both concerning the review process of lindane, can be treated together.

125. The first measure identified by the Claimant is the conduct, by the Respondent, of a seriously flawed and delayed special review, which according to the Claimant resulted in a breach of Article 1105(1) on 19 December 2001, the date when the PMRA determined that termination of lindane products was warranted and could be effected by way of phase-out by suspension of registrations or by way of voluntary discontinuation (Exh. B-56).

126. According to the Claimant, the flaws that affected the conduct of the Special Review can be summarized as follows: (i) the notice of 15 March 1999 announcing the Special Review was unspecific and provided insufficient information with respect to both the concerns underlying the process and the manner in which registrants could participate (PHB Cl., para. 99); (ii) the PMRA failed to timely complete the Special Review, preventing the Claimant from taking appropriate action in the United States to register or obtain a tolerance for the use of lindane on canola (PHB Cl., para. 101); (iii) the PMRA disingenuously failed to clarify the impact of the occupational risk

Protocol to the LRTAP Convention (PHB Resp., para. 24 ff); (ii) the scientific review of lindane falls within acceptable scientific parameters and, given the possibility of reasonable disagreements on the choice of safety factors or on the adequacy of existing data, it is not for the Tribunal to review the scientific basis of the PMRA's decision (PHB Resp., para. 30 ff); (iii) the outcome of the Special Review was not a foregone conclusion (PHB Resp., para. 47 ff); (iv) the Special Review was not fundamentally flawed from a procedural point of view, as the Claimant was given two opportunities at the outset and during the Special Review to ask questions and make comments (including at a high-level meeting between Mr. Ingulli, Chemtura's Executive Vice-President for the Crop Protection Division, and Dr. Franklin, the PMRA's Executive Director), and the announcement of the Special Review mentioned that the review could cover other issues, which included exposure considerations, a standard focus of PMRA evaluation, as acknowledged by the Claimant's witness, Mr. Thomson (PHB Resp., para. 79 ff); (v) the process leading to de-registration, including the Board of Review, provided the Claimant due process (PHB Resp., para. 93 ff).

132. The Respondent further argues that the REN was not biased, nor was it an admission that the Special Review was fundamentally flawed, and, in any event, it cured any alleged deficiencies in the Special Review (PHB Resp., para. 103 ff). The Respondent contends mainly that the evidence gathered at the hearing confirmed that Mr. Worgan had no substantive role in the REN. It refers to the testimony of Dr. Chan pursuant to which Mr. Worgan played a very limited role in the conduct of the risk assessment within the REN process given his managerial coordination role. The Respondent further refers to Mr. Worgan's own testimony that his role was distinct from the risk assessment carried out by the Health and Environmental Directorates (PHB Resp., para. 103 ff). Moreover, the Respondent stresses that the REN team conducting the scientific review was distinct from the original Special Review team. It notes in particular that scientists like Ms. Chaffey had minimal involvement in the REN and no direct involvement in the work of the evaluators (PHB Resp., para. 107). By reference to the testimony of Mr. Worgan, the Respondent finally puts forward that the primary reason for launching the REN was the series of recommendations made by the Board of Review, and that there is no evidence to suggest that the REN was not a good faith scientific process (PHB Resp., para. 108 ff).

3. The Tribunal's determination

133. In its oral and written submissions, the Claimant's argumentation has focused on two main issues. First, the Claimant has argued that the PMRA launched its Special Review of lindane as a result of a trade irritant and not of health and environmental considerations. Second, the Claimant has also argued that the process through which the PMRA reviewed the risks associated with lindane was flawed, scientifically and procedurally, and reached what was in fact a foregone conclusion.

However, the position of the Claimant as to whether lindane itself presents unacceptable health and environmental risks is somewhat ambiguous. Underlying the Claimant's argumentation is the suggestion that lindane could have remained usable, at least on some hypotheses or for a longer time-period than the one eventually decided by the PMRA. Such allegations are made to challenge the manner in which the PMRA conducted the lindane review process rather than the more fundamental question of the risks associated with using lindane.

134. The Tribunal notes at the outset that it is not its task to determine whether certain uses of lindane are dangerous, whether in general or in the Canadian context, as the Claimant acknowledged at the hearing for closing arguments: "As Canada has noted, the rule of a Chapter 11 Tribunal is not to second-guess the correctness of the science-based decision-making of highly specialized national regulatory agencies. We agree with this proposition" (Tr., 17 December 2009, 1423: 18-21).

135. Irrespective of the state of the science, however, the Tribunal cannot ignore the fact that lindane has raised increasingly serious concerns both in other countries and at the international level since the 1970s. The Respondent has amply established the existence of such concerns, by referring *inter alia* to the following examples (C.-Mem., para. 34):

(i) In 1968, Hungary restricted the use of lindane to grain treatment for winter wheat and nurseries;

(ii) In 1971, lindane was banned in Japan;

(iii) In 1974, mixed isomer-based lindane products were banned in Portugal;

(iv) In 1979, the Netherlands prohibited the sale, stocking or use of pesticides containing HCH in all of its isometric forms;

(v) In 1986, South Korea banned the sale and use of lindane and Switzerland severely restricted its sale and use;

(vi) In 1987, Cyprus restricted the use of lindane to wood protection and paints, eliminating agricultural use;

(vii) In 1988, Finland prohibited the use of lindane as a pesticide;

(viii) In both 1978 and 1988, the use of lindane was severely restricted within the European Community;

(ix) In 1988, lindane was banned in Germany;

(x) In 1988, the former USSR prohibited the use of lindane as a pesticide, and severely restricted

all other uses;

(xi) In 1989, lindane was banned in Sweden, and in Belgium its use was restricted to wood treatment and veterinary applications;

(xii) In 1990, lindane was banned in New Zealand and deregistered in Mongolia;

(xiii) In 1991, lindane was banned in Bangladesh and Hong Kong, and its use was severely restricted in Belize and China;

(xiv) In 1992, lindane was banned in Austria and Brazil;

(xv) In 1993, lindane was banned in Bulgaria;

(xvi) In 1994, lindane was banned in Norway;

(xvii) In 1995, lindane was banned in Denmark and its use was severely restricted in Argentina;

(xviii) In 1997, the U.K. Pesticides Safety Directorate (PSD), the U.K. equivalent of the PMRA, initiated a review of lindane. By 1999, the PSD had decided to ban all forms of lindane seed treatment use, on the basis of unacceptable health risks to workers exposed to the chemical during seed treatment;

(xix) In 1998 the Aarhus Protocol on Persistent Organic Pollutants to the UNECE Convention on Long-Range Transboundary Air Pollution of 1979 was adopted by some 30 countries, including the United States, Canada, and most countries of Western and Eastern Europe (this Protocol restricted the use of lindane to six specific uses and required a reassessment of lindane);

(xx) In 1998, lindane was banned in France;

(xxi) In 1998, the EU initiated a complete re-evaluation of lindane which resulted in an eventual Europe- wide ban on plant protection products containing lindane in 2000;

(xxii) At the same time, a number of European countries added lindane to the List of Chemicals for Priority Action under the OSPAR Convention for the Protection of the Marine Environment of the North-East Atlantic, further signalling international concern about the human health and environmental effects of lindane.

136. Moreover, in May 2009, lindane was included in the list of chemicals designated for elimination under the Stockholm Convention on Persistent Organic Pollutants or POPS (Exh. CC-45).

137. This broader factual context is relevant in assessing the first point raised by the Claimant, namely

whether the PMRA undertook the Special Review as a result of a trade irritant and not as a part of its mandate as a regulatory agency or as part of an international commitment undertaken by Canada under the Aarhus Protocol to the LRTAP Convention.[11] Although the Claimant has avoided formulating this allegation in such terms, the underlying idea is that the PMRA acted in bad faith and launched a review process for reasons unrelated to its mandate and to the international obligations of Canada. The burden of proving these facts rests on the Claimant, in accordance with well established principles on the allocation of the burden of proof,[12] and the standard of proof for allegations of bad faith or disingenuous behaviour is a demanding one.[13]

138. In the Tribunal's view, the evidence on the record does not show bad faith or disingenuous conduct on the part of Canada. Quite the contrary, it shows that the Special Review was undertaken by the PMRA in pursuance of its mandate and as a result of Canada's international obligations.

139. Annex II of the Aarhus Protocol expressly provides that "[a]ll restricted uses of lindane shall be reassessed under the Protocol no later than two years after the date of entry in force" (Exh. JW-10). At the hearing on the merits, Dr. Franklin, at the time the Director of PMRA, noted that the conduct of the Special Review was prompted by commitments undertaken by Canada during the negotiation of the Aarhus Protocol:

> Canada was not in a position to sign--other countries had already banned lindane, so that they had no problem with signing a Protocol that, in essence, was leading to an overall ban. For them the situation was very clear: It didn't make a difference. It was gone in their country, so they could sign that because, in effect, they had already done that. We had registered products in Canada, and we had not done a review, so that there was no way that we were in a position to support a Protocol that, in effect, was going to ban them [...]
>
> Everybody was pressuring. I mean, my goodness, countries that had already banned lindane very much wanted other countries that were still using it to stop because, of course, their use could contribute to long-range transboundary, which could then, even though a country had banned it, they could still end up being exposed to it. So, the whole purpose of these international POPs Conventions was to find a way to deal with it. Our position was that that could well be the case. But I think it really points out or should point out to everybody that we were not going to take action to ban. This wasn't a preconceived idea that Canada had that they were going to ban this, regardless. We clearly stated that we had to do a review to make a decision as to whether a ban was acceptable or not, so that there was not--there was not a—we hadn't taken a decision ahead of time as to what the outcome would be--that was based on the scientific review--despite the pressure from many other countries." (Tr., 7 September 2009, 1072-1074).

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11 Protocol to the Convention on Long-Range Transboundary Air Pollution on Persistent Organic Pollutants (Aarhus Protocol) (Exhibit JW-IO).

12 *See* Article 21, UNCITRAL Arbitration Rules.

13 *See* Bayindir Insaat Turizm Ticaret VE Sanayi A.S. v. Islamic Republic of Pakistan, ICSID Case No ARB/03/29, Award of 27 August 2009, para. 143.

140. The oral testimony of Dr. Franklin is corroborated by the testimony of three other witnesses. Examined on the reasons for the launch of the Special Review, Ms. Chaffey, Head of the Toxicology Re-Evaluation Section of the PMRA's Health Evaluation Directory, stated that the PMRA

> launched the Special Review in response to both domestic concerns such as those that were articulated in the Northern Contaminants Program Report on contaminants in the Arctic environment as well as international concerns that were specifically addressed through the United Nations LRTAP program (Tr., 3 September 2009, 457:9-14).

141. Similarly, asked in cross-examination about the uses of lindane that Canada retained under the Aarhus Protocol, Mr. Worgan, at the time PMRA's Head of Exposure Assessment, declared that

> Canada agreed to put those into that list of restricted uses because those were currently registered—at that time they were registered in Canada, and we would not have been able to agree to a ban until such time that we had done like a full re-assessment of that, and that's exactly what we committed to do at the Aarhus Protocol meeting (Tr., 4 September 2009, 564: 23-25, 565:1-3).

142. In the same vein, Ms. Sexsmith, at the time the Director of the Alternative Strategies and Regulatory Affairs Division of the PMRA, made the following statements:

> Q. Would it be fair to say that that wanting by the Canola Council of a VWA was very consonant with the desire of the PMRA to phase out all uses of lindane?
>
> A. No. I would say at that point in time they were mutually exclusive. Lindane was an older product. And according to the new re-evaluation policy that was being developed, it would naturally fall into the queue for review. And then with the international activity around concerns for lindane, Canada would be required to do a review, but requiring--being required to do a scientific review is quite different than getting rid of a product because the scientific review has to come first. So--and the upshot or the result of a scientific review, it could be positive or negative. So, you know, if you're saying that because the Canola Council wanted to get rid of it that lined up with PMRA's view of wanting to get rid of it, I have to say categorically, no, because we don't have personal views of products. We're a regulatory organization. We regulate. We ensure health and environmental safety. And it's the science that tells us whether or not it meets those provisions. So, for us to make a conclusion before we've done the work is not something that we do as an organization, so I would just have to say no to your statement (Tr., 5 September 2009, 817:10-25, 818:1-8).

143. On the basis of this evidence, the Tribunal concludes that the Claimant's allegations of bad faith in

connection with the launching of the Special Review of lindane have not been established.

144. Regarding the second broad allegation of the Claimant, namely that the lindane review process and more specifically the Special Review and the REN were flawed, the Tribunal notes as a preliminary matter that the Claimant approaches the review of lindane not as an overall process (starting with the Special Review, continuing with the assessment of the Board of Review, and ending with the REN), but rather as separate measures, two of which (the Special Review and the REN) are said to be in breach of Article 1103 of NAFTA. Aside from the fact that the conclusions of the Board of Review are relatively more favourable to the Claimant than those of the Special Review and the REN, the rationale for separating the three phases of one and the same process is not entirely clear. Without framing its allegations expressly in such terms, the Claimant has suggested that both the Special Review and the REN were flawed because they were conducted in bad faith in order to reach the foregone conclusion that lindane was to be banned. The key argument in challenging the legitimacy of the REN is that its results were allegedly influenced by Mr. Worgan, who had previously taken an important part in the Special Review, as well as by the litigation needs of the Respondent in the present case. Such allegation might provide a possible rationale for distinguishing between, on the one hand, the Special Review and the REN, both conducted in bad faith by the PMRA, and, on the other hand, the assessment of the Board of Review. However, such distinction would be dependent on the underlying contention that the PMRA acted in bad faith since the beginning of the overall review process.

145. Thus, in assessing the measures identified by the Claimant as allegedly in breach of Article 1105 of NAFTA, the Tribunal must first determine whether the Special Review was conducted in such a manner as to reflect bad faith on the part of the PMRA. If this is not the case, the allegation of bad faith in the conduct of the REN would also have to be discarded. To this first inquiry, the Tribunal must however add a second one, namely whether the review of lindane (even if in good faith), breached the due process rights of the Claimant. Such inquiry must take into account the review process as a whole, including the procedure before the Board of Review, as an additional opportunity offered to the Claimant to put forward its position. Indeed, the mechanisms for the review of regulated products, such as lindane-based products, as well as those applicable to the consequences of such review, are set out in a complex array of laws and regulations, the purpose of which is precisely that any decisions taken by the authorities in this context are subject to procedural checks and balances. The establishment of the Board of Review was an important component of such arrangements, as was the REN. In assessing whether the alleged procedural deficiencies attributable to the Respondent involved a breach of Article 1105 of NAFTA, the Tribunal should not limit its inquiry to a specific portion of such arrangements. It must appraise any procedural deficiency in the light of the mechanisms provided by the Respondent itself to manage such

239. With respect to the applicable standard, the Claimant puts forward the following arguments: (i) the concept of "measure" is defined in Article 201(1) NAFTA as "any law, regulation, procedure, requirement or practice"; (ii) an expropriation may be direct or indirect, as recognized *inter alia* by the tribunals in *Metalclad v. Mexico* and *Pope & Talbot v. Canada*; (iii) the threshold for an indirect expropriation is that of a "substantial deprivation", as noted in *Pope & Talbot;* (iv) the intent behind a measure is irrelevant, as noted in *Tippetts*, *Biloune v. Ghana*, and *Vivendi II*; (v) expropriation may affect tangible or intangible property, as recognized by *S.D. Myers v. Canada* (Mem., para. 495 ff).

2. Respondent's position

240. According to the Respondent, NAFTA tribunals, and particularly those in *Pope & Talbot v. Canada*, *Metalclad v. Mexico,* and *Methanex v. United States,* have developed a three-step methodology to assess an expropriation claim. The first step consists in determining whether there is an investment capable of being expropriated. The Respondent argues that elements of the value of the enterprise such as goodwill, market share, and customers are not investments under Article 1139 and hence cannot be subject to expropriation. In the event that there is an investment, the next step is to inquire whether that investment has been expropriated. If it has, then the third step is to assess whether the investment has been expropriated in a manner consistent with the conditions found in Articles 1110(1)(a) to (d), i.e. whether the expropriation is lawful or not (C-Mem., para. 503). The Respondent also notes that under international law an act of compulsion by the expropriating State is required for a finding of expropriation (C-Mem., para. 16, 500, 651 ff).

3. Tribunal's determination

241. Article 1110(1) of NAFTA reads in relevant part as follows:

> 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
>
> (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.

242. For a measure to constitute expropriation under Article 1110 of NAFTA, it is common ground that (i) bad faith on the part of the Respondent is not required, and (ii) the measure must amount to a substantial deprivation of the Claimant's investment (Reply, para. 550; C.-Mem., para. 531). Nor is it disputed that, in assessing an expropriation claim, the practice of NAFTA tribunals has been to

follow a three-step approach focusing on (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 in Article 1110(1)(a)-(d) have been satisfied. However, there is some divergence of views between the Parties on two issues.

243. The first controversial issue is whether elements such as goodwill, customers or market share are covered by the definition of investment given in Article 1139 of NAFTA (C.-Mem., para. 494-529). For purposes of the present case, the Tribunal does not need to determine whether such elements may be considered as investments *per se*, as the Claimant has expressly recognized that this was not its argument (Reply, para. 548). The Tribunal notes, however, that such elements may be accessory to one of the forms of "investments" within the meaning of Article 1139. Thus, goodwill or market position may indeed be seen as accessories of an "enterprise", which is *per se* an investment under Article 1139 of NAFTA.

244. The second issue in dispute concerns the definition of the "substantial deprivation" test. While both Parties refer to essentially the same NAFTA cases, their understanding of the "substantial deprivation" test diverges, particularly with respect to the use of the criteria identified in *Pope & Talbot v. Canada*, and to the weight of *Metalclad v. Mexico*. Because of this divergence, the Tribunal deems it useful to clarify the content of that test.

245. In *Pope & Talbot*, the tribunal referred to a number of criteria to determine whether there had been an indirect expropriation, including: (i) whether the investor remained in control of its investment, (ii) whether it directed its day-to-day operations, (iii) whether its officers and employees were detained by the State, (iv) whether the State supervised the work of the investor's officers and employees or not, (v) whether the State had taken the proceeds of sales other than through taxation, (vi) whether the State interfered with management or shareholders' activities, (vii) whether the State prevented the distribution of dividends to shareholders, (viii) whether the State interfered with the appointment of directors or management, and (ix) whether the State had taken any other actions ousting the investor from full ownership and control of the investment.[17]

246. The Claimant has argued that "whilst the degree of control retained in the investment following an alleged indirect expropriation may be a factor that a tribunal could consider in determining whether a governmental act (or acts) rises to the level of a treaty breach, it is not the exclusive or even a necessary factor in this determination" (Reply, para. 554). The Respondent places much stronger emphasis on the degree of interference with the investor's ownership and control of its investment as

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[17] Pope & Talbot v. Canada, UNCITRAL (NAFTA), Award of 26 June 2000, para. 100.

part of the substantial deprivation test.

247. In the opinion of the Tribunal, the divergence of views between the Parties regarding the use of the criteria mentioned in *Pope & Talbot* is not fundamental. Indeed, the Respondent has not seriously argued that each such criterion or at least some of them must be present for a deprivation to be "substantial". The criteria must thus guide the inquiry of the Tribunal when it seeks to determine whether the effects of the measures challenged are to "substantially" deprive the investor of the benefit of its investment. This is a matter of degree and not one of specific conditions.

248. This being so, the Parties also disagree on the degree required for deprivation to be substantial. The Claimant has referred to *Metalclad v. Mexico*, where the tribunal reasoned that "expropriation under NAFTA includes [...] also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State."[18] Mexico sought judicial review of this award before the Supreme Court of British Columbia on various grounds.[19] Although the award was not set aside on the issue of the definition of expropriation, Justice Tysoe noted that the tribunal's characterization of expropriation was "extremely broad."[20] The award in *Metalclad v. Mexico* has given rise to some controversy as to the degree of the required deprivation.

249. The Tribunal is however of the view that it does not need to settle that legal controversy to decide the case before it. The determination of whether there has been a "substantial deprivation" is a fact-sensitive exercise to be conducted in the light of the circumstances of each case. This observation has also been acknowledged by the Parties (Reply, para. 557: C.-Mem., para. 503). One important feature of fact-sensitive assessments is that they cannot be conducted on the basis of rigid binary rules. It would make little sense to state a percentage or a threshold that would have to be met for a deprivation to be "substantial" as such *modus operandi* may not always be appropriate. For instance, one could think of cases where one specific asset (a building, a piece of land, a line of business) which represents a part of the value of all the different assets held by a foreign investor in the host State has been entirely expropriated. In such case, applying a percentage or threshold approach to the overall assets held by the investor in the host State would preclude the deprivation from being "substantial", whereas applying the same assessment to the specific asset in question would lead to

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18 Metalclad Corporation v. United Mexican States, CASE No. ARB(AF)/97/1, Award of 2 September 2000, para. 103.

19 United Mexican States v. Metalclad Corporation, decision of 2 May 2001, 2001 BCSC 664.

20 *Ibid*., para. 99.

the opposite conclusion. Given the diversity of situations that may arise in practice, it is preferable to examine each situation in the light of its own specific circumstances.

250. The Tribunal turns then to the analysis of the measures allegedly amounting to an expropriation in breach of Article 1110 of NAFTA.

b. Cancellation of Chemtura's lindane registrations

1. Claimant's position

251. The Claimant argues that the PMRA's suspension of Crompton Canada's lindane product registrations were measures tantamount to expropriation (Mem., par. 519-520). These measures were not taken for a public purpose, as the PMRA had no new, pertinent or reasonable scientific rationale. The measures were in fact triggered by trade considerations and the related pressure from the United States (Mem., para. 521 ff). Moreover, the expropriation of the Claimant's lindane products business in Canada violated due process and was in breach of international law (Article 1105(1) of NAFTA), for reasons explained under the minimum standard heading (Mem., para. 527 ff). Finally, Canada paid no compensation (Mem., para. 531-532).

2. Respondent's position

252. The Respondent argues that only Chemtura Canada, the Claimant's enterprise as a whole, qualifies as an investment capable of being expropriated. Elements of the value of the enterprise such as goodwill, market share, and customers are not investments under Article 1139 and, hence, cannot be expropriated investments for the purposes of NAFTA (C-Mem., para. 500, 516).

253. Further, according to the Respondent, there has been no substantial deprivation of the Claimant's investment (C-Mem., par. 531 ff) because (i) the Withdrawal Agreement and PMRA's subsequent decision to phase out lindane use in general (not only for canola) had only a limited impact on Chemtura Canada; (ii) Canada never controlled the Claimant's investment, directed its operations, took proceeds of sales, intervened in management or shareholder activities, or otherwise interfered with it in any manner that can be characterized as expropriation or conduct tantamount to expropriation. In reality, the Claimant controlled all aspects of Chemtura Canada's operations; was granted an extended phase-out period during which it could deplete its lindane stock; was permitted to sell two replacement pesticide products in Canada even before the beginning of the phase-out period; and was consistently profitable before, during, and after the ban on lindane was instituted (C-Mem., para. 500). According to the Respondent, the hearing further confirmed that the Claimant was not substantially deprived of its investment (PHB Resp., para. 217 ff).

254. Even if the Tribunal concluded that there was a substantial deprivation of the Claimant's investment, there was still no expropriation because the PMRA's decision to phase out all agricultural applications of lindane was a valid exercise of Canada's police powers to protect public health and the environment (C-Mem., para. 500 and para. 565 ff). The decision of the PMRA to de-register lindane meets the test of this doctrine because (i) it was not made in an arbitrary manner since it respected due process and was based on valid science (C-Mem., para. 596 ff); (ii) it was non-discriminatory (C-Mem., para. 613 ff); (iii) it was not excessive (C-Mem., par. 622 ff); and (iv) it was made in good faith to combat the serious occupational exposure risks posed by lindane (C-Mem., para. 630 ff; PHB Resp., para. 219-220).

255. The Respondent further notes that the hearing confirmed that the Claimant entered into the Withdrawal Agreement voluntarily. As result, it cannot now claim that its investment with respect to lindane use on canola was expropriated (PHB Resp., para. 221 ff).

256. Finally, as there is no expropriation for the Respondent, there is no need to consider the conditions set by Article 1110(1)(a) to (d) for a lawful expropriation (C-Mem., para. 660).

3. Tribunal's determination

257. As noted above, in assessing a claim of expropriation, NAFTA tribunals have followed a three-step approach inquiring (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 in Article 1110(1)(a)-(d) had been satisfied. The application of the test is not disputed in the present case, and the Tribunal sees no reason to depart from such approach. There is, however, some divergence of views between the Parties on two issues.

258. The first issue is whether the Claimant had an investment in Canada capable of being expropriated. Despite some initial disagreement as to the identification of the Claimant's investment, the Parties agree that the investment allegedly expropriated is Chemtura Canada (or its predecessors in title) (Reply, para. 537; C.-Mem., para. 504ff). Such investment falls squarely under the definition of "investment" given in Article 1139 of NAFTA, according to which "investment means: (a) an enterprise [...]". The Tribunal also considers, as noted in the foregoing section, that elements such as goodwill, customers or market share, or those covered under the more generic heading of the Claimant's "lindane business" in Canada, are part of the overall investment which Chemtura Canada represented. Therefore, the Tribunal concludes that the first part of the test is satisfied.

259. The second part of the test focuses on whether the Claimant's investment, Chemtura Canada, was in

fact "expropriated" or "taken". As discussed above, in assessing whether the Claimant has suffered an indirect expropriation or a measure tantamount to expropriation, the Tribunal must determine whether the measures challenged under this heading, i.e. the cancellation of Chemtura Canada's lindane registrations, amounted to a "substantial deprivation" of the Claimant's investment. As noted by the Tribunal in paragraph 249 above, the determination of whether there has been a substantial deprivation must be based on a fact-sensitive assessment. The Tribunal will thus consider the facts on record which may give the measure or degree of the deprivation allegedly suffered by the Claimant.

260. A first indication of the impact of the measures challenged on the Claimant's overall investment is provided in the Damages Assessment Report presented by the Claimant. In explaining why the book value approach is not suitable in this case, the Claimant's expert states that "prior to the measures Crompton's lindane products represented a small share of its overall business" (LECG Report, para. 57). This assertion is further elaborated in a footnote, stating that "[p]rior to the measures in 1999, lindane based products represented around 6.3% of Crompton's overall Canadian business measured by output (pounds) and approximately 17.6% measured by net sales" (LECG Report, para. 57, footnote 27).

261. Second, at the hearing, Mr. Thomson, at the time Formulations Manager of Chemtura Canada, testified (i) that Claimant's crop protection business was at all relevant times only 10% of the sales of the company (Tr., 3 September 2009, 321:9-14). (ii) that 80% of the crop protection business of Chemtura Canada was seed treatment (the percentage of crop protection business relative to the overall business of Chemtura Canada was not specified by the witness) (Tr., 3 September 2009, 322:22-25, 323:1-2), and (iii) that sales from lindane products were no more than 5% of the overall sales from the crop protection business (itself a subset of the overall sales) of Chemtura Canada (Tr., 3 September 2009, 324:24-25, 325:1-9).

262. These indications are confirmed by the second report of the Respondent's quantum expert, where it is stated that: "after being provided with further financial statements for the crop protection division and the lindane product lines by Claimant, we were able to confirm our previous conclusions [...]. Chemtura Canada's financial statements reveal that net sales of lindane-based products represented approximately 10 percent of Crompton Canada's sales" (Second Navigant Report, para. 128).

263. The Tribunal gathers from this evidence that the sales from lindane products were a relatively small part of the overall sales of Chemtura Canada at all relevant times. Under these circumstances, the interference of the Respondent with the Claimant's investment can not be deemed "substantial".

264. This conclusion is also supported by the fact that Chemtura Canada remained operational and its yearly sales, although reduced in 2002, continued an ascending trend between 2003 and 2007 reaching levels comparable to those of 1997 to 1999 (Exh. NCI-3). Finally, there is no allegation that the Respondent interfered with Chemtura Canada's management, daily operations, or the payment of dividends, in other words, the Claimant remained at all relevant times in control of its investment.

265. In summary, the evidence shows that the measures did not amount to a substantial deprivation of the Claimant's investment.

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. As discussed in detail in connection with Article 1105 of NAFTA, the PMRA took measures within its mandate, in a non-discriminatory manner, motivated by the increasing awareness of the dangers presented by lindane for human health and the environment. A measure adopted under such circumstances is a valid exercise of the State's police powers and, as a result, does not constitute an expropriation.[21]

267. Consequently, the Tribunal comes to the conclusion that the Respondent did not breach Article 1110 of NAFTA.

E. COSTS

268. Each Party has advanced costs in the amount of USD 410'000[22], which gives a total advance of USD 820'000. The Claimant has filed a statement of legal and other costs in the amount of USD 1'294'640 while the Respondent's fees and expenses incurred in connection with this arbitration amounted to CAD 5'778'467.60. Considering the stakes involved in this case, these amounts appear reasonable.

269. The members of the Tribunal have spent time on this matter, as follows: The Honorable Charles Brower 30 days; Prof. James Crawford 25.5 days; and Prof. Gabrielle Kaufmann-Kohler 66.5 days. The Secretary of the Tribunal has spent 356 hours. The rates for time spent by the Tribunal and Secretary on this case were set in section C of PO 1 (USD 4'000 per day or 8 hours of work for the Arbitrators and USD 280 per hour for the Secretary). Accordingly, the total fees accrued for the

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21 Cf. in a different context *Saluka Investments B.V. v Czech Republic*, UNCITRAL Rules, Partial Award of 17 March 2006, para. 262.

22 Canada's Submission on Costs states this amount in CAD 477'602.07.

Tribunal and the Secretary amount to USD 587'680.

270. The PCA's fees amount to USD 2'286 and the Tribunal's expenses to USD 98'253 (including in particular costs for the various hearings and deliberations).

271. Adding up expenses, PCA and Arbitrators' fees, the total costs of the arbitration amount to USD 688'219, with an unused remainder of the advance of USD 131'781

272. The Respondent has prevailed in the present proceedings. In the exercise of its discretion under Article 38 of the UNCITRAL Arbitration Rules in matters of allocation of costs, the Tribunal finds it fair that the Claimant bear the entire costs of the arbitration, i.e. USD 688'219. Since the Parties have advanced USD 820'000 in equal shares, the PCA will refund the totality of the remainder of USD 131'781 to the Respondent, out of which USD 65'890.50 will be credited towards the Claimant's remaining payment obligation on account of arbitration costs, which thus amounts to USD 278'219, i.e. 688'219 : 2 = 344'109.50 minus 65'890.50.

273. The Tribunal finds it further appropriate and just that the Claimant bear one half of the fees and costs expended by the Respondent in connection with this arbitration, i.e. CAD 2'889'233.80.

V. DECISION

[274] For the reasons set forth above, the Tribunal issues the following Award:

a. The Tribunal has jurisdiction to hear the claims brought in the present proceedings;

b. The Respondent has not breached Article 1105 of NAFTA;

c. The Respondent has not breached Article 1103 of NAFTA;

d. The Respondent has not breached Article 1110 of NAFTA;

e. The Claimant shall bear the costs of the arbitration, which are fixed at USD 688'219. Consequently, the PCA shall pay the unused advance of USD 131'781 to the Respondent and the Claimant shall pay USD 278'219 to the Respondent within 30 days of notification of this award;

f. The Claimant shall bear 50% of the Respondent's fees and costs incurred in connection with this arbitration and shall thus pay CAD 2'889'233.80 to the Respondent within 30 days of notification of this award;

g. All other claims are dismissed.

Date: 2 August 2010

Place of the arbitration: Ottawa, Canada

The Hon. Charles N. Brower

Prof. James R. Crawford

Prof. Gabrielle Kaufmann-Kohler

INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

WASHINGTON, D.C.

IN THE PROCEEDING BETWEEN

LIBANANCO HOLDINGS CO. LIMITED
(CLAIMANT)

AND

REPUBLIC OF TURKEY
(RESPONDENT)

(ICSID CASE NO. ARB/06/8)

AWARD

Members of the Tribunal:
Mr Michael Hwang S.C., *President*
Mr Henri C. Alvarez Q.C., *Arbitrator*
Sir Franklin Berman Q.C., *Arbitrator*

Secretary of the Tribunal:
Ms Martina Polasek

Date of Dispatch to the Parties: 2 September 2011

REPRESENTATION OF THE PARTIES

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Ms Arzu Coşar and
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> *"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".*

112. Additionally, it is common ground between the Parties that Turkish law applies to the issue of whether (and when) Libananco acquired the shares in question and thus had an "Investment" under Article 26(1) of the ECT and Article 25(1) of the ICSID Convention. In interpreting the provisions of the ECT and the ICSID Convention, the Tribunal has considered previous ICSID decisions and awards relied on by the Parties.

113. Accordingly, in this Award, the Tribunal will apply the provisions of the ECT and the ICSID Convention. The Tribunal will also apply Turkish law (evidence of which has been given by both Parties) to determine whether there has been a valid transfer of the shares in question to Libananco as this is a question of domestic law.

VIII. BURDEN AND STANDARD OF PROOF

114. The Tribunal now turns to consider the issue of which Party bears the burden of proof in relation to the facts and assertions advanced by each of them. It is necessary to set the stage at the outset since the Parties differ fundamentally as to the issue of burden of proof.

A. The Claimant's position

115. The Claimant, in the C.M, made the argument initially that the Tribunal should, at the jurisdictional phase, accept *pro tem* the facts alleged by the Claimant as substantiation for its claims of breach. In support of this proposition, the Claimant cited the case of *Kardassopoulos v Georgia*, ICSID Case No. ARB/05/18 (Decision on Jurisdiction of 6 July 2007) (quoting *Siemens v Argentina*, ICSID Case No. ARB/02/8, (Decision on Jurisdiction, 4 August 2004, at paragraph 180), at paragraph 103:

> *"At this stage of the proceedings, the Tribunal is not required to consider whether the claims under the Treaty made by [Claimant] are correct. This is a matter for the merits. The Tribunal simply has to be satisfied that, if Claimant's allegations would be proven correct, then the Tribunal has jurisdiction to consider them".*

However, in the C.Rej, the Claimant recognised and admitted that the latter submission had been made at a time when the Respondent had not yet raised any objections to the Tribunal's jurisdiction. The Claimant has since expressly recognised that it bears the burden of demonstrating its timely ownership of the bearer share certificates in question, and has indeed put forward substantial

documentary, testimonial and forensic evidence in that regard in the course of these proceedings.

116. However, in relation to the remaining three Preliminary Jurisdictional Objections, the Claimant has pleaded the principle of *actori incumbit probatio* (i.e. he who asserts must prove). Specifically, the Claimant has submitted that the Respondent bears the burden of proving the legal theories on which it relies and that the latter are applicable to the facts in the present case. The Claimant's argument is this.

116.1 With respect to the Respondent's assertion that Libananco's legal personality has been "misused" for purposes of perpetrating a "fraud" (i.e. the second Preliminary Jurisdictional Objection set out in paragraph 105.2 above), it is a general principle of law that *"good faith is to be presumed, whilst an abuse of right is not"*.[1] Thus, *"It rests with the party who states that there has been such a misuse to prove his statement"*.[2]

116.2 With respect to the Respondent's contention that it has limited its consent to arbitration of the present dispute (i.e. the third Preliminary Jurisdictional Objection set out in paragraph 105.3 above), general principles of law dictate that:

> *"whoever will derive to himself any advantage by the exception to a general rule, or by interference with the generally acknowledged rights of another, is bound to prove that his case is completely within the exception"*.[3]

Accordingly, it is for the Respondent to prove that it has limited its consent to arbitration.

116.3 In relation to the Respondent's argument that it is entitled to invoke Article 17 of the ECT to deny Libananco the benefits of Part III of the treaty (i.e. the fourth Preliminary Jurisdictional Objection set out in paragraph 105.4 above), this constitutes an affirmative defence on the merits. In *Generation Ukraine v Ukraine*, ICSID Case No. ARB/00/9 (Award dated 16 September 2003), it was held by the tribunal that (at paragraph 15.7):

> *"In the absence of any competing considerations advanced by the Respondent, the Tribunal is satisfied that "third country control" over Generation Ukraine is a prerequisite for any purported invocation of Article I(2) by the Respondent. Furthermore,* ***the burden of proof*** *to establish the factual basis of the "third country control", together with*

[1] Citing Bin Cheng, *General Principles of Law as Applies by International Courts and Tribunals* (Cambridge 2006) at 305.

[2] Citing Bin Cheng, *General Principles of Law as Applies by International Courts and Tribunals* (Cambridge 2006) at 305 (quoting *Certain German Interests in Polish Upper Silesia* (F.R.G. v. Pol.), 1926 P.C.I.J. (ser. A) No. 7, at 30 (1926)).

[3] Citing Bin Cheng, *General Principles of Law as Applies by International Courts and Tribunals* (Cambridge 2006) at 306 (quoting *Jay Treaty (Art. VII) Arb* (1794) 4 INT. ADJ. M.S. 372 at 407).

the other conditions, ***falls upon the State as the party invoking the "right to deny"*** *conferred by Article 1(2)".*

(emphasis added by Claimant)

The Claimant also cited the case of *AMTO LLC v Ukraine*, Arbitration Institute of the Stockholm Chamber of Commerce, Arbitration No. 080/2005, Final Award (2008), which it argued reached a similar conclusion (at paragraphs 64 to 65):

"[W]hen a respondent alleges that the claimant is of the class of Investors only entitled to defeasible protection, so that the respondent can exercise its power to deny, then the burden passes to the respondent to prove the factual prerequisites of Article 17 on which it relies".

117. Further, with respect to the Respondent's submission that the equitable doctrine of veil-piercing applies in the present case such that Libananco does not qualify as an "Investor" for the purposes of the ICSID Convention and the ECT (i.e. the second Preliminary Jurisdictional Objection set out in 105.2 above), the Claimant has contended that since the Respondent's arguments here are premised upon the existence of "fraud or other serious wrongdoing", a heightened standard of proof should apply. The Claimant has cited, among other things, the following authorities in support of this proposition:

(a) the *Case Concerning Oil Platforms (Iran v. U.S.)*, 1996 I.C.J. Rep. 856, (Separate Opinion of Judge Rosalyn Higgins) ("*Oil Platforms case*") where it was observed that: *"the graver the charge, the more confidence there must be in the evidence relied on"*; and

(b) the decision in *Siag and Vecchi v. Egypt*, ICSID Case No. ARB/05/15 (Award dated 11 May 2009), where the tribunal reasoned as follows (at paragraphs 325 to 326):

"For reasons summarised above, the Claimants have submitted that Egypt must prove its Lebanese nationality objection to a heightened standard of proof. Chief among the reasons cited by Claimants is that Egypt's Lebanese nationality application rests upon allegations of fraud, and that claims of such nature are typically held to a heavy standard of proof. The standard suggested by the Claimants was the American standard of "clear and convincing evidence," that being somewhere between the traditional civil standard of "preponderance of the evidence" (otherwise known as the "balance of probabilities"), and the criminal standard of "beyond reasonable doubt."

The Tribunal accepts the Claimants' submission. ***It is common in most legal systems for serious allegations such as fraud to be held to a high standard of proof. The same is the case in international proceedings****, as can be seen in the cases cited by*

> *Claimants, among them the Award of the ICSID Tribunal in Wena Hotels. Egypt's principal submission was that the burden of proof was on Mr Siag, a submission which the Tribunal has rejected so far as the proof of fraud or other serious misconduct is concerned. Egypt did not submit that, if it were required to prove fraud, it should be held to a lesser standard than that argued by the Claimants.* ***The Tribunal accepts that the applicable standard of proof is greater than the balance of probabilities but less than beyond reasonable doubt. The term favoured by Claimants is "clear and convincing evidence." The Tribunal agrees with that test****".*
>
> (emphasis added by Claimant, citations omitted)

B. The Respondent's position

118. The Respondent's position is simply that the Claimant bears the burden of proof with respect to all elements required to establish the jurisdiction of the Tribunal (including, among other things, that Libananco was an "Investor" under the ECT and the ICSID Convention and that it owned a qualifying "Investment" under those instruments at all material times).

119. The Respondent has taken the position that, during an initial jurisdictional phase, a *prima facie* case on the merits may suffice to overcome an objection that a claimant has failed to state a cognisable claim, since a tribunal will wish to avoid pre-judging disputed factual issues on the merits in adjudicating such an objection. However, with respect to jurisdictional facts (such as the existence or lawful ownership of an investment), mere allegations are insufficient. These facts must be proven, and the burden to do so rests squarely on a claimant. In support of this proposition, the Respondent has cited, among other things, the *Oil Platforms case* (Separate Opinion of Judge Higgins, at paragraphs 32 to 34):

> *"The only way in which, in the present case, it can be determined whether the claims of Iran are sufficiently plausible based upon the 1955 Treaty is to accept pro tem the facts as alleged by Iran to be true and in that light to interpret Articles I, IV and X for jurisdictional purposes – that is to say, to see if on the basis of Iran's claims of fact there could occur a violation of one or more of them.*
>
> *… The Court should thus see if, on the facts as alleged by Iran, the United States actions complained of might violate the Treaty articles.*
>
> *Nothing in this approach puts at risk the obligation of the Court to keep separate the jurisdictional and merits phases….What is for the merits…is to determine what exactly the facts are, whether as finally determined they do sustain a violation of, for example, Article X; and if so, whether there is a defence to that violation, lying in Article XX or elsewhere. In short, it is at the merits that one sees "whether there really has been a breach.""*

(citations omitted)

120. In response to the Claimant's argument that the standard of proof with respect to the determination of the second Preliminary Jurisdictional Objection (set out in paragraph 105.2 above) should be heightened, the Respondent has submitted, among other things, that the Claimant's contention that a heightened standard *"is common practice in municipal legal systems"* is not correct. In civil law systems, there is no special standard of proof applicable in cases involving fraud. The Respondent has submitted that, under English law, the standard of proof does not change simply because fraud has been alleged. It says the decision of the English House of Lords in *In re Doherty* [2008] UKHL 33 is instructive (at paragraphs 25 and 28):

> *"Fraud is usually less likely than negligence ... [T]his does not mean that where a serious allegation is in issue the standard of proof required is higher ...*
>
> *[I]n some contexts a court or tribunal has to look at the facts more critically or more anxiously than in others before it can be satisfied to the requisite standard. The standard itself is, however, finite and unvarying. Situations which make such heightened examination necessary may be the inherent unlikelihood of the occurrence taking place ..., the seriousness of the allegation to be proved or, in some cases, the consequences which could follow from acceptance of proof of the relevant fact".*
>
> (citations omitted, underline added by Claimant)

C. Analysis

121. The Tribunal notes that, in relation to the issue of whether Libananco acquired timely ownership of the share certificates in question (i.e. the first Preliminary Jurisdictional Objection set out in paragraph 105.1 above), it is now common ground between the Parties that the Claimant has the burden of proof. However, for the avoidance of doubt, the Tribunal confirms its view that it is not required to make a *pro tem* assumption of the truth of a fact if the evidence of that fact has been fully presented, and sufficient evidence exists for the Tribunal to make an informed and dispositive finding at this stage.

122. The Tribunal is assisted by the following remarks of the tribunal in *Phoenix Action, Ltd. v Czech Republic*, ICSID Case No. ARB/06/5 (Award dated 15 April 2009) ("*Phoenix Action*") (at paragraphs 60 to 61):

> "*In the Tribunal's view, it cannot take all the facts alleged by the Claimant as granted facts ... but must look into the role these facts play either at the jurisdictional level or at the merits level.*
>
> *If the alleged facts are facts that, if proven, would constitute a violation of the relevant BIT, they have indeed to be accepted as such*

> *at the jurisdictional stage, until their existence is ascertained or not at the merits level.* ***On the contrary, if jurisdiction rests on the existence of certain facts, they have to be proven at the jurisdictional stage****. For example, in the present case, all findings of the Tribunal to the effect that there exists a protected investment must be proven, unless the question could not be ascertained at that stage, in which case it should be joined to the merits".*
>
> (emphasis added)

123. In *PSEG Global Inc and Konya Ilgin Elektrik Uretim ve Ticaret Limited Sirketi v Republic of Turkey*, ICSID Case No. ARB/02/5 (Decision on Jurisdiction of 4 June 2004) ("*PSEG*"), the parties made similar arguments concerning the *prima facie* test for jurisdictional challenges. The tribunal stated that (at paragraph 64):

> "*The Tribunal is aware that the prima facie test has been applied in a number of cases, including ICSID cases…and that as a general approach to jurisdictional decisions it is a reasonable one. However,* ***this is a test that is always case-specific. If, as in the present case, the parties have views which are so different about the facts and the meaning of the dispute, it would not be appropriate for the Tribunal to rely on the assumption that the facts as presented by the Claimants are correct."***
>
> (emphasis added)

124. The Tribunal agrees with the tribunal in *PSEG* that whether or not the *prima facie* test should be applied when deciding a jurisdictional challenge is case-specific. In this case, the Tribunal made the decision for a bifurcation of proceedings to hear the Preliminary Jurisdictional Objections first, on the basis that any of these objections, if successful, would be dispositive of the case. Full evidence and argument on all factual and legal issues relating to the Preliminary Jurisdictional Objections has been received and heard by the Tribunal. It would wholly defeat the purpose of bifurcation if the Tribunal were to now assess only whether the Claimant has provided *prima facie* evidence of ownership of the share certificates, and allow the proceedings to move to the merits on that basis, leaving the question of the substantive ownership of the shares still to be determined.

125. In relation to the Claimant's contention that there should be a heightened standard of proof for allegations of "fraud or other serious wrongdoing", the Tribunal accepts that fraud is a serious allegation, but it does not consider that this (without more) requires it to apply a heightened standard of proof. While agreeing with the general proposition that *"the graver the charge, the more confidence there must be in the evidence relied on"* (see paragraph 117(a) above), this does not necessarily entail a higher standard of proof. It may simply require more persuasive evidence, in the case of a fact that is inherently improbable, in order for the Tribunal to be satisfied that the burden of proof has been discharged.

126. In any event, the question of the applicable standard of proof for allegations of "fraud or other serious wrongdoing" and the other disputed issues set out in paragraph 116 above (as to which Party should bear the burden of proof in relation to the second, third and fourth Preliminary Jurisdictional Objections) are of academic interest only. As will be apparent from the Tribunal's observations and findings below, the second, third and fourth Preliminary Objections (set out in paragraphs 105.2, 105.3 and 105.4 above respectively) are not dispositive in these proceedings. Accordingly, the question of burden of proof and/or the applicable standard of proof in respect of these Preliminary Jurisdictional Objections does not arise for consideration. Although the Parties have raised interesting and novel points, the Tribunal does not consider that it is necessary to say more than it already has at this stage. For the avoidance of doubt, the respective submissions of the Parties not analysed by the Tribunal here are neither accepted nor rejected in the circumstances.

IX. HAS THE CLAIMANT PROVED THAT IT OWNED ÇEAŞ AND KEPEZ SHARES BEFORE 12 JUNE 2003?

127. It is common ground between the Parties that the Tribunal's jurisdiction over the merits depends on whether Libananco owned ÇEAŞ and Kepez shares at the time of the alleged expropriation (i.e. 12 June 2003).

128. In order to establish jurisdiction, the Claimant must prove that it owned ÇEAŞ and Kepez shares during the time at which it claims the acts constituting a violation of the ECT were committed by the Respondent. In *Aram Sabet et al v. Islamic Republic of Iran – Bonyad-E-Mostazafan,* Iran-US Claims Tribunal Case No. 815-816-817, Award No. 593-815/816/817-2, 29 June 1999, the tribunal held (at paragraph 55 of the award) that: "*In order to succeed in their claims, the Claimants must prove, as a preliminary matter, that, during the relevant period, they owned the shares that they claim the Respondents expropriated*".

129. The point is further underscored by the award in *Saluka Investment BV (the Netherlands) v. Czech Republic*, UNCITRAL, Partial Award, 17 March 2006, where the tribunal similarly held that its jurisdiction would be limited to claims arising after Saluka acquired the shares from its parent, Nomura. It was accordingly held that the tribunal did not have jurisdiction in respect of damage suffered by Nomura before October 1998 when the bulk of the shares became vested in the claimant, Saluka.

130. A similar conclusion follows from the jurisdictional provisions of investment treaties, including the ECT and the ICSID Convention. Article 1(6) of the ECT defines "Investment" as *"every kind of asset, owned or controlled directly or indirectly by an Investor"*. Although, the ECT speaks of ownership and control (both direct and indirect), this case has been argued by the Parties on the sole basis of ownership (i.e. it is not part of the Claimant's case that it had control but not ownership of the share certificates in question). Accordingly, unless Libananco "owned" ÇEAŞ and Kepez share certificates at the time of the events giving rise to the present dispute, there can be no jurisdiction under

INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
(ICSID Case No. ARB(AF)/12/1)

In the Arbitration under Chapter Eleven of the North America Free Trade Agreement (NAFTA)

Between:

(1) APOTEX HOLDINGS INC.

(2) APOTEX INC.

First and Second Claimants

and

UNITED STATES OF AMERICA

Respondent

AWARD

The Arbitration Tribunal:

V.V. Veeder, President
J. William Rowley, Arbitrator
John R. Crook, Arbitrator

The Tribunal's Secretary:
Monty Taylor

Date of dispatch to the Parties: 25 August 2014

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PART VII – RES JUDICATA: JURISDICTION AND NAFTA ARTICLE 1139

(1) *Introduction*

7.1. The Tribunal here addresses the second principal issue, namely the Respondent's jurisdictional objections in regard to the claims made by Apotex Inc. and Apotex-Holdings as investors in regard to the ANDAs as investments. As already indicated, this issue depends upon the interpretation of the ANDAs as an "investment" under NAFTA Article 1139 raising in turn the issue of Apotex Inc. and Apotex-Holdings as investors with investments, forming part of the threshold requirements as to jurisdiction contained in NAFTA Article 1101(1) (with Article 1116).

7.2. However, this issue first raises the question whether and to what extent the Respondent can invoke the doctrine of *res judicata* to preclude the Claimants from providing any positive answer to this issue as a matter of jurisdiction, given the Apotex I & II Award made between Apotex Inc. and the Respondent. Although that Award identifies the Respondent as "the Government of the United States of America", it is common ground between the Parties that the Respondent is a party or "privy" to the Award.[1] It is also common ground that Apotex-Holdings is not a named party to that Award or the arbitration in which that Award was made. The position of Apotex-Holdings must therefore be considered separately from Apotex Inc., on the basis of the limited concession made by Apotex-Holdings as a "privy", which is described later below.

7.3. The Apotex I & II Award was made under NAFTA's Chapter Eleven and the UNCITRAL Arbitration Rules 1976, with its place of arbitration stated to be New York, New York, USA. The Tribunal has only been shown the redacted version of this Award; but nothing material to this arbitration has been withheld from the Tribunal by Apotex Inc. or the Respondent. Indeed, only a part of the Apotex I & II Award is relevant to the Parties' submissions on *res judicata*; and, for ease of reference below, the relevant (redacted) passages of the Award are set out as an Annex to this Part VII.

[1] In answer to the Tribunal's Question A3 at the Hearing, TD6.1578 for the Claimants and TD6.1646 for the Respondent.

(2) *NAFTA Article 1136(1)*

7.4. The Parties' respective submissions begin with NAFTA Article 1136(1). It provides: "An award made by a Tribunal shall have no binding force except between the disputing parties and in respect of the particular case." The Claimants interpret this provision to mean that the legal effects of the Apotex I & II Award are wholly confined to that particular arbitration and can have no binding force in this different arbitration. Thus, according to the Claimants, there can be no possible *res judicata* effect upon the Claimants' claims in the present case. The Respondent disagrees.

7.5. The Tribunal does not share the Claimants' interpretation of NAFTA Article 1136(1).

7.6. In the Tribunal's view, NAFTA Article 1136(1) closely parallels, and appears to be based upon, Article 59 of the Statute of the International Court of Justice ("ICJ"). Article 59 provides that: "The decision of the Court has no binding force except between the parties and in respect of that particular case." This text repeats verbatim Article 59 of the earlier Statute of the Permanent Court of International Justice ("PCIJ"). For both international courts (the ICJ and the PCIJ), the text consistently has been understood to mean that the court has no rule of *stare decisis*. Neither international court has interpreted the provision to bar the operation of *res judicata*. Moreover, as described below, both international courts have applied the doctrine of *res judicata.*

7.7. Professor Rosenne writes that, for the ICJ, "[t]he effect of Article 59 is that the Statute itself excludes the doctrine of *stare decisis*, the binding force of a judicial decision as a law-creating precedent."[2] Addressing Article 59's role in the PCIJ's Statute, Judge Hudson similarly observes that "Article 59 ... clearly precludes the Court from adopting any doctrine similar to the Anglo-American doctrine of *stare decisis.*"[3] However, "[t]he elimination of the possibility of the Court's developing a doctrine of *stare decisis* does not preclude it from applying the general principle of *res judicata*. Indeed, the application of that principle seems to be required by Article

[2] Rosenne, Shabtai, III *The Law and Practice of The International Court, 1920-1995* (2006), at p. 1571.
[3] Hudson, Manley O., *The Permanent Court of International Justice* (1934), at p. 536, §522.

59 of the Statute, for otherwise a decision of the Court would not be binding on the parties."[4]

7.8. Other learned commentators have also understood NAFTA Article 1136(1) in the same sense as Article 59 of the ICJ and PCIJ Statutes, as precluding a rule of binding precedent. In the scholarly work edited by Ms. Kinnear (et al), it is observed: "Article 1136(1) makes clear that the rule of *stare decisis* does not apply to awards rendered under Chapter 11."[5]

7.9. Accordingly, the Tribunal decides that NAFTA Article 1136(1) does not bar the Respondent in this arbitration from invoking the doctrine of *res judicata* on the basis of the Apotex I & II Award, where applicable. If the position were otherwise, the Claimants' submission would effectively mean that it could re-litigate the same claims over and over again in different arbitrations against the same party, which would be an absurd result for an arbitral procedure intended to produce finality with a legally binding decision.

(3) *Res Judicata in International Law*

7.10. The Parties agree that the Tribunal, under NAFTA Article 1131, "shall decide the issues in dispute in accordance with this Agreement [NAFTA] and applicable rules of international law."

7.11. In the Tribunal's view, the doctrine of *res judicata* is a general principle of law and is thus an applicable rule of international law within the meaning of NAFTA Article 1131. In its Advisory Opinion of 13 July 1954, the ICJ affirmed that "[a]ccording to a well-established and generally recognized principle of law, a judgment rendered by ... a judicial body [such as the U.N. Administrative Tribunal] is *res judicata* and has binding force between the parties to the dispute."[6] Accordingly, Professor Bin Cheng writes, "[t]here seems little, if indeed any, question as to *res judicata* being a general principle of law or as to its applicability in international judicial

[4] *Id.*, at p. 537, §523.

[5] Kinnear, Meg N., Bjorkland, Andrea K., and Hannaford, John F. G., *Investment Disputes Under NAFTA: An Annotated Guide to NAFTA Chapter 11* (2006, updated March 2008), at p. 1136-3.

[6] *Effect of Awards of Compensation Made by the U.N. Administrative Tribunal, Advisory Opinion of 13 July 1954*, I.C.J. Reports 1954, p. 47, p. 53.

proceedings."[7] As later confirmed in the *Amco* award, "The principle of *res judicata* is a general principle of law."[8]

7.12. The doctrine of *res judicata* defines the binding effect of a prior final determination made by a competent tribunal. In *Amco*, the tribunal decided: "The general principle, announced in numerous cases is that a right, question, or fact *distinctly put in issue and distinctly determined* by a court of competent jurisdiction as a ground of recovery, cannot be disputed."[9] Thus, according to Professor Bin Cheng, "[o]nce a case has been decided by a valid and final judgment, the same issue may not be disputed again between the same parties, as long as that judgment stands."[10]

7.13. The doctrine of *res judicata* is often described as operating in international proceedings where three conditions establish the congruence of the matters previously determined and those currently at issue. Legal scholars often refer to Judge Anzilotti's formulation of this triple identity test in his dissent in the PCIJ case of *Chorzów Factory (Interpretation)*. Judge Anzilotti there referred to: "the three traditional elements for identification, *persona, petitum, causa petendi*, for it is clear that 'that particular case' (*le cas qui a été décidé*) covers both the object and the grounds of the claim."[11] The judgment of the majority had there accorded *res judicata* to the passage in the Court's earlier declaratory judgment setting out the grounds or 'essential conditions' on which that decision was based.[12]

7.14. No issue arises in the present case regarding *persona*: Apotex Inc. and the Respondent are named parties to the Apotex I & II Award (the position of Apotex-Holdings as a privy, albeit not a named party, is considered separately below). Professors Schreuer and Reinisch explain the Latin legal terms *petitum* and *causa petendi*, as follows: "[i]dentical 'object' (*petitum*) means that the same type of relief

[7] Cheng, Bin, *General Principles of Law as Applied by International Courts and Tribunals* (1953), at p. 336.

[8] *Amco Asia Corp. v. Republic of Indonesia*, ICSID Case No. ARB/81/1, Resubmitted Case, Decision on Jurisdiction (10 May 1988), 27 ILM 1281 (1988).

[9] *Id.*, Para. 30 (quoting expert report of Professor Reisman) (emphasis in original).

[10] Cheng, *supra*, at p. 337.

[11] *Interpretation of Judgments Nos. 7 & 8 Concerning the Case of the Factory at Chorzow*, 1927 P.C.I.J. (ser. A) no. 13 (16 December 1927) (dissenting opinion of Judge Anzilotti) at p. 23. Judge Anzilotti's Latin terms were translated by the tribunal in *Trail Smelter Case (United States of America v. Canada)*, 3 R.I.A.A. 1938 (11 March 1941) to mean "parties, object, and cause."

[12] *Interpretation of Judgments Nos. 7 & 8 Concerning the Case of the Factory at Chorzow*, *supra*, at p. 20.

is sought in different proceedings. Identical 'ground' (*causa petendi*) means that the same legal arguments are relied upon in different proceedings."[13]

7.15. Whilst the triple identity test is often referred to in describing the requirements for *res judicata* to operate,[14] certain international tribunals and scholars have questioned its division between *petitum* and *causa petendi*; and many cases have used a simpler analysis.[15] The British-U.S. Claims Arbitral Tribunal saw the doctrine as involving only two elements: "res judicata applies only where there is identity of the parties and of the question at issue."[16] The *Pious Fund* tribunal (applying *res judicata* in the Permanent Court of Arbitration's first case and viewed as "[t]he leading early case"[17]) also applied a two-part test, emphasising that "there are not only the same parties to the suit, but also the same subject-matter that was judged" in a prior arbitral award.[18]

7.16. Professor Cheng questions the division between *petitum* and *causa petendi*, observing that "an examination of international decisions ... throws some doubt about the accuracy of this sub-division, especially in border-line cases."[19] Professors Schreuer and Reinisch point out that "[i]nternational tribunals have ... been aware of the risk that if they use too restrictive criteria of 'object' and 'grounds', the doctrine of *res judicata* would rarely apply: if only an exactly identical relief sought (object) based on exactly the same legal arguments (grounds) in a second case would be precluded as a result of *res judicata*, then litigants could easily evade this by slightly modifying either the relief requested or the grounds

[13] Schreuer, Christoph and Reinisch, August, Legal Opinion, *CME Czech Republic B.V. v. Czech Republic*, UNCITRAL (20 June 2002), at p. 16, Para. 43 ("Schreuer & Reinisch"). *See also* Amerasinghe, Chittharanjan F, *International Arbitral Jurisdiction* (2011), at p. 169; and Lowe, Vaughan, *Res Judicata and the Rule in International Arbitration*, 8 RADIC 38 (1996), at pp. 40-41. Professors Schreuer and Reinisch discuss the use by contemporary tribunals of an "economic approach" in assessing identity; but that is not relevant to the present case (see Paras. 21-40).

[14] International Law Association, *Interim Report, "Res Judicata" and Arbitration*, International Law Association, Berlin Conference on International Arbitration (2004), at p. 2. ("ILA Interim Report"). The Tribunal notes that the ILA's Final Report on "Res Judicata" was expressly limited to international commercial arbitration: hence its citation here is of limited relevance, as submitted by the Claimants [TD1.158].

[15] *See* the cases cited by Schreuer and Reinisch, *supra*, at p. 8, Para. 15.

[16] *British-U.S. Claims Arbitration* (1910), cited in Cheng, *supra*, at pp. 339-340.

[17] Schreuer & Reinisch, *supra*, at p. 3, Para. 6.

[18] *The Pious Fund of the Californias*, Permanent Court of Arbitration, Award (14 October 1902), at p. 3 (unofficial English translation).

[19] Cheng, *supra*, at p. 343.

relied upon."[20] Professor Dodge voices a similar concern, although he indicates (as do Professors Schreuer and Reinisch) that tribunals have not allowed "claim splitting" by claimants seeking to avoid the preclusive effects of prior awards.[21]

7.17. The Claimants and the Respondent disagree on the scope of *res judicata's* effect in international law. The Parties agree that the provisions of the *dispositif*, or operative part, of a prior judgment or award have *res judicata* effect. They disagree whether *res judicata* in international law includes the broader concept of or akin to issue estoppel, the principle that a party in subsequent proceedings cannot contradict an issue of fact or law not reflected in the *dispositif* if it has already been distinctly raised and finally decided in earlier proceedings between the same parties (or their privies). The Claimants submit it does not; whereas the Respondent says it does.

7.18. It is clear that past international tribunals have applied forms of issue estoppel, without necessarily using the term. Umpire Plumley's award in *Orinoco Steamship* found that "every matter and point distinctly in issue ... and which was directly passed upon and determined in said decree, and which was its ground and basis, is confirmed by said judgment, and the claimants ... are forever estopped from asserting any right or claim based in any part upon any fact actually and directly involved in the said decree."[22] In Professor Lowe's opinion, the tribunal in the resubmitted *Amco* case[23] "clearly applied the principle of issue estoppel to the determination of specific facts and of the legal characterisations of facts by the previous tribunal."[24] Most recently, the ICSID tribunal in *Grynberg v. Grenada*[25] applied issue estoppel (albeit describing it as "collateral estoppel"[26]) to foreclose the

[20] Schreuer & Reinisch, *supra*, at p. 17, Para. 45.

[21] Dodge, William, *National Courts and International Arbitration: Exhaustion of Remedies and Res Judicata Under Chapter Eleven of NAFTA*, 23 Hastings Int'l & Comp. L. (2000), at p. 366; Schreuer & Reinisch, *supra*, at pp. 17-18, Paras. 46-48.

[22] *Claim of Company General of the Orinoco Case*, Report of French-Venezuelan Mixed Claims Commission of 1902 (1906, Ralston, Jackson H., ed.) at p. 355.

[23] *Amco v. Indonesia*, *supra*.

[24] Lowe, *supra*, at p. 42.

[25] *Rachel S. Grynberg, Stephen M. Grynberg, Miriam Z. Grynberg and RSM Production Corporation v. Grenada*, ICSID Case No. ARB/10/6, Award (10 December 2010).

[26] Although the *Grynberg* Award referred to the principle as "collateral estoppel", the US legal concept of "collateral estoppel" is broader, permitting non-parties (or privies) to a prior litigation to invoke the doctrine to preclude re-litigation of an issue previously decided. That broader principle is not an issue in the present case, as the Respondent recognised [TD4.1190].

claimants' efforts to re-open issues decided in an award made in a prior ICSID arbitration.[27]

7.19. In *Grynberg v. Grenada*, the award in the first ICSID arbitration had dismissed the claims against Grenada as the respondent made by a Texan company (RSM) alleging contractual breaches of a concession agreement. In the second ICSID arbitration, RSM and its three shareholders alleged breaches by the same respondent of the bilateral investment treaty between the USA and Grenada. On the face of it, the triple identity test was not satisfied as regards these three shareholders as *persona*, nor the *petitum* or *causa petendi* as regards both RSM and the shareholders. Yet, the second arbitration tribunal summarily dismissed all claims made by these four claimants as being "manifestly without legal merit" under ICSID Arbitration Rule 41(5), together with costs orders adverse to the claimants.

7.20. In so doing, the second tribunal accepted the respondent's submission of issue estoppel arising from the first award, to the effect that the legal and factual contentions on which the new claims depended had already been fully litigated in the first ICSID arbitration.[28] Applying the doctrine to all four claimants as "privies" as a general principle of law recognised in *Amco v Indonesia*[29] and the *Orinoco* case, the second ICSID tribunal accepted that "a finding concerning a right, question or fact may not be re-litigated (and, thus, is binding on a subsequent tribunal), if, in a prior proceeding: (a) it was distinctly put in issue; (b) the court or tribunal actually decided it; and (c) the resolution of the question was necessary to resolving the claims before that court or tribunal."[30] Applying these principles, the tribunal concluded: "that an essential predicate to the success of each of Claimants' claims is an ability for the Tribunal to re-litigate and decide in Claimants' favour conclusions of fact or law concerning the parties' contractual rights that have already distinctly been put in issue and distinctly determined by the Prior Tribunal";

[27] *Grynberg v. Grenada, supra*, Para. 7.1.8.

[28] *Id.*, Para. 4.1.1.

[29] *Amco v. Indonesia, supra*, quoting the expert report of Professor Reisman at Para. 30: "[A] right, question or fact distinctly put in issue and distinctly determined by a court of competent jurisdiction as a ground of recovery, cannot be disputed."

[30] *Grynberg v. Grenada, supra*, Para. 7.1.1.

and having determined that ability adversely to the claimants, the tribunal decided that each of their claims was manifestly without legal merit.[31]

7.21. The Claimants denied the relevance of the *Grynberg* award to the present case, contending that the parties there had agreed to the application of collateral estoppel (issue estoppel) under the governing law.[32] In the Tribunal's view, this submission is incorrect.[33] The parties strongly disputed its application to their case; but, significantly, there was no dispute as its requirements as a general principle of international law.

7.22. The Claimants also contend that *Orinoco Steamship* (and presumably other like authorities[34]) do not correctly reflect *res judicata* under international law. In their submission, the case reflected Umpire Plumley's common law orientation, as evidenced by his reliance on a decision of the US Supreme Court decision as legal authority for the cited principle.[35] The Claimants contend that notions of issue estoppel found in common law systems are not found in civil law systems, which typically (so the Claimants submit) limit *res judicata* effects to matters addressed in the *dispositif* of an award or judgment.[36] Given this significant difference in approach between two major systems of law, the Claimants contend that issue estoppel cannot be said to be an aspect of *res judicata* as a general principle of law "recognised by civilized nations."

7.23. The Tribunal recognises that historical differences as to issue estoppel have existed and, to a lesser extent, still exist in national laws between certain common law and certain civil law systems. As the ILA Interim Report makes clear, however, there is no sharp divide between these two legal systems.[37] It is also clear that international courts and tribunals have regularly examined under international law a prior tribunal's reasoning, and the arguments it considered, in determining the scope, and thus the preclusive effect, of the prior award's operative part. The first international

[31] *Id.*, Para. 7.2.1.
[32] TD3.542.
[33] *Grynberg v. Grenada*, *supra*, *see* (*inter alia*) Paras. 5.3.5 and 5.3.6.
[34] *See, e.g.*, Cheng, *supra*, at p. 337; *Amco v. Indonesia*, *supra*, Para. 30.
[35] *Southern Pacific R.R. Co. v. United States*, 168 U.S. 1 (1897).
[36] *See* ILA Interim Report, *supra*, at p. 14.
[37] *Id.*, at p. 15.

tribunal's analysis and reasoning thus often play a significant role before the second international tribunal in determining the *res judicata* effect of the earlier award.

7.24. This is illustrated in the *Pious Fund* arbitration, where the tribunal held that an umpire's award in a prior mixed claims commission proceeding had *res judicata* effect, and obliged Mexico to pay certain annuities to the USA on behalf of the Archbishop of San Francisco and the Bishop of Monterey. The tribunal rejected Mexico's contention that only the amount specified in the prior award had *res judicata* effect, instead considering that it must consider the earlier award in its entirety to determine the *res judicata* effect of its *dispositif*: "Considering that all the parts of a judgment or a decree concerning the points debated in the dispute enlighten and mutually supplement each other, and that they all serve to render precise the meaning and bearing of the *dispositif* (the decisory part of the judgment), to determine the points upon which there is *res judicata* and which therefore cannot be put in question."[38]

7.25. The Permanent Court of International Justice was of like mind in *Advisory Opinion No. 11*: "It is perfectly true that all the parts of a judgment concerning the points in dispute explain and complete each other and are to be taken into account in order to determine the precise meaning and scope of the operative portion. This is clearly stated in the award of the Permanent Court of Arbitration of October 14th, 1902, concerning the Pious Fund of the Californias ... The Court agrees with this statement."[39]

7.26. In his dissent in *Chorzów Factory*, Judge Anzilotti was of the view that "the binding effect attaches only to the operative part of the judgment and not to the statement of reasons." However, he added: "[w]hen I say that only the terms of a judgment are binding, I do not mean that only what is actually written in the operative part constitutes the Court's decision. On the contrary, it is certain that it is almost always necessary to refer to the statement of reasons to understand clearly the operative part and above all to ascertain the *causa petendi*."[40]

[38] *Pious Fund*, *supra*, at p. 2.

[39] *Polish Postal Service in Danzig, Advisory Opinion*, 1925 P.C.I.J. (Ser. B) No. 11 (May 16), Para. 86.

[40] *Interpretation of Judgments Nos. 7 & 8 Concerning the Case of the Factory at Chorzow*, *supra*, at p. 24.

7.27. The *Channel Arbitration* tribunal similarly observed that while *res judicata* "attaches in principle only to the provisions of" the *dispositif*, "it is equally clear that, having regard to the close links that exist between the reasoning of a decision and the provisions of its *dispositif*, recourse may in principle be had to the reasoning in order to elucidate the meaning and scope of the *dispositif*."[41]

7.28. The International Court of Justice also looks to the parties' arguments and submissions to determine the legal effect of prior judgments. As Professor Rosenne observes, "[t]he relevance of whether a question was argued between the parties might arise ... if it is necessary to determine the scope of the *res judicata* ... In the *Asylum* case ... the problem was ... of the scope of the binding force of the decision. The *res judicata* does not derive from the operative clause of the judgment, which confined itself to stating which submissions of the parties were rejected or accepted and to what extent, but from the reasons in point of law given by the Court."[42] Accordingly, cases such as *Asylum*[43] and *Corfu Channel*[44] "bring into sharp relief the delayed-action effect attaching to the written and oral pleadings. In the last analysis the scope of *res judicata* can only be determined by reference to the pleadings in general, and to the parties' submissions in particular."[45]

7.29. The jurisprudence of the European Court of Justice (ECJ) is to like effect. For the ECJ (applying the laws of the European Union and international law), the legal effect of a decision by the ECJ and other EU institutions is not to be limited to the wording of the operative part. In *Asteris & Greece v. Commission*, the ECJ noted that the EU institution was required to have regard not only to the operative part of the decision but also to the *motifs* which led to that decision in order to determine the former's exact meaning.[46] In *Commission v. BASF*,[47] the ECJ noted that: "the operative part of such a decision can be understood, and its full effect ascertained, only in the light of the statement of reasons"; and that a decision's *dispositif* and

[41] *Case Concerning the Delimitation of the Continental Shelf (U.K. v. France)*, 18 R.I.A.A. 272 (14 March 1978), 295 (Para. 28).

[42] Rosenne, *supra*, at p. 1603.

[43] *Request for Interpretation of the Judgment of 20 November 1950, in the Asylum Case (Colombia v. Peru), Judgment of 27 November 1950*, I.C.J. Reports 1950, p. 395.

[44] *Corfu Channel case, Judgment of 9 April 1949*, I.C.J. Reports 1949, p. 4.

[45] Rosenne, *supra*, at p. 1603.

[46] *Asteris & Greece v Commission*, [1988] ECR 2181, Para. 27.

[47] *Commission of the European Communities v. BASF AG & Others*, [1994] ECR I-2555, Para. 67.

motifs constituted "an indivisible whole." In *Deggendorf v. Commission*, the ECJ held that: "the operative part of an act is indissociably linked to the statement of reasons for it, so that, when it has to be interpreted, account must be taken of the reasons which led to its adoption."[48]

7.30. Thus, where there is a question regarding the extent of a prior decision or award's *res judicata* effect, international tribunals regularly look to the prior tribunal's reasons and indeed also to the parties' arguments, in order to determine the scope of what was finally decided in that earlier proceeding.

7.31. In Professor Rosenne's opinion, in examining a prior tribunal's reasoning and the arguments it considered, international tribunals have not drawn the distinctions between *ratio decidendi* and *obiter dicta* "which is an essential element of the common-law rule of the binding force of judicial precedents (*stare decisis*)."[49] For the International Court of Justice, Professor Rosenne observes, " [t]he reasons in point of law of Article 95 ... of the Rules of Court do not contemplate such a finely drawn distinction."[50] As in the *Pious Fund* arbitration, tribunals have considered that "all the parts of the judgment or the decree concerning the points debated in the litigation enlighten and mutually supplement each other."[51]

7.32. It would be possible to cite many further legal materials in support of the legal analysis made above; but it would serve no purpose here to prolong what is already a lengthy analysis. However, the Tribunal is comforted to see its approach above confirmed by the ICJ's recent Judgment of 11 November 2013 in *Cambodia v Thailand.*[52] In that Judgment, albeit not directly concerned with the doctrine of *res judicata*, the ICJ considered in regard to an earlier judgment of 1962 the scope of Article 60 of the ICJ's Statute, which provides: "The judgment is final and without appeal. In the event of dispute as to the meaning or scope of the judgment, the Court shall construe it upon the request of any party." In accordance with the ICJ's jurisprudence, a dispute under Article 60 must relate to the operative part of the

[48] *Textilwerke Deggendorf GmbH (TWD) v Commission,* [1997] ECR I-2549, Para. 21.

[49] Rosenne, *supra*, at p. 1556.

[50] *Id.*

[51] *Pious Fund*, *supra*.

[52] *Request for Interpretation of the Judgment of 15 June 1962 in the Case Concerning the Temple of Preah Vihear (Cambodia v. Thailand*), Judgment of 11 November 2013 (ICJ).

judgment in question and cannot concern the reasons for the judgment except in so far as these are inseparable from the operative part.[53] The ICJ nonetheless held under Article 60 that the "scope of the operative part of a judgment of the Court is necessarily bound up with the scope of the dispute before the Court."[54] The Tribunal concludes from this Judgment that even with the restrictive language of Article 60, the ICJ is not barred from interpreting the operative part of a judgment by reference to its reasons for that judgment.

(4) ***Res Judicata under the UNCITRAL Arbitration Rules***

7.33. The Apotex I & II Award was made under the UNCITRAL Arbitration Rules 1976 forming part of the arbitration agreement between the parties to that arbitration. Under Article 32(2) of the UNCITRAL Rules, an award "shall be final and binding on the parties", including an award made in the exercise of the tribunal's power to decide upon its own jurisdiction. Under Article 32(3) of the UNCITRAL Rules, an award "shall state the reasons upon which the award is based." Accordingly, as an award containing reasons under Article 32 of the UNCITRAL Rules, the Apotex I & II Award (with its reasons) was and remains final and binding upon Apotex Inc. and the Respondent, as agreed by those Parties.

7.34. The Respondent submitted at the Hearing that the combined effect of Articles 32(2) and 32(3) means that the reasons in the Apotex I and II Award have effect as *res judicata* as between the Parties to this arbitration, just as much as its operative part: "… This is because the purpose of an Award is to decide the Parties' dispute for all time, both as to the whole and as to its constituent parts."[55]

7.35. The Tribunal is minded to accept this submission as a matter of legal logic; but, for the purpose of deciding this issue, it is unnecessary to apply it here in full. Given the status of both the operative part and the reasons in the Apotex I & II Award under Article 32 of the UNCITRAL Arbitration Rules, the Tribunal concludes that those relevant reasons can be read together with the operative part for the purpose of applying the doctrine of *res judicata* in this arbitration, similarly to the position under international law. It is not necessary in this case to read the reasons

[53] *Id.*, Para. 34.
[54] *Id.*, Para. 101.
[55] TD6.1653-1654.

independently from the operative part (as the Respondent submits); but it would clearly be impermissible for this Tribunal to read the operative part independently in isolation from its relevant reasons under the UNCITRAL Arbitration Rules.

7.36. The Tribunal has not addressed separately the legal status under New York law (as the *lex loci arbitri*) of the reasons or the operative part of the Apotex I & II Award. In the Tribunal's view, if and to the extent relevant, the effect of New York law does not materially change or add to the analysis made above. It is not disputed that the Apotex I & II Award (with its reasons) is final and binding under New York law; nor has Apotex Inc. sought to challenge that Award before the New York courts (or elsewhere).

(5) ***Summary as to the Res Judicata Doctrine***

7.37. Applying NAFTA Article 1131(1), the rules of international law and the UNCITRAL Arbitration Rules, the Tribunal concludes that the Apotex I & II Award, with its relevant reasons, operates in this arbitration as *res judicata* as regards both named parties to that arbitration, namely Apotex Inc. and the Respondent. It remains to be considered in what manner it operates in regard to the specific claims made by Apotex Inc. in this arbitration.

7.38. As regards Apotex-Holdings, the Claimants agreed at the Hearing that Apotex-Holdings, for the purpose of *res judicata*, should be identified as a "privy" to the Apotex I and II Award: "… having reviewed the RSM versus Grenada decision, the second one, Apotex would agree that privies are bound to the same extent as the Party with which they stand in privity. So we would accept that Apotex Holdings could not bring the claim asserted and decided in the Apotex [I and] II case …"[56] In other words, the two named Claimants in this arbitration stand in similar shoes, as regards the effect of *res judicata* resulting from the Apotex I and II Award, notwithstanding the fact that only one of them was a named party to the Apotex I and II Award.

7.39. However, Apotex-Holding's shoes are only similar and not the same. As the Claimants made clear towards the end of the Hearing, in answer to the Tribunal's Question A2: "… there is a distinction between derivative claims made on behalf of

[56] TD3.542. *See also* TD3.544.

a company and claims made directly by a shareholder on its own behalf. In this arbitration, Apotex Holdings brings a claim in its own right and in its own name. It is different from the claim made by Apotex-Canada [Apotex Inc.]. Apotex Holdings is bound by the Apotex I and II Award only to the extent that it addresses Apotex-Canada as the investor and holder of the two tentatively approved ANDAs at issue."[57]

7.40. In the Tribunal's view, independently from the concession (rightly) made by Apotex-Holdings at the Hearing, Apotex-Holdings is a "privy" with Apotex-US, albeit not a named party in the Apotex I & II arbitration. Its relevant claims in this arbitration, albeit made in its own right and in its own name, depend upon Apotex Inc.'s ANDAs as investments under NAFTA Articles 1116 and 1139; and if these are not investments, Apotex-Holdings cannot bring such claims before this Tribunal as a matter of jurisdiction.

(6) *The Application of Res Judicata*

7.41. It is self-evident that the "Operative Order" in Paragraph 358 of the Apotex I & II Award (pages 118-119) does not, read strictly in isolation by itself, address the Claimants' specific claims in this arbitration. That operative part merely records, in Paragraph 358(a), that Apotex Inc. "does not qualify as an 'investor', who has made an 'investment' in the U.S., for the purposes of NAFTA Articles 1116 and 1139, and accordingly both the Sertraline and Pravastatin Claims are hereby dismissed in their entirety, on the basis that the Tribunal lacks jurisdiction in relation thereto." The Claimants in this arbitration make no similar claims regarding Sertraline and Pravastatin.

7.42. However, in this Tribunal's view, that operative part as a "*dispositif*" can and should be read with the relevant "*motifs*" or reasons for that operative part, as decided above. Hence, the Tribunal concludes, for the purpose of *res judicata*, that Paragraph 358(a) of the operative part is to be applied together with the reasons applicable to that paragraph, namely the relevant passages in Paragraphs 177 to 246 of the Apotex I & II Award (pages 55 to 78). As indicated above, for ease of reference and given their significance, these paragraphs are reproduced in full from

[57] TD6.1577.

the redacted public version of the Apotex I & II Award in the Annex to this Part VII. It is nonetheless useful briefly to summarise the tribunal's approach in these parts of the Apotex I & II Award.

7.43. First, the tribunal addresses the issue whether activities surrounding ANDAs qualify as 'investments' under NAFTA Article 1139, as there submitted by Apotex Inc. and there disputed by the Respondent: see Paragraphs 177ff. For several reasons, the tribunal rejects Apotex Inc.'s submissions: see Paragraphs 178, 186ff & 225.

7.44. Second, the tribunal addresses the issue whether ANDAs qualify as 'intangible property' under NAFTA Article 1139(g) in Paragraphs 196ff. For several reasons, the tribunal rejects Apotex Inc.'s submissions: see Paragraphs 178, 206ff & 225. In Paragraphs 206 and 208, the tribunal equates Apotex Inc. to "a mere exporter of goods into the United States" and decides that " … property is not an 'investment' if, as here, it merely supports cross-border sales." In Paragraph 217, the tribunal states (*inter alia*): "… The ANDA was thus a requirement in order to conduct an export business. If there had been no ANDA process, the underlying business could not be said to be an 'investment' in the U.S. The fact that an ANDA was required does not change the nature of the business." The tribunal concludes, in Paragraph 225: "Thus, neither Apotex's ANDAs, nor its activities in Canada, nor the costs incurred there in meeting the requirements of the U.S. regulatory regime for exporting its goods, are '*investments*' in the United States."

7.45. Third, the tribunal addresses the issue whether Apotex Inc.'s commitment of capital and resources towards ANDAs could constitute an 'investment' under NAFTA Article 1139(h) in Paragraphs 226ff. The tribunal notes that Apotex Inc. "made clear that its submissions under NAFTA Article 1139(h) were to be treated as part of its submissions under NAFTA Article 1139(g), and not as independent grounds": see Paragraph 229. The tribunal rejects Apotex Inc.'s submissions under Article 1139(h): see paragraph 230ff. In Paragraph 233, the tribunal decides that NAFTA Article 1139(h) " … excludes simple cross-border trade interests. Something more permanent is necessary"; and, in Paragraph 235, that "each of the specific activities and expenses relied upon by Apotex [*i.e.* Apotex Inc.] simply supported and facilitated its Canadian-based manufacturing and export operations."

7.46. In Paragraphs 241-246, the tribunal concludes overall that Apotex Inc. had made no "investment" in the territory of the USA within the meaning of NAFTA Article 1139; that, as a necessary consequence, Apotex Inc. does not qualify as an "investor" under NAFTA Article 1116; and that, accordingly, the tribunal has no jurisdiction over the claims there made by Apotex Inc. as the claimant.

7.47. Lastly, in the first part of the operative part, in Paragraph 358(a), the Tribunal unanimously orders and awards: "[Lines 1-2] Apotex does not qualify as an '*investor*', who has made an '*investment*' in the U.S., for the purposes of NAFTA Articles 1116 and 1139, [Lines 2-4] and accordingly both the Sertraline and Pravastatin Claims are hereby dismissed in their entirety, on the basis that the Tribunal lacks jurisdiction in relation thereto."

7.48. This Tribunal accepts that there are several factors in the Apotex I & II Award which qualify the application of its passages for the purpose of *res judicata* in this arbitration.

7.49. The specific claims pleaded by Apotex-Canada in the Apotex I & II arbitration, as recited and decided in the Apotex I & II Award, are different from the specific claims made by the Claimants in this arbitration. The former claims related to "tentatively approved" ANDAs. This is not the specific case pleaded by the Claimants in this arbitration where the ANDAs were "finally approved" and where no claim as to "tentatively approved" ANDAs is advanced by the Claimants.[58] Hence, the operative part, read by itself and in strict isolation from the preceding reasons, could not form the basis of *res judicata* in this arbitration.

7.50. However, as decided above, it is necessary to read the first two lines of Paragraph 358(a) of the operative part in the Apotex I & II Award with the tribunal's earlier relevant reasons for this part of the paragraph. It is clear from those reasons that the parties put distinctively in issue ANDAs generally, not limited to tentatively approved ANDAs but also including finally approved ANDAs; that the tribunal actually decided that issue; and that, as that tribunal saw it, that decision, amongst others, was necessary to resolve the parties' dispute before it. In the Tribunal's

[58] The complaints made in the Request (Paras. 55-56) and the Apotex Memorial (Paras. 530-538) as regards "pending ANDAs" were subsequently abandoned by the Claimants: see the Claimants' letter to the Tribunal dated 7 February 2013.

view, it is not required for the application of the *res judicata* doctrine that there should be a single reason necessary for the tribunal's decision: there can be two or more reasons of equal relevance for the application of the doctrine, particularly when the parties advance more than one argument in support of their respective cases (as the parties clearly did in the Apotex I & II arbitration).

7.51. Nevertheless, several reasons in the Apotex I & II Award are inapplicable to this arbitration for the purpose of *res judicata*, being expressly limited to tentatively approved ANDAs.[59] Accordingly, the Tribunal here takes no account of these reasons in applying *res judicata* in this case. On the other hand, other passages clearly do refer to or necessarily include finally approved ANDAs.[60] It is therefore not possible to conclude that the tribunal's reasons are limited to tentatively approved ANDAs.

7.52. Whilst addressing whether ANDAs were "property" under NAFTA Article 1139(g), the tribunal did not independently address ANDAs as "interests" under NAFTA Article 1139(h). In Paragraph 229 of the Apotex I and II Award, as noted above, the tribunal records Apotex Inc.'s confirmation that its submissions under NAFTA Article 1139(h) "were to be treated as part of its submissions under NAFTA Article 1139(g), and not as independent grounds." It is not entirely clear what these "submissions" were as part of Apotex Inc.'s submissions under Article 1139(g); but it is any event clear that both parties made submissions regarding Article 1139(h) and that the tribunal did address and decide upon ANDAs as investments under Article 1139(h).[61]

7.53. Lastly, it is necessary to record that this is not a case which raises any issue of bad faith or abuse of process by the Claimants. Indeed, the contrary was not suggested by the Respondent; and, although the Claimants' Request in this arbitration originally included a claim relating to non-approved ANDAs, that claim was

[59] Apart from its summaries of the parties' respective arguments, see in Paras. 200, 209, 210 (in part), 211, 212-215, 220-221 (in part) and 223 (in part) of the Apotex I & II Award.

[60] See, in particular, Paras. 196-199, 202-205, 207-208, 210-211 (in part), 216-219, 220-221 (in part), 222, 223 (in part), 224-225, 226 and 229-240 of the Apotex I & II Award.

[61] See the Apotex I & II Award, Paras. 226ff and 235. (Apotex Inc. was represented by different Counsel in the Apotex I & II arbitration than Counsel for the Claimants in this arbitration).

abandoned before the publication of the Apotex I & II Award, as already indicated above.

7.54. For the reasons set out below, as regards the claims made by Apotex Inc. in this arbitration, the Tribunal decides that the Apotex I & II Award, applying the doctrine of *res judicata*, precludes Apotex Inc. from contending that its finally approved ANDAs, within the meaning of NAFTA Article 1139(g), are "property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes."

7.55. In the Tribunal's view, the operative part (first two lines) and its relevant reasons in the Apotex I & II Award apply equally to all ANDAs, whether tentatively approved or finally approved. As part of their essential character, as distinctly decided in the Apotex I & II Award, Apotex Inc.'s ANDAs are no more than applications operating as quasi-import licences which support cross-border sales by Apotex Inc. to its consignees in the USA of products manufactured at its Canadian facilities. The possibilities of Apotex Inc. selling or transferring ANDAs (albeit revocable and remaining site-specific to the designated manufacturing facility) do not change the inherent nature of these ANDAs, as decided in the Apotex I & II Award. ANDAs are not commodities in the territory of the USA.

7.56. As regards Apotex Inc., the Tribunal comes to the same conclusion in regard to NAFTA Article 1139(h). Applying the doctrine of *res judicata*, the Tribunal decides that Apotex Inc. is precluded from contending that its finally approved ANDAs, within the meaning of NAFTA Article 1139(h), are "interests arising from the capital or other resources in the territory of a Party [the USA] to economic activity in such territory …" As decided in the Apotex I & II Award, an ANDA operates only as a quasi-import licence supporting cross-border trade interests falling outside the definition of this provision. Whilst the tribunal in the Apotex I & II Award did not independently apply NAFTA Article 1139(h), as noted above, the tribunal nonetheless distinctly addressed this provision. The tribunal rejected the case advanced by Apotex Inc.[62]

[62] See the Apotex I & II Award, Paras. 230-235.

7.57. Shorn of all semantic technicalities, it is worth asking the simple question after reading the relevant passages from the Apotex I & II Award in the Annex to this Part VII: how would that tribunal respond to the specific claims made by Apotex Inc. in this arbitration under NAFTA Article 1139? In this Tribunal's view, that question admits of only one answer: the Apotex I & II tribunal would say that it had already decided the essential issues relating to these claims in its award; and, applying the same two lines of its operative part with its same supporting reasons, that these claims failed to meet the requirements of NAFTA Article 1139 for jurisdiction under NAFTA's Chapter Eleven.

7.58. In the Tribunal's view, it is impossible to dismiss those reasons as mere 'obiter dicta' or to read one passage in isolation from those reasons as a whole. Those reasons under both NAFTA Articles 1139(g) and 1139(h) were essential to the operative part and thereby distinctly determined matters distinctly in issue in the Apotex I & II arbitration. It is also impermissible to parse the two sets of claims in the two arbitrations, so as artificially to distinguish one case from the other. The purpose of the *res judicata* doctrine under international law is to put an end to litigation; and it would thwart that purpose if a party could so easily escape the doctrine by 'claim-splitting' in successive proceedings.

7.59. Thus, the Claimants did not argue (nor could they) that simply because the Apotex I & II Award addressed specific claims relating to Sertraline and Pravastatin, the Claimants could still bring the same claims relating to other drug products. Similarly, in the Tribunal's view, the Claimants cannot now distinguish tentatively approved ANDAs from finally approved ANDAs so as to frustrate the application of *res judicata* to issues decided in the Apotex I & II Award. That is an impermissible attempt to re-argue and overturn the final and binding decisions in the Apotex I & II Award. The Tribunal notes that, in *Grynberg v. Grenada*, that tribunal likewise rejected an analogous attempt based upon a new allegation of corruption.[63] Indeed, were it so easy to side-step the application of *res judicata*, the doctrine would be largely meaningless under international law, a risk recognised by

[63] *Grynberg v. Grenada, supra*, Para. 7.3.6 ("It is true that Claimants style the present arbitration as Treaty claim based [the first arbitration was contract-based upon a concession agreement]. But the difficulty with this is that, as pleaded and argued, the present case is no more than an attempt to re-litigate and overturn the findings of another ICSID tribunal, based on allegations of corruption that were either known at the time or which ought to have been raised by way of a revision application and over which the Prior Tribunal had jurisdiction").

several scholars, including Professors Dodge, Schreuer and Reinisch in the works cited earlier in this Part. The costs and time required for investor-state arbitrations, already not inconsiderable, would be multiplied several times over if unsuccessful claimants could persuade later tribunals to restrict the effect of earlier awards by simply reformulating their claims and arguments. As already described, there is a strong interest, both public and private, in bringing an end to a dispute by one final and binding arbitration award.

7.60. In regard to Apotex-Holdings, the Tribunal decides that same result must follow, albeit for additional reasons. Given that Apotex Inc.'s ANDAs are not "investments" under NAFTA Article 1139, it follows that Apotex-Holdings cannot make any claim in respect of its indirect interest in such ANDAs because Apotex-Holdings is not, for that purpose, an investor with a relevant "investment" under NAFTA Article 1139.

(7) ***Conclusion***

7.61. Accordingly, for these reasons, the Tribunal (by a majority) decides this second issue in favour of the Respondent and against Apotex Inc. and Apotex-Holdings. Thus, the Tribunal (by a majority) upholds the Respondent's jurisdictional objections to the claims made by the Claimants in regard to the ANDAs under NAFTA Articles 1101(1), 1116 and 1139. (This decision does not apply, of course, to the other claims made by Apotex-Holdings for itself and for Apotex-US which are considered in the Parts which follow).

7.62. Whilst this conclusion disposes of the Claimants' claims under the doctrine of *res judicata*, it should not be assumed that the Tribunal (by a majority) would have reached any different decision on the Claimants' other submissions under NAFTA Article 1139. Notwithstanding a well-researched argument by Counsel for the Claimants as regards the correct interpretation of Article 1139 (to which the Tribunal here pays tribute), the Tribunal remains attracted to the succinct submissions of the Respondent and Mexico to the effect that the definition of an "investment" under both Article 1139(g) and 1139(h) must be read with Article NAFTA 1101(1), collectively requiring such investment to be "in the territory" of the host State. Although Apotex Inc.'s ANDAs were originally submitted and approved in the USA, this Tribunal (by a majority) considers that such ANDAs

cannot meet that particular requirement, particularly when Apotex Inc. has never had any presence, activity or other investment in the territory of the USA, including the non-payment of any relevant US taxes. (This is not inconsistent with the approach taken in the Apotex I & II Award.)[64]

7.63. *Dissent:* As noted above, the decision on this issue is not made by the Tribunal unanimously. What follows in the next three paragraphs is the dissent on this issue by Mr. Rowley.

7.64. Had he been sitting alone, Mr. Rowley would have reached a different conclusion on this issue. For him, the essence of *res judicata* is that a right, question or fact has distinctly been put in issue and distinctly determined by a court or tribunal of competent jurisdiction in an earlier proceeding between the same parties. He considers that the Apotex I & II tribunal neither decided, nor needed to decide the question which is now before the Tribunal, *i.e.*, whether Apotex Inc.'s finally approved ANDAs plus associated products are to be characterised as "property" for the purposes of NAFTA Article 1139(g). The Apotex I & II tribunal stated clearly that: "The jurisdictional issue here turns upon the inherent nature of the relevant ANDAs …" (Paragraph 224, emphasis added). The relevant ANDAs were understood to be Apotex Inc.'s Sertraline and Pravastatin ANDA filings which had only been tentatively approved by the FDA. The Apotex I & II tribunal well understood the difference between tentatively approved and finally approved ANDAs, and made the point that " … it remains entirely unclear whether a tentatively-approved ANDA (*i.e.* as distinct from (i) a finally-approved ANDA, and (ii) a finally-approved ANDA plus associated products) has value." (Paragraph 220, emphasis added). Because the ANDAs before the Apotex I & II tribunal had only been tentatively approved, the tribunal reasoned that " … at the relevant time, (a) Apotex's [*i.e.* Apotex Inc.'s] ANDAs could not (yet) be characterised as '*property*' for the purposes of NAFTA Article 1139(g), and (b), even if they did constitute "*property*", Apotex's [*i.e.* Apotex Inc.'s] ANDAs were not yet '*acquired in the expectation or used for the purpose of economic benefit or other business purposes'* …" (Paragraph 209, emphasis added/italics in the original).

[64] See Paras. 186, 192, 196 and 225 of the Apotex I & II Award.

7.65. For Mr. Rowley, it was plain that the Apotex I & II tribunal simply did not determine whether the relevant ANDAs here in issue (*i.e.* finally approved ANDAs plus associated products) constitute an "investment" under the terms of NAFTA Article 1139(g). Indeed, as it addressed the character of tentatively approved ANDAs, it was at pains to point out how they differed from finally approved ANDAs. How the Apotex I & II tribunal would have decided the claims made by Apotex in this proceeding is not relevant to the question as to what was "distinctly in issue" before it, and what it "distinctly determined", except to the extent that if the question needs to be asked, it points strongly to the conclusion that the Apotex I & II tribunal did not decide the question here in issue.

7.66. As to whether Apotex Inc.'s finally approved ANDAs are properly characterised as an "investment" for the purposes of NAFTA Article 1139(g), Mr. Rowley considers the uncontroverted evidence that: (i) Apotex's finally approved ANDAs were being used for the purposes of economic benefit at the time of the Import Alert; (ii) such ANDAs are regularly bought and sold in the US (often for substantial amounts); (iii) FDA regulations explicitly recognise that ANDAs are "owned" by the applicant; and (iv) US tax law treats ANDAs as franchises or intangibles for the purposes of the US tax code, is sufficient proof that Apotex's ANDAs here in issue constitute intangible property for the purposes of NAFTA Article 1139(g).

Date of dispatch to the parties: December 16, 2002

International Centre for Settlement of Investment Disputes

MARVIN FELDMAN

v.

MEXICO
CASE No. ARB(AF)/99/1

AWARD

President	: Prof. Konstantinos D. KERAMEUS
Members of the Tribunal	: Mr. Jorge COVARRUBIAS BRAVO Prof. David A. GANTZ
Secretary of the Tribunal	: Mr. Alejandro A. ESCOBAR and Ms. Gabriela ALVAREZ AVILA

In Case No. ARB(AF)/99/1,

between

Mr. Marvin Roy Feldman Karpa,
represented by
Mr. Mark B. Feldman, Ms. Mona M. Murphy, Mr. Douglas R.M. King
of Feldman Law Offices, P.C. (formely Feith & Zell, P.C.), and
Mr. Nathan Lewin and Ms. Stephanie Martz of the Law Firm of Miller, Cassidy,
Larroca & Lewin, L.L.P.

and

The United Mexican States,
represented by Lic. Hugo Perezcano Díaz, Consultor Jurídico Subsecretaría de
Negociaciones Comerciales Internacionales
Ministry of Economy

THE TRIBUNAL,
Composed as above,
Makes the following Award

have considered allegations of a violation of Article 1110 and attempted to articulate criteria for the determination (*S.D. Myers v. Canada* and *Pope & Talbot v. Canada*) the tribunals for various reasons have failed to find violations of Article 1110.

H.3 Respondent's Actions as an Expropriation Under Article 1110.

108. The Tribunal has struggled at considerable length, in light of the facts and legal arguments presented, the language of Article 1110 and other relevant NAFTA provisions, principles of customary international law and prior NAFTA tribunal decisions, to determine whether the actions of the Respondent relating to the Claimant constituted indirect or "creeping" expropriation, or actions tantamount to expropriation. (There is in this case no allegation of a direct expropriation or taking under Article 1110.) The conclusion that they do not is explained below.

109. The facts presented here might, depending on their interpretation, appear to support a finding of an indirect or creeping expropriation. The Claimant, through the Respondent's actions, is no longer able to engage in his business of purchasing Mexican cigarettes and exporting them, and has thus been deprived completely and permanently of any potential economic benefits from that particular activity.8 Between 1991, when the Claimant brought his *Amparo* action, and December 1997, when SHCP definitively refused to provide CEMSA with tax rebates on exported cigarettes, SHCP followed an inconsistent and non-transparent course of action. In some instances, SHCP authorized and paid the rebates (for 1992 exports, for example), in others, for significant periods of time (1994 -1995), it denied them. At various times SHCP officials provided written documentation to the Claimant that might have led some persons—reasonably or otherwise-- to believe that SHCP had agreed with the Claimant's position that the 1993 *Amparo* decision required that the Claimant be afforded the rebates (see, *e.g.*, letters of March 12, 1992, May 10, 1994 and March 16, 1997). SHCP has

8As discussed in the "Damages" section of this Award (paras. 189-207), there is a serious question as to whether the Claimant's business would have been economically viable even had SHCP consistently granted the rebates in the proper amount, given the very low gross profit, based on the gross profit of less than US$0.10 between CEMSA's net-of-tax cost of the cigarettes and the selling prices realized from CEMSA's customers.

sought through a tax audit a refund of rebates paid to the Claimant in 1996 and 1997, increased by an inflation factor, interest and possible penalties. Also, under Article 2103(6) of NAFTA, the State Parties expressly confirm that tax regulatory activity may be expropriatory under Article 1110, albeit with significant limitations.9

110. No one can seriously question that in some circumstances government regulatory activity can be a violation of Article 1110. For example, in *Pope & Talbot*, Canada argued that "mere interference is not expropriation; rather, a significant degree of deprivation of fundamental rights of ownership is required."10 That tribunal rejected this approach:

> Regulations can indeed be characterized in a way that would constitute creeping expropriation... Indeed, much creeping expropriation could be conducted by regulation, and a blanket exception for regulatory measures would create a gaping loophole in international protection against expropriation. (*Id., para.* 99.)

However, the *Pope & Talbot* tribunal failed to find a violation of Article 1110 in that case. This Tribunal finds the legal arguments against a finding of expropriation more persuasive, for reasons described in detail below, and reaches the same conclusion on facts very different from those in *Pope & Talbot.*

111. This Tribunal's rationale for declining to find a violation of Article 1110 can be summarized as follows: (1) As *Azinian* suggests, not every business problem experienced by a foreign investor is an expropriation under Article 1110; (2) NAFTA and principles of customary

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9 First, NAFTA Article 2103 generally excludes tax measures from coverage under NAFTA: "Except as set out in this Article, nothing in this Agreement shall apply to tax measures." However, this exclusion is not absolute. Article 2103(3)(b) makes Article 1102 applicable to tax measures, and Article 2103(6) makes Article 1110 applicable under certain conditions. Article 1105 is not mentioned among the exceptions to the exclusion; therefore, it does not apply to tax measures, other than in a situation in which an expropriation under Article 1110 has been found, and there is an analysis as to whether the expropriatory action met the requirements of due process and Article 1105 as provided in Article 1110(1)(c).

10 *Pope & Talbot v. Government of Canada*, Interim Award, June 26, 2000, paras. 87-88, http://www.state.gov/documents/organization/3989.pdf. Canada also asserted that "tantamount" simply means "equivalent," and that this language was not intended to expand Article 1110's coverage beyond creeping expropriation to cover regulatory action. *Id*. para. 89.

international law do not *require* a state to permit "gray market" exports of cigarettes; (3) at no relevant time has the IEPS law, as written, afforded Mexican cigarette resellers such as CEMSA a "right" to export cigarettes (due primarily to technical/legal requirements for invoices stating tax amounts separately and to their status as non-taxpayers); and (4) the Claimant's "investment," the exporting business known as CEMSA, as far as this Tribunal can determine, remains under the complete control of the Claimant, in business with the apparent right to engage in the exportation of alcoholic beverages, photographic supplies, contact lenses, powdered milk and other Mexican products--any product that it can purchase upon receipt of invoices stating the tax amounts-- and to receive rebates of any applicable taxes under the IEPS law. While none of these factors alone is necessarily conclusive, in the Tribunal's view taken together they tip the expropriation / regulation balance away from a finding of expropriation.

H.3.1 Many Business Problems Are Not Expropriations

112. First, the 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). As the *Azinian* tribunal observed, "It is a fact of life everywhere that individuals may be disappointed in their dealings with public authorities... It may be safely assumed that many Mexican parties can be found who had business dealings with governmental entities which were not to their satisfaction..." (*Robert Azinian and Others v. The United Mexican States*, Award, November 1, 1999, para. 83, 14 ICSID Review. FILJ 2, 1999.) To paraphrase *Azinian*, not 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.

113. Here, it is undeniable that the Claimant has experienced great difficulties in dealing with SHCP officials, and in some respects has been treated in a less than reasonable manner, but that treatment under the circumstances of this case does not rise to the level of a

violation of international law under Article 1110. Unfortunately, tax authorities in most countries do not always act in a consistent and predictable way. The IEPS law on its face (although not necessarily as applied) is undeniably a measure of general taxation of the kind envisaged by Restatement Comment g (see *supra*, paras. 105, 106). As in most tax regimes, the tax laws are used as instruments of public policy as well as fiscal policy, and certain taxpayers are inevitably favored, with others less favored or even disadvantaged.

114. Moreover, the Claimant could have availed himself early on of the procedures available under Mexican law to obtain a formal, binding ruling on the invoice issue from SHCP, but apparently chose not to do so (see prepared testimony of Fernando Heftye, paras. 7-9). Despite the legal uncertainties of the issues upon which the success of his business depended, the Claimant asked for clarification of the legal issues under Article 4 of the IEPS law only when effectively forced to do so, in April 1998 after SHCP denied the Claimant's request for tax rebates for the October 1997 – January 1998 exports, and in March 1999 when as a result of a tax audit SHCP demanded return of rebates, plus interest, inflation adjustment and penalties, for rebates earlier received in 1996 and 199711. It is unclear why he refrained from seeking clarification, but he did so at his peril, particularly given that he was dealing with tax laws and tax authorities, which are subject to extensive formalities in Mexico and in most other countries of the world.

H.3.2 Gray Market Exports and International Law

115. Second, NAFTA and principles of customary international law do not, in the view of the Tribunal, *require* a state to permit cigarette exports by unauthorized resellers (gray market exports). A prohibition to this effect may rely on objective reasons. Such reasons include

11 Also, although the Tribunal is aware, as indicated earlier, that the 1999 Fiscal Court proceedings challenging SHCP's efforts to recoup tax rebates from the Claimant are not final, the most recent decision has upheld the Claimant's position that the requirements of the IEPS law for invoices stating the tax amounts separately and precluding rebates for exports to low tax jurisdictions, are unconstitutional under Mexican law. The significance of this court decision is somewhat offset by the fact that in a separate, 1998 proceeding challenging denials of tax rebates from October 1997 through January 1998, which is final, another Mexican court determining essentially the same issues found in favor of SHCP (*see* Amparo decision of August 24, 2000).

despite the likely absence of invoices stating the tax amounts separately (*e.g*. memorial, para. 36; App. 1047-1070). As a result of this decision and Lynx' *Amparo* victory (which applied specifically only to alcoholic beverage exports), SHCP also paid rebates to Lynx for IEPS taxes applicable to cigarette exports in 1992, along with substantial additional amounts for interest and inflation.40 This was a period during which CEMSA faced uncertainty over the availability of rebates for cigarette exports, despite the fact that limited exports were made in 1992 by CEMSA. However, by 1996, when SHCP recognized Lynx' right to the rebates, SHCP had denied rebates to CEMSA for test shipments for several years.

180. All of this confirms a further weakness in the Respondent's argument that there can be no *de facto* discrimination under circumstances where rebates are essentially granted initially on the basis of a ministerial decision, with the detailed analysis coming later in the event of questions or an audit. Given the Claimant's notoriety at SHCP over the years, the newspaper articles and threats of litigation against SHCP officials, the audit that was initiated and then abruptly terminated in 1995, the multiple meetings with SHCP officials, etc., it is difficult for the Tribunal to believe that the Claimant's requests and actions were not well-known to and carefully monitored by SHCP officials. Those factors certainly created the necessary conditions for discrimination.

I.2.3 Discrimination as a Result of Nationality

181. It is clear that the concept of national treatment as embodied in NAFTA and similar agreements is designed to prevent discrimination on the basis of nationality, or "by reason of nationality." (U.S. Statement of Administrative Action, Article 1102.) However, it is not self-evident, as the Respondent argues, that any departure from national treatment must be

40 See Zaga-Hadid testimony, transcript, July 13, 2001, p. 142, tables introduced into evidence during the hearing. Allegations that Lynx had been intentionally paid excessive rebates by SHCP were denied (third witness statement of Diaz-Guzman, App. 06455-06456) and further disputed at the hearing by both parties. The evidence on this issue before the Tribunal is conflicting, and the Tribunal is not convinced that the amounts paid, including interest paid and the inflation adjustment for the 1993-1996 period, were in fact excessive.

explicitly shown to be a result of the investor's nationality. There is no such language in Article 1102. Rather, Article 1102 by its terms suggests that it is sufficient to show less favorable treatment for the foreign investor than for domestic investors in like circumstances. In this instance, the evidence on the record demonstrates that there is only one U.S. citizen/investor, the Claimant, that alleges a violation of national treatment under NAFTA Article 1102 (transcript, July 13, 2001, p. 178), and at least one domestic investor (Mr. Poblano) who has been treated more favorably. For practical as well as legal reasons, the Tribunal is prepared to assume that the differential treatment is a result of the Claimant's nationality, at least in the absence of any evidence to the contrary.

182. However, in this case there is evidence of a nexus between the discrimination and the Claimant's status as a foreign investor. In the first place, there does not appear to be any rational justification in the record for SHCP's less favorable *de facto* treatment of CEMSA other than the obvious fact that CEMSA was owned by a very outspoken foreigner, who had, prior to the initiation of the audit, filed a NAFTA Chapter 11 claim against the Government of Mexico. Certainly, the action of filing a request for arbitration under Chapter 11 could *only* have been taken by a person who was a citizen of the United States or Canada (rather than Mexico), i.e., as a result of his (foreign) nationality. While a tax audit in itself is not, of course, evidence of a denial of national treatment, the fact that the audit was initiated shortly after the Notice of Arbitration (first Feldman affidavit, paras. 85-86) and the existence of the unsigned memo at SHCP noting the filing of the Chapter 11 claim in the context of the Claimant's export registration efforts, at minimum raise a very strong suspicion that the events were related, given that no similar audit action was taken against domestic reseller/exporter taxpayers at the time.

183. More generally, requiring a foreign investor to prove that discrimination is based on his nationality could be an insurmountable burden to the Claimant, as that information may only be available to the government. It would be virtually impossible for any claimant to meet the burden of demonstrating that a government's motivation for discrimination is nationality rather than some other reason. Also, as the Respondent argues, if the motives for a government's actions should not be examined, there is effectively no way for the Claimant or this Tribunal to make the subjective determination that the discriminatory action of the government is a result of

the Claimant's nationality, again in the absence of credible evidence from the Respondent of a different motivation. If Article 1102 violations are limited to those where there is explicit (presumably *de jure*) discrimination against foreigners, e.g., through a law that treats foreign investors and domestic investors differently, it would greatly limit the effectiveness of the national treatment concept in protecting foreign investors.

184. This conclusion is consistent with that reached in an earlier Chapter 11 proceeding, *Pope & Talbot v. Government of Canada.* The *Pope & Talbot* tribunal indicated its inclination to presume that discriminatory treatment of foreign investors in like circumstances would be in violation of Article 1102. According to that tribunal such differences between domestic and foreign investors would "presumptively violate Article 1102(2), unless they have a reasonable nexus to rational government policies that (1) do not distinguish, on their face or *de facto*, between foreign-owned and domestic companies, and (2) do not otherwise unduly undermine the investment liberalizing objectives of NAFTA." One of that tribunal's concerns was that if there had to be a showing that the discrimination was based on nationality, it would "tend to excuse discrimination that is not facially directed at foreign owned investments" (*Pope & Talbot v. Government of Canada*, Award on the Merits of Phase 2, April 10, 2001, paras. 78, 79, http://www.dfait-maeci.gc.ca/tna-nac/Award_Merits-e.pdf) (The *Pope & Talbot* tribunal, on the facts, ultimately declined to find a violation of national treatment). In the instant case, the treatment between the foreign investor and domestic investors in like circumstances is different on a *de facto* basis, and such discrimination is clearly in conflict with the investment liberalization objective found in Article 1102. This Tribunal sees no reason to disagree with the *Pope & Talbot* tribunal's articulation in this respect.

I.2.4 Most Favored Investor Requirement?

185. NAFTA is on its face unclear as to whether the foreign investor must be treated in the most favorable manner provided for *any* domestic investor, or only with regard to the treatment generally accorded to domestic investors, or even the least favorably treated domestic investor. There is no "most-favored investor" provision in Chapter 11, parallel to the most favored nation provision in Article 1103, that suggests that a foreign investor must be treated no less favorably than the most favorably treated national investor, if there are other national

L. DECISION

For these reasons, the Tribunal

209. Finds that the Respondent has not violated the Claimant's rights or acted inconsistently with the Respondent's obligations under NAFTA Article 1110;

210. Finds that the Respondent has acted inconsistently with the Claimant's rights and the Respondent's obligations under NAFTA Article 1102;

211. Orders the Respondent to pay immediately to the Claimant the sum of $ 9,464,627.50 Mexican pesos as principal, plus interest generated at the time of signature of this award, in the amount of $7,496,428.47 Mexican pesos, which interest shall accrue until the date the payment is effectively made, pursuant to the last part of paragraph 205 of this award; the interest to be calculated shall be simple interest, for each month of the period of calculation at a rate equivalent to the yield for the month, of the Federal Treasury Certificates, issued by the Mexican Government, with a maturity of 28 days.

212. Denies all other claims for compensation;

213. Orders that each party be responsible for its own legal fees and related costs, and that the costs of the arbitration, as billed by ICSID, be shared equally by the parties.

Made as at Ottawa, Province of Ontario, Canada, in English and Spanish.

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Professor Konstantinos D. Kerameus
Date:

_____

Mr. Jorge Covarrubias Bravo
(subject to the attached dissenting opinion)
Date:

_____

Professor David A. Gantz
Date:

CASE No. ARB(AF)/97/l

INTERNATIONAL CENTRE FOR
SETTLEMENT OF INVESTMENT DISPUTES
(ADDITIONAL FACILITY)

B E T W E E N:

METALCLAD CORPORATION
Claimant

and

THE UNITED MEXICAN STATES
Respondent

A W A R D

Before the Arbitral Tribunal constituted under Chapter Eleven of the North American Free Trade Agreement, and comprised of:

Professor Sir Elihu Lauterpacht, QC, CBE
President

Mr Benjamin R. Civiletti

Mr José Luis Siqueiros

Date of dispatch to the parties: August 30, 2000

timely disposition in relation to an investor of a Party acting in the expectation that it would be treated fairly and justly in accordance with the NAFTA.

100. Moreover, the acts of the State and the Municipality – and therefore the acts of Mexico – fail to comply with or adhere to the requirements of NAFTA, Article 1105(1) that each Party accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment. This is so particularly in light of the governing principle that internal law (such as the Municipality's stated permit requirements) does not justify failure to perform a treaty. (*Vienna Convention on the Law of Treaties, Arts. 26, 27*).

101. The Tribunal therefore holds that Metalclad was not treated fairly or equitably under the NAFTA and succeeds on its claim under Article 1105.

C. NAFTA, Article 1110: Expropriation

102. NAFTA Article 1110 provides that "[n]o party shall directly or indirectly . . . expropriate an investment . . . or take a measure tantamount to . . . expropriation . . . except: (a) for a public purpose; (b) on a nondiscriminatory basis; (c) in accordance with due process of law and Article 1105(1); and (d) on payment of compensation . . . ." "A measure" is defined in Article 201(1) as including "any law, regulation, procedure, requirement or practice".

103. Thus, expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.

104. By permitting or tolerating the conduct of Guadalcazar in relation to Metalclad which the Tribunal has already held amounts to unfair and inequitable treatment breaching Article 1105 and by thus participating or acquiescing in the denial to Metalclad of the right to operate the landfill, notwithstanding the fact that the project was fully approved and endorsed by the federal government, Mexico must be held to have taken a measure tantamount to expropriation in violation of NAFTA Article 1110(1).

105. The Tribunal holds that the exclusive authority for siting and permitting a hazardous waste landfill resides with the Mexican federal government. This finding is consistent with the testimony of the

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referred to in NAFTA Article 1117.

Secretary of SEMARNAP and, as stated above, is consistent with the express language of the LGEEPA.

106. As determined earlier (see above, para 92), the Municipality denied the local construction permit in part because of the Municipality's perception of the adverse environmental effects of the hazardous waste landfill and the geological unsuitability of the landfill site. In so doing, the Municipality acted outside its authority. As stated above, the Municipality's denial of the construction permit without any basis in the proposed physical construction or any defect in the site, and extended by its subsequent administrative and judicial actions regarding the *Convenio*, effectively and unlawfully prevented the Claimant's operation of the landfill.

107. These measures, taken together with the representations of the Mexican federal government, on which Metalclad relied, and the absence of a timely, orderly or substantive basis for the denial by the Municipality of the local construction permit, amount to an indirect expropriation.

108. The present case resembles in a number of pertinent respects that of *Biloune, et al. v. Ghana Investment Centre, et al.*, 95 I.L.R.183, 207-10 (1993) (Judge Schwebel, President; Wallace and Leigh, Arbitrators). In that case, a private investor was renovating and expanding a resort restaurant in Ghana. As with Metalclad, the investor, basing itself on the representations of a government affiliated entity, began construction before applying for a building permit. As with Metalclad, a stop work order was issued after a substantial amount of work had been completed. The order was based on the absence of a building permit. An application was submitted, but although it was not expressly denied, a permit was never issued. The Tribunal found that an indirect expropriation had taken place because the totality of the circumstances had the effect of causing the irreparable cessation of work on the project. The Tribunal paid particular regard to the investor's justified reliance on the government's representations regarding the permit, the fact that government authorities knew of the construction for more than one year before issuing the stop work order, the fact that permits had not been required for other projects and the fact that no procedure was in place for dealing with building permit applications. Although the decision in *Biloune* does not bind this Tribunal, it is a persuasive authority and the Tribunal is in agreement with its analysis and its conclusion.

109. Although not strictly necessary for its conclusion, the Tribunal also identifies as a further ground for a finding of expropriation the Ecological Decree issued by the Governor of SLP on September 20, 1997. This Decree covers an area of 188,758 hectares within the "Real de Guadalcazar" that includes the landfill site, and created therein an ecological preserve. This Decree had the effect of barring forever the operation of the landfill.

110. The Tribunal is not persuaded by Mexico's representation to the contrary. The Ninth Article, for instance, forbids any work inconsistent with the Ecological Decree's management program. The

management program is defined by the Fifth Article as one of diagnosing the ecological problems of the cacti reserve and of ensuring its ecological preservation. In addition, the Fourteenth Article of the Decree forbids any conduct that might involve the discharge of polluting agents on the reserve soil, subsoil, running water or water deposits and prohibits the undertaking of any potentially polluting activities. The Fifteenth Article of the Ecological Decree also forbids any activity requiring permits or licenses unless such activity is related to the exploration, extraction or utilization of natural resources.

111. The Tribunal need not decide or consider the motivation or intent of the adoption of the Ecological Decree. Indeed, a finding of expropriation on the basis of the Ecological Decree is not essential to the Tribunal's finding of a violation of NAFTA Article 1110. However, the Tribunal considers that the implementation of the Ecological Decree would, in and of itself, constitute an act tantamount to expropriation.

112. In conclusion, the Tribunal holds that Mexico has indirectly expropriated Metalclad's investment without providing compensation to Metalclad for the expropriation. Mexico has violated Article 1110 of the NAFTA.

VIII. QUANTIFICATION OF DAMAGES OR COMPENSATION

A. Basic Elements of Valuation

113. In this instance, the damages arising under NAFTA, Article 1105 and the compensation due under NAFTA, Article 1110 would be the same since both situations involve the complete frustration of the operation of the landfill and negate the possibility of any meaningful return on Metalclad's investment. In other words, Metalclad has completely lost its investment.

114. Metalclad has proposed two alternative methods for calculating damages: the first is to use a discounted cash flow analysis of future profits to establish the fair market value of the investment (approximately $90 million); the second is to value Metalclad's actual investment in the landfill (approximately $20–25 million).

115. Metalclad also seeks an additional $20–25 million for the negative impact the circumstances are alleged to have had on its other business operations. The Tribunal disallows this additional claim because a variety of factors, not necessarily related to the La Pedrera development, have affected Metalclad's share price. The causal relationship between Mexico's actions and the reduction in value of Metalclad's other business operations are too remote and uncertain to support this claim. This element of damage is, therefore, left aside.

International Centre for Settlement of Investment Disputes

TECNICAS MEDIOAMBIENTALES TECMED S.A.

v.

THE UNITED MEXICAN STATES

CASE No. ARB (AF)/00/2

AWARD

President: **Dr. Horacio A. GRIGERA NAON**

Co-arbitrators: **Prof. José Carlos FERNANDEZ ROZAS**
Mr. Carlos BERNAL VEREA

Secretary to the Tribunal: **Ms. Gabriela ALVAREZ AVILA**

Date of dispatch to the parties: May 29, 2003

have similar characteristics. Although formally an expropriation means a forcible taking by the Government of tangible or intangible property owned by private persons by means of administrative or legislative action to that effect, the term also covers a number of situations defined as *de facto* expropriation, where such actions or laws transfer assets to third parties different from the expropriating State or where such laws or actions deprive persons of their ownership over such assets, without allocating such assets to third parties or to the Government.[125]

114. Generally, it is understood that the term "…equivalent to expropriation…" or "tantamount to expropriation" included in the Agreement and in other international treaties related to the protection of foreign investors refers to the so-called "indirect expropriation" or "creeping expropriation", as well as to the above-mentioned *de facto* expropriation.[126] Although these forms of expropriation do not have a clear or unequivocal definition, it is generally understood that they materialize through actions or conduct, which do not explicitly express the purpose of depriving one of rights or assets, but actually have that effect. This type of expropriation does not necessarily take place gradually or stealthily — the term "creeping" refers only to a type of indirect expropriation—and may be carried out through a single action, through a series of actions in a short period of time or through simultaneous actions. Therefore, a difference should be made between creeping expropriation and *de facto* expropriation,[127] although they are usually included within the broader concept of "indirect expropriation" and although both expropriation methods may take place by means of a broad number of actions that have to be examined on a case-by-case basis to conclude if one of such expropriation methods has taken place.[128]

115. To establish whether the Resolution is a measure equivalent to an expropriation under the terms of section 5(1) of the Agreement, it must be first determined if the Claimant, due to the Resolution**,** was radically deprived of the economical use and enjoyment of its investments, as if the rights related thereto —such as the income or benefits related to the Landfill or to its exploitation— had ceased to exist. In other words, if due to the actions of the Respondent, the assets involved have lost their value or economic use for their holder and the extent of the loss.[129] This determination is important because it is one of the main elements to distinguish, from the point of view 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

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[125] Award dated August 30, 2000, in ICSID case No. ARB(AF)/97/1 *Metalclad v. United Mexican States*, 16 Mealey's International Arbitration Report (2000), pp. A-1 *et seq*.; p. A-13 (p. 33 of the award, 103): «Thus, expropriation [...] includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favor of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be expected economic benefit of property even if not necessarily to the obvious benefit of the host State. »

[126] G. Sacerdoti, Bilateral Treaties and Multilateral Instruments on Investment Protection, 269 Recueil des cours, Académie de droit international de La Haye, 255, 385-386 (1997).

[127] *Ibid*. p. 383.

[128] R. Dolzer & M.Stevens, Bilateral Investment Treaties, pp. 99-100 (1995).

[129] Partial award in the case *Pope Talbot Inc v. Government of Canada*, 102-104, pp. 36-38, www.naftalaw.org; and II Restatement of the Law (Third) Restatement of the Foreign Relations Law of the United States, § 712, pp. 200-201; notes 6-7, pp. 211-212 (1987).

those assets and rights of any real substance. Upon determining the degree to which the investor is deprived of its goods or rights, whether such deprivation should be compensated and whether it amounts or not to a *de facto* expropriation is also determined. Thus, the effects of the actions or behavior under analysis are not irrelevant to determine whether the action or behavior is an expropriation. Section 5(1) of the Agreement confirms the above, as it covers expropriations, nationalizations or

> ...any other measure with similar characteristics or *effects*...[130]

The following has been stated in that respect:

> In determining whether a taking constitutes an «indirect expropriation», it is particularly important to examine the effect that such taking may have had on the investor's rights. Where the effect is similar to what might have occurred under an outright expropriation, the investor could in all likelihood be covered under most BIT provisions.[131]

116. In addition to the provisions of the Agreement, the Arbitral Tribunal has to resolve any dispute submitted to it by applying international law provisions (Title VI.1 of the Appendix to the Agreement), for which purpose the Arbitral Tribunal understands that disputes are to be resolved by resorting to the sources described in Article 38 of the Statute of the International Court of Justice[132] considered, also in the case of customary international law, not as frozen in time, but in their evolution.[133] Therefore, it is understood that the measures adopted by a State, whether regulatory or not, are an indirect *de facto* expropriation if they are irreversible and permanent and if the assets or rights subject to such measure have been affected in such a way that "…any form of exploitation thereof…" has disappeared; i.e. the economic value of the use, enjoyment or disposition of the assets or rights affected by the administrative action or decision have been neutralized or destroyed.[134] Under international law, the owner is also deprived of property where the use or enjoyment of benefits related thereto is exacted or interfered with to a similar extent, even where legal ownership over the assets in question is not affected, and so long as the deprivation is not temporary. The government's intention is less important than the effects of the measures on the owner of the assets or on the benefits arising from such assets affected by the measures; and the form of the deprivation measure is less important than its actual effects.[135] To determine whether such an expropriation has taken place, the Arbitral Tribunal should not

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[130] Emphasis added by the Arbitral Tribunal.
[131] R. Dolzer & M. Stevens, Bilateral Investment Treaties, p. 100 (1995).
[132] I. Brownlie, Principles of International Law (5th Edition, 1998) p.3: «These provisions […] represent the previous practice of arbitral tribunals, and Article 38 is generally regarded as a complete statement of the sources of international law ».
[133] *Mondev International Ltd v. United States of America* award, October 11, 2002, ICSID case No. ARB(AF)/99/2, p. 40, 116
[134] European Court of Human Rights, *In the case of Matos e Silva, Lda., and Others v. Portugal,* judgment of September 16, 1996, 85, p. 18, http://hudoc.echr.coe.int
[135] See Iran-USA Claims Tribunal, *Tippetts, Abbet,McCarthy, Stratton v.TAMS/Affa Consulting Engineers of Iran et al.,* decision of June 29, 1984; 6 Iran-United States Rep., p. 219 *et seq*.; p. 225 (1984-II); of the same Tribunal, *Phelps Dodge Corp. et al.v.Iran*, 10 Iran-U.S.Cl. Trib. Rep. p. 121 *et seq*..; esp. 22, p.130 (1986-I).

.... restrict itself to evaluating whether a formal dispossession or expropriation took place, but should look beyond mere appearances and establish the real situation behind the situation that was denounced.[136]

117. The Resolution meets the characteristics mentioned above: undoubtedly it has provided for the non-renewal of the Permit and the closing of the Landfill permanently and irrevocably, not only due to the imperative, affirmative and irrevocable terms under which the INE's decision included in the Resolution is formulated, which constitutes an action — and not a mere omission— attributable to the Respondent, with negative effects on the Claimant's investment and its rights to obtain the benefits arising therefrom, but also because after the non-renewal of the Permit, the Mexican regulations issued by INE become fully applicable. Such regulations prevent the use of the site where the Landfill is located to confine hazardous waste due to the proximity to the urban center of Hermosillo. Since it has been proved in this case that one of the essential causes for which the renewal of the Permit was denied was its proximity and the community pressure related thereto, there is no doubt that in the future the Landfill may not be used for the activity for which it has been used in the past and that Cytrar's economic and commercial operations in the Landfill after such denial have been fully and irrevocably destroyed, just as the benefits and profits expected or projected by the Claimant as a result of the operation of the Landfill. Moreover, the Landfill could not be used for a different purpose since hazardous waste has accumulated and been confined there for ten years. Undoubtedly, this reason would rule out any possible sale of the premises in the real estate market. Finally, the destruction of the economic value of the site should be assessed from the investor's point of view at the time it made such an investment. In consideration of the activities carried out, of its corporate purpose and of the terms and conditions under which assets related to the Landfill were acquired from Promotora, the Claimant, through Tecmed and Cytrar, invested in such assets only to engage in hazardous waste landfill activities and to profit from such activities. When the Resolution put an end to such operations and activities at the Las Víboras site, the economic or commercial value directly or indirectly associated with those operations and activities and with the assets earmarked for such operations and activities was irremediably destroyed. The above conclusions are not jeopardized by the fact that the Resolution has not prevented Cytrar from continuing operating the Landfill until completion of the authorized installed capacity existing as of the Resolution's date. Such limited, temporary and partial continuation of operation of the Landfill does not modify the definitive and detrimental effects of the Resolution with respect to the long-term investment made in the Landfill. As far as the effects of such Resolution are concerned, the decision can be treated as an expropriation under Article 5(1) of the Agreement.

118. However, the Arbitral Tribunal deems it appropriate to examine, in light of Article 5(1) of the Agreement, whether the Resolution, due to its characteristics and considering not only its effects, is an expropriatory decision.

119. The principle that the State's exercise of its sovereign powers within the framework of its police power may cause economic damage to those subject to its powers as administrator without entitling them to any compensation whatsoever is undisputable. Another undisputed issue is that within the framework or from the viewpoint of the

[136] Interamerican Court of Human Rights, *Ivcher Bronstein Case (Baruch Ivcher Bronstein vs. Peru),* judgment of February 6, 2001, 124, p. 56; www.corteidh.or.cr.

domestic laws of the State, it is only in accordance with domestic laws and before the courts of the State that the determination of whether the exercise of such power is legitimate may take place. And such determination includes that of the limits which, if infringed, would give rise to the obligation to compensate an owner for the violation of its property rights.

120. However, the perspective of this Arbitral Tribunal is different. Its function is to examine whether the Resolution violates the Agreement in light of its provisions and of international law. The Arbitral Tribunal will not review the grounds or motives of the Resolution in order to determine whether it could be or was legally issued. However, it must consider such matters to determine if the Agreement was violated. That the actions of the Respondent are legitimate or lawful or in compliance with the law from the standpoint of the Respondent's domestic laws does not mean that they conform to the Agreement or to international law:[137]

> An Act of State must be characterized as internationally wrongful if it constitutes a breach of an international obligation, even if the act does not contravene the State's internal law – even if under that law, the State was actually bound to act that way.[138]

121. After reading Article 5(1) of the Agreement and interpreting its terms according to the ordinary meaning to be given to them (Article 31(1) of the Vienna Convention), we find no principle stating that regulatory administrative actions are *per se* excluded from the scope of the Agreement, even if they are beneficial to society as a whole —such as environmental protection—, particularly if the negative economic impact of such actions on the financial position of the investor is sufficient to neutralize in full the value, or economic or commercial use of its investment without receiving any compensation whatsoever. It has been stated that:

> Expropriatory environmental measures – no matter how laudable and beneficial to society as a whole – are, in this respect, similar to any other expropriatory measures that a state may take in order to implement its policies: where property is expropriated, even for environmental purposes, whether domestic or international, the state's obligation to pay compensation remains.[139]

122. After establishing that regulatory actions and measures will not be initially excluded from the definition of expropriatory acts, in addition to the negative financial impact of such actions or measures, the Arbitral Tribunal will consider, in order to determine if they are to be characterized as expropriatory, whether such actions or measures are proportional to the public interest presumably protected thereby and to the protection legally granted to investments, taking into account that the significance of such impact has a key role upon deciding the proportionality.[140] Although the analysis starts at the due deference owing to

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[137] International Court of Justice, *Elettronica Sicula s.p.a.(ELSI)(United States v. Italy)* case, judgment dated July 20, 1989, ICJ Reports, 1989, 73. ICSID Case No.ARB(AF)/99/1, *Marvin Feldman v. Mexico*, award of December 16, 2002, p.26, 78, www.naftalaw.org.

[138] J. Crawford, The International Law Commission's Articles on State Responsibility, p. 84 (Cambridge University Press, 2002).

[139] Award: *Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica,* ICSID case No. ARB/96/1, 15 ICSID Review-Foreign Investment Law Journal, 72, p.192 (2000).

[140] European Court of Human Rights, *In the case of Matos e Silva, Lda., and Others v. Portugal,* judgment of September 16, 1996, 92, p. 19 , http://hudoc.echr.coe.int.

International Centre for Settlement of Investment Disputes

BAYINDIR INSAAT TURIZM TICARET VE SANAYI A.Ş.

CLAIMANT

v.

ISLAMIC REPUBLIC OF PAKISTAN

RESPONDENT

ICSID Case No. ARB/03/29

AWARD

Rendered by an Arbitral Tribunal composed of:

Prof. Gabrielle Kaufmann-Kohler, President

Sir Franklin Berman, Arbitrator

Prof. Karl-Heinz Böckstiegel, Arbitrator

Martina Polasek, Secretary

Date of Dispatch to the Parties: August 27, 2009

the Decision on Jurisdiction, in which the Tribunal stated with reference to *Impregilo v. Pakistan*:[136]

> "[O]nly measures taken by Pakistan in the exercise of its sovereign power ('puissance publique'), and not decisions taken in the implementation or performance of the Contracts, may be considered as measures having an effect equivalent to expropriation."[137]

438. If a showing of breach of contract resulting from governmental directives were sufficient to constitute expropriation, then any "governmental act would by definition be one of *puissance publique*" (C.-Mem. M., ¶ 4.77), a proposition that Pakistan considers unfounded. More specifically, Pakistan argues that:

> "[I]n circumstances where (i) a State entity enters into a contract, (ii) that contract was negotiated between the investor, the State entity and given governmental departments and (iii) those governmental departments remain involved in monitoring the performance of the contract, indeed, their input is actively sought by the investor, it would not in any event be an act of puissance publique for the governmental departments to recommend or even direct that the contract should be terminated because of the investor's breach. Such a recommendation or decision would constitute nothing more than a decision taken in the implementation or performance of the given contract." (C.-Mem. M., ¶ 4.77)

439. Finally, Pakistan contends that a finding of expropriation generally requires, in addition to the loss of the investment, arbitrary conduct or an intentional deprivation on the part of the State (C.-Mem. M., ¶ 4.79; Rej. M., ¶ 4.49).

3. Tribunal's determination

440. The basis for the assessment of Bayindir's expropriation claim is Article III(1) of the Treaty, which reads as follows:

> "Investments shall not be expropriated, nationalized or subject, directly or indirectly, to measures of similar effects except for a public purpose, in a non-discriminatory manner, upon payment of prompt, adequate and effective compensation, and in accordance with due process of law and the general principles of treatment provided for in Article II of this Agreement."

441. The Tribunal concurs with the Claimant when it asserts that Article III(1) adopts a broad concept of expropriation, potentially applicable not only to tangible property but also to contractual and other rights, even outside the context of a nationalization.

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136 *Impregilo v. Pakistan*, *supra* footnote 26, ¶ 281.

137 Decision on Jurisdiction, ¶ 257.

442. The first step in assessing the existence of an expropriation is to identify the assets allegedly expropriated. In the present case, the assets identified by the Claimant, namely its contractual rights, plant and equipment, and the Mobilisation Advance Guarantees, are within the scope of Article III(1) of the Treaty, and may potentially be subject to an interference amounting to expropriation.

443. Having identified the assets, the next step is to identify the allegedly expropriatory conduct. As stated in the Decision on Jurisdiction, expropriation may arise out of a simple interference by the host State in the investor's rights with the effect of depriving the investor of its investment.[138] A critical issue in this regard concerns the intensity or the effect of such conduct with respect to the investor's property. The Tribunal concurs with *Tecmed*, *CMS*,[139] and *Telenor*,[140] that an expropriation might occur even if the title to the property is not affected, depending on the level of deprivation of the owner[141]:

> "[I]t is understood that the measures adopted by a State, whether regulatory or not, are an indirect *de facto* expropriation if they are irreversible and permanent and if the assets or rights subject to such measure have been affected in such a way that "…any form of exploitation thereof…" has disappeared; i.e. the economic value of the use, enjoyment or disposition of the assets or rights affected by the administrative action or decision have been neutralized or destroyed. Under international law, the owner is also deprived of property where the use or enjoyment of benefits related thereto is exacted or interfered with to a similar extent, even where legal ownership over the assets in question is not affected, and so long as the deprivation is not temporary. The government's intention is less important than the effects of the measures on the owner of the assets or on the benefits arising from such assets affected by the measures; and the form of the deprivation measure is less important than its actual effects. To determine whether such an expropriation has taken place, the Arbitral Tribunal should not:
> [...] restrict itself to evaluating whether a formal dispossession or expropriation took place, but should look beyond mere appearances and establish the real situation behind the situation that was denounced."[142]

444. The third step in this inquiry consists in examining whether the alleged interference with the property or the rights of the investor has been made in the State's exercise of its

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138 Decision on Jurisdiction, ¶ 255.

139 *CMS v. Argentina*, *supra* footnote 77, ¶ 260-264.

140 *Telenor Mobile Communications AS v. Republic of Hungary* (ICSID Case No. ARB/04/15), Award of 13 September 2006.

141 *Starrett Housing Corp. v. The Government of the Islamic Republic of Iran*, Interlocutory Award of 19 December 1983, 4 Iran-US CTR 122; *Tippetts, Abbett, McCarthy, Stratton v. TAMS-AFFA Consulting Engineers of Iran*, Award of 22 June 1984, 6 Iran-US CTR 219.

142 *Tecmed v. Mexico, supra* footnote [53], ¶ 116.

sovereign powers. As noted for instance in *Impregilo v. Pakistan* cited in lieu of others, such as *Siemens v. Argentina*,[143] or *RFCC v. Morocco*[144]:

> "[O]nly measures taken by Pakistan in the exercise of its sovereign power (*"puissance publique"),* and not decisions taken in the implementation or performance of the Contracts, may be considered as measures having an effect equivalent to expropriation."[145]

445. In the present case, the Claimant has suggested that a breach of the Contract as a result of governmental directives would suffice for a finding of expropriation. The Tribunal disagrees. First, not every contract breach deprives an investor of the substance of its investment. Second, even where it does and the breach stems from a governmental directive, it would not necessarily follow that the contractual breach is the result of a sovereign act, as a directive of the State may be given in the framework of the contract.

446. The fourth step in assessing the existence of an expropriation in breach of the Treaty is the analysis of the conditions specified in Article III(1), namely (i) the lack of a public purpose, (ii) discrimination, (iii) the absence of payment of prompt, adequate and effective compensation, and (iv) a breach of "due process of law and the general principles of treatment provided for in Article II of this Agreement."

b. Contractual rights

1. Bayindir's position

447. Bayindir submits that Pakistan expropriated the investment indirectly in a clandestine manner under the pretext of exercising contractual rights, in order to give effect to a governmental change in policy towards Bayindir. In Bayindir's submission, Pakistan acted in an arbitrary and discriminatory manner with the intention of permanently depriving it of its contractual rights. More specifically, through its forcible expulsion pursuant to the notice of 23 April 2001, it was deprived of the benefits it expected to derive from the Contract as well as from payment for works executed until the expulsion.

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143 *Siemens v. Argentina*, *supra* footnote 59, ¶ 253.

144 *RFCC v. Morocco*, *supra* footnote 32, ¶¶ 65-69, 85-89.

145 *Impregilo v. Pakistan*, *supra* footnote 26, ¶ 281.

V. RELIEF

[491] For the reasons set forth above, the Tribunal issues the following Award:

a. The Respondent has not breached the fair and equitable treatment standard applicable through the operation of Article II(2) of the Treaty;

b. The Respondent has not breached the national treatment and most favoured nation standards contained in Article II(2) of the Treaty;

c. The Respondent has not expropriated the Claimant in breach of Article III(1) of the Treaty;

d. The measures recommended in PO#1 and PO#11 shall no longer be in effect as of the date of the notification of the present Award;

e. The Parties shall bear the costs of the arbitration in equal shares;

f. Each Party shall bear its own legal and other costs;

g. All other claims are dismissed.

Sir Franklin Berman

Date: 20 August 2009

Prof. Karl-Heinz Böckstiegel

Date: 24 August 2009

Prof. Gabrielle Kaufmann-Kohler

Date: August 14, 2009

International Centre for Settlement of Investment Disputes
Washington, D.C.

Total S.A.

v.

Argentine Republic

(ICSID Case No. ARB/04/1)

Decision on Liability

Members of the Tribunal

Professor Giorgio Sacerdoti, President

Mr. Henri C. Alvarez, Arbitrator

Dr. Luis Herrera Marcano, Arbitrator

Secretary of the Tribunal

Ms. Natalí Sequeira

Representing Total S.A.:

Mr. Jan Paulsson, Mr. Nigel Blackaby,
Mr. Georgios Petrochilos, Mr. Noah Rubins,
Ms. Sylvia Noury, Mr. Craig Chiasson,
Mr. Moto Maeda, Ms. Caroline Richard
Freshfields Bruckhaus Deringer LLP
Paris, France

Mr. Alexander Yanos and Mr. Giorgio Mandelli
Freshfields Bruckhaus Deringer LLP
New York, NY, Unites States of America

Mr. Luis A. Erize and Mr. Sergio M. Porteiro
Abeledo Gottheil Abogados SC
Buenos Aires, Argentina

Representing the Argentine Republic:

Dr. Joaquín Pedro da Rocha
Procurador del Tesoro de la Nación Argentina
Procuración del Tesoro de la Nación Argentina
Buenos Aires, Argentina

Date of Dispatch to the Parties: December 27, 2010

compensation."[216] On the other, Total points out that Argentina's Measures, even if regarded as regulatory or police power measures, constitutes an expropriation because they contradict the specific undertakings Argentina gave to Total and are therefore in breach of Article 5(2) of the BIT, last sentence. These specific undertakings or assurances are identified by the Claimant as:

> "(a) the commitment to preserve TGN's economic equilibrium through recurrent and extraordinary tariff reviews with the aim of ensuring that tariffs remained sufficient to cover costs and earn a reasonable rate of return; and, in support of this commitment (b) the promise to calculate tariffs in dollars and adjust them in accordance with the US PPI; …"[217]

9.2 Tribunal's Conclusions

191. Before discussing the legal issues, the Tribunal considers it appropriate to recall the evidence concerning Total's position as a major shareholder of TGN and its role as "Technical Operator". On the basis of the evidence and the arguments of the parties in their Post-Hearing Briefs it is uncontested that Total is in full control of its investment in TGN. Conversely, TGN operates under the management of its shareholders and carries on its daily activities. It is listed on the Buenos Aires Stock Exchange. The government's decision in 2004 to establish a trust fund system in order to finance expansions of the network by imposing surcharges on the tariffs paid by industrial users does not entail either loss of control by Total over its investments nor TGN's loss of control over its business operations. The trust fund finances the expansion of the network (which TGN is unable to do due to the lack of adequate revenues caused by freezing the tariffs), while TGN operates the network as licensee,[218] besides managing the expansion projects.[219] Total has not shown that the trust fund interferes with the ability of TGN shareholders to manage TGN. Based on the evidence, the Tribunal considers that Total has not been precluded in any way from exercising its rights as a shareholder in TGN, as it was able to go on managing TGN's business together with the other shareholders in TGN. The Tribunal

[216] See Total's Post-Hearing Brief, para. 586.
[217] See Total's Post-Hearing Brief, para. 587.
[218] See Argentina Rejoinder, paras 452-457 and Total's Post-Hearing Brief, para. 519. The parties agree that a small part of the expansion was financed by TGN and that the cooperation between the trust fund and TGN is governed by agreement between them.
[219] See Total's Post-Hearing Brief, para. 519.

concludes that Total "is in control of the investment; the Government does not manage the day-to-day operations of the company; and the investor has full ownership and control of the investment", as the ICSID Tribunal dealing with *CMS* claim – another foreign investor in TGN - found in May 2005.[220]

192. The Tribunal will first examine Article 5(2) of the BIT, interpreting it in accordance with Article 31 of the Vienna Convention on the Law of the Treaties.[221] As mentioned above, Article 5(2) states that:

> "The Contracting Parties shall not take, directly or indirectly, any expropriation or nationalization measures or any other equivalent measures having a similar effect of dispossession, except for reasons of public necessity and on condition that the measures are not discriminatory or contrary to a specific undertaking."[222]

193. The key expression as to indirect expropriation is the protection from "any expropriation or nationalisation measures or any other equivalent measures having a similar effect of dispossession." Therefore, besides expropriations and nationalisations, Article 5(2) covers measures which are "equivalent" to expropriation and nationalisation, as far as they have a "similar effect of dispossession."[223] Contrary to Total's position, the term "dispossession" is not a "non-technical term." The term "dispossession" refers to a precise legal concept under civil law systems to which both France and Argentina belong. Possession is a factual relation between a thing, object or asset and a person who exercises factual control over it. Possession in Roman and civil law is independent in part from legal property.[224] While a lawful owner or acquirer is entitled to obtain and exercise

[220] See *CMS Gas Transmission Company v. Argentina*, *supra* note 29, para. 263.
[221] Article 31 VCLT states that: "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."
[222] In the French original: "Les Parties contractantes ne prennent pas, directement ou indirectement, de mesures d'expropriation ou de nationalisation, ni tout autre mesure équivalente ayant un effet similaire de dépossession, si ce n'est pour cause d'utilité publique et à condition que ces mesures ne soient ni discriminatoires, ni contraires à un engagement particulier." In the Spanish original: "Las Partes Contratantes se abstendrán de adoptar, de manera directa o indirecta, medidas de expropiación o de nacionalización o cualquier otra medida equivalente que tenga un efecto similar de desposesión, salvo por causa de utilidad pública y con la condición que estas medidas no sean discriminatorias ni contrarias a un compromiso particular."
[223] See Argentina's Rejoinder, para. 542 where Argentina points out that: "…,the Argentina-France BIT also makes reference to measures equivalent to expropriation, as the Argentina-US BIT and the NAFTA, which the Claimant fails to mention…."
[224] See G. Cornu, *Vocabulaire Juridique*, Presses Universitaires de France, 2000, p. 651, according to whom 'possession' is a "*pouvoir de fait exercé sur une chose avec l'intention de s'en affirmer le maître (animus domini), même si – le sachant ou non – on ne l'est pas*;" and the term "*possesio rei*" "*signifiant «possession d'une chose*»

possession, possession, as a factual matter, may exist without or irrespective of a title. Indeed, property may derive from protracted undisturbed possession over a thing by a non-owner. The term "dispossession" therefore refers necessarily to the loss of the control which is characteristic of "possession".

194. The use of the terms "*dépossession*" or "*mesures dont l'effet est de déposséder*" to characterise indirect expropriation is typical of French BITs. As stressed by two authoritative French commentators "*dans son acception habituelle, la mesure de dépossession est celle qui prive l'investisseur de ses droit essentiels sur l'investissement au profit de l'autorité publique, quelles que soient les modalités de cette dépossession.*"[225] Contrary to Total's position, in requiring a loss of material control over the investment, the term "dispossession" in Article 5(2) appears somehow to be more restrictive than the parallel provisions in the Argentina-U.S. ("tantamount to expropriation") and the Argentina-UK BIT which refer only to "equivalent to nationalisation or expropriation". Since Total has not been dispossessed of its TGN holding nor of the management of its business, the Tribunal concludes that the requirement of dispossession under Article 5(2) has not been met.

195. In any case, the Tribunal will also address Total's argument that it is well-established that a substantial deprivation of the value of an investment constitutes indirect expropriation. Hence, Total requests the Tribunal to find *in casu* that Argentina's measures, having caused such a loss, are in breach of Article 5(2) of the BIT. Looking beyond the specific wording of Article 5(2), the Tribunal considers that under international law a measure which does not have all the features of a formal expropriation could be equivalent to an expropriation if an effective deprivation of the investment is thereby caused. An effective deprivation requires, however, a total loss of value of the property such as when the property affected is rendered worthless by the measure, as in case of direct expropriation, even if formal title continues to be

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servant aujourd'hui à désigner la possession qui correspond au droit de propriété." See also, *ibid.* p. 278 where the term '*dépossession'* is defined as "[*p]erte de la possession, soit par violence ou voie de fait, soit à un titre juridique (gage, antichrèse, séquestre*); privation effective de la détention matérielle d'une chose. " As to this notion under Argentina's legal system see the entry '*poseer'* in Ana María Cabanellas de las Cuevas, Diccionario Jurídico Universitario, Editorial Heliasta, 1ra Edición, 2000, Tomo II: poseer is defined as "*tener materialmente una cosa en nuestro poder. Encontrarse en situación de disponer y disfrutar directamente de ella…"*

[225] See D. Carreau, P. Juillard, *Droit international économique*, 1ere édition, 2003, para 1376, at p. 508. The two authors, discussing the use of term "*dépossession*" in the French model BIT, go on to state that "*[m]ais d'autres instruments, notamment le modèle américain et…l'ALENA, utilisent l'expression, qui parait mieux appropriée, de mesures équivalant à une mesure d'expropriation ou de nationalisation.*" (see para. 1377 at p. 509)

held.[226] This is supported by the general direction of the case law under BITs,[227] other international jurisprudence[228] and scholarly legal opinions.[229]

196. In light of the above legal principles, the Tribunal turns to examine the merits of Total's claim that it is the victim of an indirect expropriation. The Tribunal considers that Total has not shown that the negative economic negative impact of the Measures has been such as to deprive its investment of all or substantially all its value. Therefore the Tribunal rejects Total's claim of indirect expropriation in breach of Article 5(2) of the BIT. We note that this conclusion is consistent with all of the previous arbitral precedents dealing with indirect expropriation claims brought by foreign investors in the utility sector under various BITs in respect of the same or similar measures of Argentina in 2001-2002. According to this uniform arbitral case law, Argentina's Measures have been considered to not give rise to an indirect expropriation under various BITs,[230] in the absence of an effective deprivation of the value of the foreign investment in the above-mentioned meaning (*i.e.*, total deprivation of the investment's value or total loss of control by the investor of its investment, both of a permanent nature).

197. Before concluding on this claim, the Tribunal recalls that the Claimant challenged a number of distinct measures under Article 5(2) of the BIT: the

[226] Thus, an expropriation could be found even where control remains in the hands of the foreign investor provided that economic profitability of the investment has been totally destroyed in some other way.

[227] See *Sempra Energy International v. Argentina*, *supra* note 189, para. 285 where the Tribunal stated that "a finding of indirect expropriation would require more than adverse effect. It would require that the investor no longer be in control of its business operation, or that the value of the business have been virtually annihilated." As to Argentina's Measures see also *LG&E v. Argentina*, *supra* note 111, para. 191 where it is stated that "[i]nterference with the investment's ability to carry on its business is not satisfied where the investment continues to operate, even if profits are diminished. The impact must be substantial in order that compensation may be claimed for the expropriation"; *BG Group Plc v. Argentina*, *supra* note 113, paras 258-266 and *Enron Corporation and Ponderosa Assets, L.P. v. Argentina*, *supra* note 20, para. 245. See also *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States*, *supra* note 116, para. 115; *CME Czech Republic B.V. v. Czech Republic*, UNCITRAL, Partial Award, 13 September 2001, para. 604; *Goetz and others v. Burundi*, ICSID Case No. ARB/95/3, Award (Embodying the Parties' Settlement Agreement), 10 February 1999, para. 124.

[228] See for example *Starrett Housing Corp. v. Iran*, Award, 14 August 1987, 4 Iran-US C.T.R. 122, at pp. 154-157; *Tippets, Abbett, McCarthy, Stratton v. TAMS-AFFA Consulting Engineers of Iran*, Award, 29 June 1984, 6 Iran-US C.T.R. 219, p. 255.

[229] See C. Leben, *La liberté normative de l'État et la question de l'expropriation indirecte*, C. Leben (dir.), *Le contentieux arbitral transnational relative à l'investissement*, Anthemis, 2006, 163 ff. at p. 173-175; R. Dolzer, C. Schreuer, *supra* note 133, at p. 96-101.

[230] See *LG&E v. Argentina*, *supra* note 111, para. 200 where the Tribunal stated that: "the effect of the Argentine State's actions has not been permanent on the value of the Claimants' share, and Claimants' investment has not ceased to exist. Without a permanent, severe deprivation of LG&E's rights with regard to its investment, or almost complete deprivation of the value of LG&E's investment, the Tribunal concludes that these circumstances do not constitute expropriation." See also *BG Group Plc v. Argentina*, *supra* note 113, para. 268-270; *Enron Corporation and Ponderosa Assets, L.P. v. Argentina*, *supra* note 20, para. 246.

Part V - Decision of the Tribunal on Liability

485. Based on the above reasoning and findings, the Tribunal, partially granting Total's claims, DECIDES as follows:

a) Argentina breached its obligations under Article 3 of the BIT to grant to Total fair and equitable treatment, as specified in paragraphs 184, 346, 444, 455, 461, causing damage to Total;

b) All other claims by Total, including those under Articles 4 and 5 of the BIT, are rejected;

c) All defences by Argentina, including those relating to the alleged state of necessity, are rejected;

d) The Argentine Republic is liable to Total for the aforementioned violations of the BIT and the damages thereby suffered by Total must be compensated by Argentina, as will be determined in a separate quantum phase of these arbitration proceedings, and in respect of which the Tribunal retains jurisdiction. The Tribunal will issue a separate order concerning the further proceedings for the quantum phase.

e) Any decision on the costs of the arbitration is reserved.

Done in English and Spanish, both versions being equally authoritative.

ICSID Case No. ARB(AF)/04/01

International Centre for Settlement of Investment Disputes
(Additional Facility)

CORN PRODUCTS INTERNATIONAL, INC.
Claimant

and

THE UNITED MEXICAN STATES
Respondent

DECISION ON RESPONSIBILITY

Before the Arbitral Tribunal constituted under Chapter Eleven of
the North American Free Trade Agreement (NAFTA), and comprised of:

Professor Andreas F. Lowenfeld
Licenciado Jesús Alfonso Serrano de la Vega
Professor Christopher J. Greenwood (President)

Secretary of the Tribunal
Mr. Gonzalo Flores

Date: 15 January 2008

107. Instead, Mexico urged the Tribunal to rely upon the award in *GAMI v. Mexico*,[32] where the tribunal had held that financially secure sugar producers in Mexico were not in like circumstances as those sugar producers which were in financial difficulty, so that the Mexican Government had not violated Article 1102 when it expropriated a number of financially insecure concerns, some of which were owned by United States investors, while leaving in private ownership other financially secure mills, some of which were Mexican-owned.

108. Mexico also relied on the award in *Loewen v. USA*,[33] which it read as authority for the proposition that parties in adverse interest could not also be in like circumstances for the purposes of Article 1102. CPI and the Mexican sugar producers were, it said, in adverse interest not only because they competed in the market for soft drink sweeteners but also because CPI, through the trade association of which it was a member, had opposed the relaxation of United States barriers on access for Mexican sugar to the United States market.

C. The Tribunal's Analysis

109. The Tribunal notes at the outset that Article 1102 embodies a principle of fundamental importance, both in international trade law and the international law of investment, that of non-discrimination. A study prepared for UNCTAD went so far as to say that –

[32] Award of 15 November 2004; to be published in 13 ICSID Reps.
[33] ICSID Case No. ARB(AF)/98/3; 7 ICSID Reps. 421.

> "the national treatment standard is perhaps the single most important standard of treatment embodied in international investment agreements."[34]

110. Its significance in the legal regime of GATT/WTO is also beyond doubt. GATT Article III, which embodies the principle of like treatment for like products irrespective of national origin is one of the cornerstones of that regime. Article III.4 provides that -

> "The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. The provisions of this paragraph shall not prevent the application of differential internal transportation charges which are based exclusively on the economic operation of the means of transport and not on the nationality of the product."[35]

111. The absolute character of this provision, as well as its central role within the regime, was highlighted by the GATT Panel in the *Section 337* case, involving a challenge by the European Community to procedures for determining patent disputes between domestic and imported products. The Panel there stated that -

> "The Panel noted that, as far as the issues before it are concerned, the 'no less favourable' treatment requirement set out in Article III.4 is unqualified ... The words 'treatment no less favourable' ... call for effective equality of opportunities for imported products in respect of the application of laws, regulations and requirements affecting the internal sale, purchase, transportation, distribution or use of products. This clearly sets a minimum standard as a basis. ... Given that the underlying objective is to guarantee equality of treatment, it is incumbent on the contracting party applying differential treatment to

[34] UNCTAD, *National Treatment* (1999), United Nations Doc UNCTAD/ITE/IIT/11 (vol. IV), p. 1
[35] See also Article XVII of the GATS.

> show that, in spite of such differences, the no less favourable treatment standard of Article III is met."[36]

112. The relationship between the principle of non-discrimination in matters of trade and non-discrimination in matters of investment was evident in the Canada-US Free Trade Agreement, Chapter 16 of which was largely carried over into Chapter XI of NAFTA (although Chapter XI of NAFTA contained the important additional feature of investor-State arbitration which had been absent from the earlier agreement).

113. The principle of national treatment is given prominence in the statement of the objectives of the NAFTA in Article 102(1), which provides that –

> "The objectives of this Agreement, as elaborated more specifically through its principles and rules, including *national treatment*, most-favoured-nation treatment and transparency, are to:
>
> (a) eliminate barriers to trade in, and facilitate the cross-border movement of, goods and services between the territories of the Parties;
>
> (b) promote conditions of fair competition in the free trade area;
>
> (c) increase substantially investment opportunities in the territories of the Parties;
>
> (d) provide adequate and effective protection and enforcement of intellectual property rights in each Party's territory;
>
> (e) create effective procedures for the implementation and application of this Agreement, for its joint administration and for the resolution of disputes; and

[36] *United States - Section 337 of the Tariff Act of 1930,* GATT Panel Report adopted 7 November 1989, BISD 36th Supp. 345 (1990), para. 5.11.

(f) establish a framework for further trilateral, regional and multilateral cooperation to expand and enhance the benefits of this Agreement.".[37]

114. Specific instances of the principle of non-discrimination appear in Articles 301 (national treatment with regard to goods), 1202 (national treatment with regard to services) and 1405 (national treatment with regard to financial services), as well as Article 1102, the provisions of which were described by the Tribunal in *Feldman* as "a fundamental obligation of Chapter XI".[38] The *Feldman* Tribunal also stressed that language analogous to that of Article 1102 was to be found in GATT Article III and in the Canada-US Free Trade Agreement.[39]

115. The parties in the present case agreed that Article 1102 embraces *de facto* as well as *de jure* discrimination.[40] The Tribunal agrees. The parties differed, however, on almost every other issue of relevance to the application of Article 1102 to the HFCS Tax.

116. The Tribunal considers, therefore, that it is necessary to start from first principles. The text of Article 1102 suggests that there are three elements which have to be established for a claim under that provision to succeed.

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[37] Emphasis added. Article 102(2) provides that "the Parties shall interpret and apply the provisions of this Agreement in the light of its objectives as set out in paragraph 1 and in accordance with applicable rules of international law".

[38] 7 ICSID Reps. 318, para. 165.

[39] Ibid.

[40] CPI asserted that Article 1102 encompassed *de facto* discrimination in its Memorial, para. 298. Mexico accepted that proposition in response to a question from the Tribunal at the oral hearings, Transcript, Day 4, p. 1019, lines 15-16 (Mr Becker).

117. First, it must be shown that the Respondent State has accorded to the foreign investor or its investment "treatment ...with respect to the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition" of the relevant investments. Secondly, the foreign investor or investments must be "in like circumstances" to an investor or investment of the Respondent State ("the comparator"). Lastly, the treatment must have been less favourable than that accorded to the comparator.[41]

118. The application of this three-fold test must, however, be sensitive to the particular circumstances of each case with the analysis focussing on the specific nature of the measure under challenge. In this respect, there is a close relationship between whether the State intentionally discriminated on grounds of nationality and the test of like circumstances. As other Chapter XI tribunals have emphasised, it is necessary to consider the entire factual and legal context.[42]

119. Applying these principles to the facts of the present case, the first question is whether the imposition of the HFCS tax on the soft drink bottlers can be regarded as "treatment" accorded by Mexico to CPI. The Tribunal considers that it should be so regarded. Mexico concedes that the tax was not intended to raise revenue but to assist the Mexican sugar industry at a time of crisis and to respond to what Mexico considered was a US violation of other NAFTA provisions. It is obvious that if either of these objectives was to be

[41] See, e.g., the Award on the Merits of 24 May 2007 in *UPS* v. *Canada*, para. 83.
[42] *Pope and Talbot* Award, paras 75-78; *SD Myers*, para. 245.

achieved, the tax would have to produce an effect upon the HFCS producers and suppliers, of which CPI was the largest (with approximately [XXX] of the HFCS share of the market before the HFCS tax took effect). By contrast, there was no intention to produce any effect upon the bottlers other than of pressuring them to switch from HFCS to sugar as a sweetener. In these circumstances, it would be the triumph of form over substance to hold that the fact that the tax was structured as a tax on the bottlers, rather than the suppliers of sweeteners, precluded it from amounting to treatment of the latter for the purposes of Article 1102.

120. Turning to the question of whether CPI and the other producer of HFCS in Mexico were in like circumstances to the Mexican sugar producers – the only suggested comparator – the Tribunal concludes that this requirement is satisfied on the facts of the present case. It considers that it is necessary to begin with a comparison between domestic and foreign investors operating in the same business or economic sector as the claimant.[43] There can be no doubt that Mexican sugar producers operated in the same business or economic sector as CPI. When it came to supplying sweeteners to the soft drinks industry, their products were in direct competition with one another, treated both by customers and by Mexican law as being interchangeable. The purpose of the HFCS tax was avowedly to alter the terms of competition between them.

[43] See, e.g., *Pope and Talbot*, paras. 75-78.

121. In this context the Tribunal takes note of the fact that the WTO Panel and Appellate Body have held that HFCS and sugar were "like products" for the purposes of Article III of GATT. The Tribunal is mindful of the warning, afforded by *Methanex,*[44] that the terms of GATT Article III were taken into Chapter III of the NAFTA and not Chapter XI, where different language was used. It is also conscious that its jurisdiction is limited to the provisions of Chapter XI and does not extend to Chapter III. It accepts that CPI cannot succeed in its claim under Article 1102 simply by showing that HFCS and sugar are "like products" for the purposes of Article III of GATT, nor does it understand CPI to have advanced such an argument. The test under Article 1102 is a separate and distinct test from that under Article III.4 of GATT (or Article 301 of the NAFTA for that matter).

122. Nevertheless, the Tribunal does not accept that the fact that HFCS and sugar are like products for the purposes of GATT is irrelevant to the application of the Article 1102 test. On the contrary, it considers that this fact is highly relevant to the application of that test. While the Tribunal would not suggest that the fact that a foreign investor and a domestic investor are producing like products will necessarily mean that they are to be considered as being in like circumstances for the purposes of Article 1102, or that differential treatment will necessarily entail a violation of that provision, where the measure said to constitute the violation of Article 1102 is directly concerned with the products and designed to discriminate in favour of one and against the other,

[44] 44 ILM (2005) 1343 at Part IV, Chapter B, para. 30.

then that is a very strong indication that there has been a breach of Article 1102.

123. Although the passage from *Methanex* quoted in paragraph 103, above might be thought to take a different view, the Tribunal considers that the Final Award in *Methanex*, taken as a whole, is not inconsistent with the approach suggested in the preceding paragraph. The *Methanex* tribunal expressly recognized the relevance of GATT/WTO jurisprudence.[45] In addition, it is pertinent to note that that tribunal was at pains to emphasise that methanol was not a direct competitor with ethanol, since the latter was used as an additive to petrol whereas the former was merely one ingredient of the additive MTBE,[46] that the measure said to violate Article 1102 was not discriminatory on its face since it applied equally to US producers of methanol who were the obvious comparators for Methanex[47] and that the measure was adopted for legitimate regulatory reasons.

124. By contrast, HFCS is directly substitutable for sugar as a soft drink sweetener and, as stated above, had always been treated as such by Mexico. That fact also sets the present case apart from the facts of the *UPS* case, where the tribunal pointed out that packages delivered by mail and those sent by courier were treated differently (and had historically been treated differently) both by Canada and by other States.

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[45] 44 ILM (2005) 1343 at Part II, Chapter B, para. 6.

[46] "The incontrovertible fact is that Methanex produced methanol as a feedstock for MTBE and not as a gasoline additive in its own right." (Ibid., at Part IV, Chapter B, para. 28).

[47] Para. 21.

X. Conclusions and Decision

193. The Tribunal therefore decides that:-

(1) Mexico has incurred responsibility for a violation of Article 1102 in respect of CPI and CPIng;

(2) The quantum of compensation will be determined in a later phase of the proceedings;

(3) CPI and CPIng's other claims are dismissed;

(4) The question of costs will be determined as part of the next phase of the proceedings.

[signature]
Andreas F. Lowenfeld

[signature]
Jesús Alfonso Serrano de la Vega

[signature]
Christopher J. Greenwood

In proceedings pursuant to NAFTA Chapter 11 and the UNCITRAL Arbitration Rules:

BETWEEN

GAMI INVESTMENTS, INC.

Claimant

And

THE GOVERNMENT OF THE UNITED MEXICAN STATES

Respondent

FINAL AWARD

15 November 2004

Before the Tribunal comprising:

W. Michael Reisman
Julio Lacarte Muró
Jan Paulsson

Representing the Claimant:

Weil Gotshal & Manges LLP
Charles E. Roh, Jr.
Adam P. Strochak
J. Sloane Strickler
Alicia Cate

SAI Abogados
Guillermo Aguilar Alvarez
Lucía Ojeda
Elsa Ortega
Itziar Esparza

Representing the Respondent:

Consultor jurídico de los Estados Unidos Mexicanos
Hugo Perezcano Díaz

Secretaría de Economía
Luis González García

Thomas & Partners
J. Cameron Mowatt
Gregory A. Tereposky

Shaw Pittmann LLP
Stephan E. Becker
Sanjay Mullick

Secretary to the Tribunal:
Zachary Douglas

Formal seat of the arbitration: Vancouver

Mexico's failure to do so made it impossible to apply and enforce the 2000 *Acuerdo*.

82. Mexico takes exception to the following passage in GAMI's Post-Hearing Brief:

> *"There is no question that the 1998 Acuerdo required the Government to determine per mill base production levels starting with the 1997-1998 harvest... Chief Justice Schmill's testimony that the Government was under a legal obligation to act stands unchallenged..."*

Mexico insists that Lic. Schmill said no more than that *producción base* levels set by the authorities for individual mills would be obligatory. This is not the same as saying that Mexico violated the 1998 *Acuerdo* because it did not define such levels for the 1998/99 harvest. Mexico's position is that both mill owners and *cañeros* agreed that the methodology of the 1998 *Acuerdo* was inadequate. It was therefore agreed with the Government to seek a new methodology. The result was a decision that the methodology of the 2000 *Acuerdo* would be based on the number of cultivated hectares corresponding to each mill. This was an "objective datum." (The previous reference to volumes produced during the 1997-98 harvest had resulted in an underestimation.) Each mill as well as the CNIAA itself thus knew what the point of reference would be. Mr Santos (as President of the CNIAA) explicitly acknowledged it as the product of an agreement which would be applied as of the 2000/01 harvest. The 2000 *Acuerdo* does not require that the levels be published. They are simply made available in the offices of the *Secretaría de Economía* and the CAA. GAM never asked for written or "official" confirmation.

6(B) Minimum standard of treatment: GAMI's claim under Article 1105

83. One cannot fail to observe that GAMI's complaint of alleged unfair and inequitable treatment is not connected with a demonstration of specific and quantifiable prejudice. Mexico's alleged wrongdoing would doubtless have resulted in some short-term decline in the value of its shares in GAM. (There would have been no loss of dividends: GAM's business strategy has never been to distribute earnings to shareholders.) The ultimate duration of this unspecified decline in value is

uncertain. It was bound to be reversed to some degree by the return of the three wrongfully expropriated mills and by the prospect of compensation for the two others (the expropriation of which GAM did not challenge). Above all there is consensus as to the positive effect of the more vigorous application of Mexico's Sugar Program.

84. GAMI did not attempt to prove or even present a theoretical financial analysis of what the short-term decline might have been. GAMI rather proceeds on the basis that the entire value of its investment has been destroyed. This is demonstrably untrue. GAMI's shareholding in GAM remains intact. GAM's principal productive assets have either been restored to it or are the subject of negotiations to determine compensation. The sugar industry is now operating on a better footing. Mr Pinto testified that a tax on soft drinks sweetened by fructose "has turned out to be a very beneficial measure for the Mexican sugar industry." GAM has declared itself to be optimistic for the future. Counsel for GAMI declared flatly in final oral submissions that "the system is working now." GAMI's failure to make good on its claim of total destruction will be dealt with in detail below when examining its claim of expropriation. But also with respect to the Article 1105 claim it must be noted that GAMI has not sought to quantify the alleged prejudice arising from particular alleged acts or omissions.

85. GAMI's approach seems to be all or nothing. But no credible cause-and-effect analysis can lay the totality of GAMI's disappointments as an investor at the feet of the Mexican Government. Both sides agree that the economics of sugar are highly distorted and subject to powerful international market forces. No one has suggested that NAFTA entitles an investor to act on the basis that a regulatory scheme constitutes a guarantee of economic success. GAMI can assert only that maladministration of the Sugar Program caused it *some* prejudice. But the prejudice must be particularised and quantified. GAMI has not done so. The Tribunal does not know if such a demonstration would even be possible in the circumstances given the problem of timing. There are years when the sun shines on the sugar industry. In Mexico in particular the industry has had its ups and downs. Recent developments have apparently been positive. GAMI presumably benefits from them. Absent a complete destruction of its investment GAMI has not identified a particular point in time when a metaphorical snapshot of its prejudice should be taken. It may be that such a demonstration is impossible in this case. At any rate the Tribunal would have been in no position to

award damages even if it had found a violation of Article 1105. The Tribunal will nevertheless explain its conclusion that GAMI also failed to establish its claim in principle under Article 1105.

86. GAMI has comprehensively demonstrated that the regulations which it refers to as "the Mexican Sugar Program" were not carried out in accordance with their terms. GAMI refers to "legal obligations" incumbent upon the Government under that regulatory scheme. It relies on an impressive legal opinion by a former Chief Justice of Mexico (Lic. Schmill) to the effect that the Government has a duty "to intervene directly and permanently" to ensure the effective implementation of decrees it has promulgated.

87. The three broad instances of failure of implementation and enforcement have been described in Section 6(A)(ii) above. The present Tribunal does not doubt that the fulfilment of the overarching regulatory objectives in question (reference price/export requirements/production controls) would in a very significant way have improved GAM's prospects and those of its shareholders. The Sugar Program has more recently been implemented with considerable success. The industry as a whole has enjoyed a revival even without the desired access to the US market.

88. GAMI contends that Mexico's failure to implement and enforce its laws was flagrant and arbitrary. GAMI submits that Mexico has thus infringed the standard articulated in *Técnicas Medioambiente Tecmed* as follows:

> *"The Arbitral Tribunal considers that this [fair and equitable treatment] provision of the Agreement, in light of the good faith principle established by international law, requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and*

> *administrative practices or directives, to be able to plan its investment and comply with such regulations. Any and all State actions conforming to such criteria should relate not only to the guidelines, directives or requirements issued, or the resolutions approved thereunder, but also to the goals underlying such regulations. The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities."*[12]

89. GAMI considers that the terms articulated in the subsequent *Waste Management II* award suggest greater leniency in assessing state behaviour under Article 1105. (*Técnicas Medioambiente Tecmed* was not a NAFTA case. It arose under the Spain/Mexico BIT which provides that each state party "shall guarantee fair and equitable treatment" to investors of the other state party.) GAMI submits that its grievance nevertheless satisfies the requirements articulated in that award. It quotes *Waste Management II* with the following added emphasis:

> *"Taken together, the* S.D. Myers, Mondev, ADF *and* Loewen *cases suggest that the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety – as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host*

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12 Award of 29 May 2003, 10 ICSID REPORTS (forthcoming) at para. 154.

> *State which were reasonably relied on by the claimant."*[13]

90. Mexico does not question this synthesis as such. It rather insists that this Tribunal does not have the mandate to control the application of national law by national authorities.

91. This contention misconceives the role of international law in the context of the protection of foreign investment. International law does not appraise the content of a regulatory programme extant before an investor decides to commit. The inquiry is whether the state abided by or implemented that programme. It is in this sense that a government's failure to implement or abide by its own law in a manner adversely affecting a foreign investor may but will not necessarily lead to a violation of Article 1105. Much depends on context. The imposition of a new licence requirement may for example be viewed quite differently if it appears on a blank slate or if it is an arbitrary repudiation of a preexisting licensing regime upon which a foreign investor has demonstrably relied.

92. The relevant international obligation is expressed in Article 1105(1) as follows:

> *"Each 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."*[14]

The challenging task for this Tribunal is to apply these abstractions. It is necessary first to enquire how they relate to compliance with national law.

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13 Para. 98.

14 The NAFTA Free Trade Commission issued Notes of Interpretation of Certain Chapter 11 Provisions in July 2001. These Notes state that Article 1105 is not intended to require treatment of aliens "beyond that which is required by the customary international law minimum standard." They also state that the determination that there has been a breach of another treaty obligation does not of itself establish a breach of Article 1105. GAMI says that its claims in this case "satisfy the standard set forth in the interpretation." It therefore deems it unnecessary to question whether the Notes constitute "a proper exercise of the interpretive power in Article 1131."

93. To repeat: NAFTA arbitrators have no mandate to evaluate laws and regulations that predate the decision of a foreigner to invest. The present Tribunal endorses and adopts the following passages from *S.D. Myers*:

> *"When interpreting and applying the 'minimum standard', a Chapter 11 tribunal does not have an open-ended mandate to second-guess government decision-making. Governments have to make many potentially controversial choices. In doing so, they may appear to have made mistakes, to have misjudged the facts, proceeded on the basis of a misguided economic or sociological theory, placed too much emphasis on some social values over others and adopted solutions that are ultimately ineffective or counterproductive. The ordinary remedy, if there were one, for errors in modern governments is through internal political and legal processes, including elections."*[15]

94. The duty of NAFTA tribunals is rather to appraise whether and how preexisting laws and regulations are applied to the foreign investor. It is no excuse that regulation is costly. Nor does a dearth of able administrators or a deficient culture of compliance provide a defence. Such is the challenge of governance that confronts every country. Breaches of NAFTA are assuredly not to be excused on the grounds that a government's compliance with its own law may be difficult. Each NAFTA Party must to the contrary accept liability if its officials fail to implement or implement regulations in a discriminatory or arbitrary fashion.

95. The ICSID tribunal in *Waste Management II* made what it called a "survey" of standards of review applied by international tribunals dealing with complaints under Article 1105. It observed the emergence of a "general standard for Article 1105."[16] It noted that a violation does not require proof of "the kind of outrageous treatment referred to in the *Neer* case."[17] *Neer* envisaged conduct that amounted to an "outrage,

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15 First Partial Award, *op. cit.*, note 8, para. 261.

16 Award of 24 April 2004, 10 ICSID REPORTS (forthcoming) at para. 98.

17 *Ibid.* para. 93.

to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that any reasonable and impartial man would readily recognize its insufficiency."[18] *Neer* was decided more than half a century before NAFTA saw the light of day. The *ADF* award observed that customary international law as reflected in Article 1105 is "constantly in a process of development." The standard which emerged from the *Waste Management II* tribunal's study has been properly identified by GAMI and is reproduced in Paragraph 89 above. GAMI contends that its claim satisfies this standard.

96. The award in *Waste Management II* goes on to say: "Evidently the standard is to some extent a flexible one which must be adapted to the circumstances of each case." The arbitrators concluded that the acknowledged failure to fulfil contractual obligations did not suffice to create liability under Article 1105.[19] This non-performance was balanced against the authorities' *attempts* to achieve the objectives of the concession. The tribunal was not persuaded that the record *as a whole* proved a breach of international law.

97. Four implications of *Waste Management II* are salient even at the level of generality reflected in the passages quoted above. (1) The failure to fulfil the objectives of administrative regulations without more does not necessarily rise to a breach of international law. (2) A failure to satisfy requirements of national law does not necessarily violate international law. (3) Proof of a good faith effort by the Government to achieve the objectives of its laws and regulations may counter-balance instances of disregard of legal or regulatory requirements. (4) The record as a whole – not isolated events – determines whether there has been a breach of international law. It is in this light that GAMI's allegations with respect to Article 1105 fall to be examined.

98. GAMI recognises that NAFTA tribunals have taken the view expressed as follows in *ADF v. USA*:

> *"[S]omething more than simple illegality or lack of authority under the domestic law of a State is necessary to render an act or measure*

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18 L.F. Neer v. Mexico, 1927 AJIL 555 at 556.

19 *Op. cit.* n. 16, at para. 109.

> *inconsistent with the customary international law requirements of Article 1105(1), even under the Investor's view of that Article."*[20]

GAMI argues that the requirement of "something more" is met as follows:

> *"Mexico's conduct in this case is far more egregious than a simple or isolated failure to follow some provision of the Sugarcane Decree. Mexico's actions and failures to act individually and cumulatively undermined the fundamental balance of the sugar laws, effectively turning GAMI's investment in GAM into a large contribution for the benefit of* cañeros, *and the Mexican Government itself, and those mills that were left unexpropriated. This is precisely what NAFTA prohibits. Such conduct is arbitrary, grossly unfair and far below the minimum standard required under Article 1105 and international law. ... [Mexico] arbitrarily and discriminatorily implemented certain aspects of the law and capriciously refused to implement and enforce others, thereby substantially destroying GAMI's investment."*

99. The factual and legal components of this argument must be examined. The proposition that GAMI's investment was destroyed is plainly not proven. GAM still exists. Its chief executive officer testified that GAM is recovering and he is "optimistic." Nor can it be accepted that GAM's difficulties were due entirely to Mexico's alleged failure to implement the Sugar Program. GAMI's argument is not that its investment would have been profitable but for Mexico's non-feasance. It is quite evident that this is not what GAMI believed at the time. Its Form 20-F Annual Report to the US Securities Exchange Commission for the year 1999 stated:

> *"There can be no assurance that the Company will be able to maintain sales at generally prevailing market prices for sugar in Mexico without discounts and that sufficient exports*

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[20] 6 ICSID REPORTS 470, at para. 190 (2003).

will take place in order to assure a domestic market balance."

100. The key question is the extent to which an investor may rely on the implementation by the host state of laws in place before its investment is made. What efforts by a government to implement its regulatory programme suffice to fulfil the international standards requirement of Article 1105? *Waste Management II* involved contractual undertakings between a governmental authority and the investor. No such undertakings may be invoked by GAMI. Some elements of the analysis in *Waste Management II* are nevertheless instructive.

101. The investor in *Waste Management II* adduced evidence which made it "clear that the City failed in a number of respects to fulfil its contractual obligations to Claimant."[21] The investor's contractual claims could be brought before the Mexican courts. Indeed as contractual claims they could be brought nowhere else given the relevant jurisdictional provisions. Yet claims of breaches of NAFTA could be brought to arbitration under Chapter 11 without the need to exhaust local remedies. The problem in *Waste Management II* was therefore to identify the types of interference with contractual rights that could rise to the level of a breach of international obligations. The tribunal noted that in itself "even the persistent non-payment of debts by a municipality is not to be equated with a violation of Article 1105."[22] Otherwise "Chapter 11 would become a mechanism of equal resort for debt collections and analogous purposes in respect of all public (including municipal) contracts, which does not seem to be its purpose."[23] Something more was required. The conduct giving rise to the complaint does not violate Article 1105 as long as it does not "amount to an outright and unjustified repudiation of the transaction" and "some remedy is open to the creditor to address the problem."[24]

102. Something akin to this sequence of propositions is extant in the present case.

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21 *Op. cit.* n. 16, at para. 109.

22 Para. 115.

23 Para. 116.

24 Para. 115. This leaves open the issue of denial of justice. Such a claim was raised in *Waste Management II* but rejected. No such claim arises in the present case.

103. GAMI has demonstrated clear instances of failures to implement important elements of Mexican regulations. It has adduced eminent evidence to the effect that the Mexican government is constitutionally required to give effect to its regulations. Claims of maladministration may be brought before the Mexican courts. Indeed as breaches of Mexican administrative law they could be brought nowhere else. Yet GAMI's claims of breaches of NAFTA may be brought before this Tribunal under Chapter 11 without the need to exhaust local remedies. The problem is therefore to identify the type of maladministration that could rise to the level of a breach of international obligations. A claim of maladministration would likely violate Article 1105 if it amounted to an "outright and unjustified repudiation" of the relevant regulations. There may be situations where even lesser failures would suffice to trigger Article 1105. It is the record as a whole – not dramatic incidents in isolation – which determines whether a breach of international law has occurred.

104. GAMI has not been able to show anything approaching "outright and unjustified repudiation" of the relevant regulations. The Sugarcane Decree and its related measures certainly did not operate in accordance with their terms. But there is no evidence that Mexico set its face against implementation. There is no reason to doubt that Mexico would have *preferred* that all participants in the industry would find prosperity in the economic equilibrium conceived by the regulators. The Mexican authorities might have acted with greater initiative and perseverance. But it is not certain that the Mexican government was the sole and critical actor. There are unexplained questions with respect to the ultimate responsibility for the "consultations" which were to take place within the *Comités* and the JCACA. The same is true with respect to the apparent passivity of the CNIAA.

105. Would something less than repudiation still be actionable under Article 1105? What about an egregious failure to regulate? Might it be said that Mexico refused to hold feckless administrators to account for failure to carry out their assigned task? GAMI's thesis is not that Article 1105 requires Mexico to conceive and implement a successful regime of regulations for the sugar industry. Mr Roh rather put it as follows:

> *"... having chosen to create a sugar program, Mexico must abide by it and cannot arbitrarily*

> *apply some of its elements to reward some groups at the severe pain of others."*

GAMI understandably places much relevance on Lic. Schmill's statement to the effect that "*tratándose de une actividad de interés público, el Gobierno necesitaba intervenir de manera directa y permanente para hacer cumplir los objetivos del Decreto de 1991, sus modificaciones de 1993 y los Acuerdos de 1997, 1998 y 2000*" ("as this concerned an activity *de interés público*, the government had the duty to intervene in a direct and permanent manner to cause the objectives of the 1991 Decree to be fulfilled, along with its modifications in 1993 and the *Acuerdos* of 1997, 1998 and 2000").

106. GAMI argues that it relied on this proposition. Mr Aguilar forcefully outlined governmental shortcomings. He insisted that there was no valid explanation for the Government's failure to provide the data necessary for the adjustment of the reference price pursuant to the 1997 *Acuerdo*. He said that the CAA could hardly be faulted for not having generated timely base production levels when the Government waited for 21 months before convening the CAA. He opined that it would have been "futile" for aggrieved mills to go before the JCACA given that it "depended on government data and initiative."

107. Did Mexico indeed refuse to implement regulations in accordance with their terms? Or has GAMI overstated the import of those terms?

108. The record shows that Mexico failed to implement key struts of its Sugar Program notwithstanding its duties as explained by Lic. Schmill. GAMI alleges an abject failure to implement a regulatory program indispensable for the viability of foreign investments that had relied upon it. GAMI urges that in law this is no different from a violation by the government of the rules of that program. Both action and inaction may fall below the international standard. So far the Arbitral Tribunal is prepared to accept GAMI's proposition. But a critical step at this stage of the analysis is whether the specific failures of the Sugar Program are attributable to the government. It is on this point that the Tribunal concludes GAMI has not made its case.

109. The preamble of the 1997 *Acuerdo* refers to the objective of the Sugarcane Decree to augment the participation

of the social and private sectors (i.e. labour and industry) "*como responsables de la producción nacional de azúcar.*" It also refers to the authorisation given to the CAA to draw up "rules, definitions, and provisions" ("*reglas, definiciones y disposiciones*") to enhance the competitiveness of sugar production. The *Acuerdo* itself contains sophisticated formulae. Yet anyone can see that the expected national consumption and production are key elements (*Ce* and *Qu* in the formula). These were to be determined by the *Secretaría de Comercio* and other relevant government officials after having considered:

> *"la opinión de la Secretaría de Agricultura, Ganadería y Desarrollo Rural, de Financiera Nacional Azucarera S.N.C. del Comité de la Agroindustria Azucarera, de la Cámara Nacional de las Industrias Azucarera y Alcoholera, de la Unión Nacional de Productores de Caña de Azúcar de la Confederación Nacional Campesina y de la Unión Nacional de Cañeros de la Confederación Nacional de la Pequeña Propiedad."*

110. In sum: the regulatory regime was structured on the premise of broad consultations and cooperation. The intervention of the private sector was explicitly called for. An explicit role was reserved for the unions. The Mexican government was not the only actor in important aspects of the Sugar Program. GAMI says the Government could have forced the issue to ensure that the consultations took place. GAMI's closing oral arguments sought to build on a declaration by the *Secretaría de Agricultura* to the effect that the industry "*debe estar adecuadamente supervisada por el Estado.*" But the argument turns against GAMI. The distinction between "adequate supervision" and "effective implementation" is hardly subtle. There are certainly arguments on both sides. The debate is complex. For an international tribunal the relevant conclusion is simply that GAMI has not shown that the government's self-assigned duty in the regulatory regime was simple and unequivocal. It is impossible to conclude that the failures in the Sugar Program were both directly attributable to the government and directly causative of GAMI's alleged injury.

9. DECISION

137. For the reasons stated above the Tribunal hereby unanimously declares that it has jurisdiction over the claims and dismisses them in their entirety. All contentions to the contrary are rejected. There is no award of costs.

Done on 15 November 2004 in equally authoritative English and Spanish versions.

Julio Lacarte Muró

W. Michael Reisman

Jan Paulsson

IN THE MATTER OF AN ARBITRATION UNDER CHAPTER 11 OF
THE NORTH AMERICAN FREE TRADE AGREEMENT
AND THE UNCITRAL ARBITRATION RULES

BETWEEN:

MERRILL & RING FORESTRY L. P.

Claimant/Investor

and

THE GOVERNMENT OF CANADA

Respondent/Party

(ICSID Administered Case)

AWARD

The Tribunal

Professor Francisco Orrego Vicuña, President

Professor Kenneth W. Dam, Arbitrator

J. William Rowley QC, Arbitrator

Eloïse M. Obadia, Secretary of the Tribunal

141. While there can be no doubt that property such as the lands, logs or timber which are affected to the requisite degree by government measures will be protected under Article 1139(h), just as intangible interests arising from a contract directly related to the investment will be protected, the kind of right the Investor claims has been expropriated appears to fall under the exclusions noted. This was in fact the kind of situation envisaged in *Methanex* in respect of goodwill and in its conclusion that goodwill cannot be considered as a stand-alone vested right, a view which is also consistent with the principles of international law governing acquired rights, which also had limits, as reflected in the decision in *Oscar Chinn*.[71]

142. The right concerned would have to be an actual and demonstrable entitlement of the investor to a certain benefit under an existing contract or other legal instrument. This reasoning underlies the *Feldman* tribunal's conclusion that an investor cannot recover damages for the expropriation of a right it never had.[72] Expropriation cannot affect potential interests.

143. The Tribunal is in agreement with the view expressed in *Pope & Talbot* to the effect that the access to the United States' market was an important aspect of the business concerned in that case. So too, the Tribunal has no doubt that in this case, the right to access the international market is a fundamental aspect of the log export business of the Investor. Were this right impeded or prohibited it would certainly qualify for protection under NAFTA because it is the very objective of the investment made. However, there can be no doubt that the conditions and terms under which such a right may be exercised may be subject

[71] *See infra* para. 215.
[72] Feldman Award, para. 118.

to appropriate regulation, provided this does not result in a form of substantial interference with the business.

144. In this regard, as was also concluded in *Pope & Talbot*, the business of the investor has to be considered as a whole and not necessarily with respect to an individual or separate aspect, particularly if this aspect does not have a stand-alone character. It could well happen that a certain aspect is so fundamental to the business concerned that interference with it might result in a kind of compensable expropriation. And while the right to export is one such fundamental aspect, the protection against expropriation does not, and cannot, guarantee exports will be made at a certain price. Such a conclusion would transform NAFTA into an insurance policy, guaranteeing that every investor exporter will get for its products the best price available in the international market, which is a somewhat farfetched proposition.

145. The next question for the Tribunal to decide, assuming for this purpose that the Investor complains about the expropriation of a protected investment, is whether the degree of interference relied upon amounts to a taking of the rights concerned, either directly or indirectly. The standard of substantial deprivation identified in *Pope & Talbot*, and followed by many other decisions, both in the context of NAFTA and other investment protection agreements, is the appropriate measurement of the requisite degree of interference.

146. It is first patently clear to the Tribunal that neither the Government of Canada nor that of British Columbia has ever directed the operations of the company, which have been at all times directed by the Investor. In fact, it is the Investor that decides how much timber it wishes to plant and to cut under a production plan which is prepared entirely by its management. It is the Investor that

decides the amount of logs it wishes to submit to the export permit process and how much it may wish to sell in the domestic market. The question of minimum and maximum volumes only applies to the advertisement of logs from remote areas and it responds to specific conditions of those areas. The fact of having the production and export process regulated under government measures is entirely unrelated to the issue of directing the operations of the company. If it were, all industries and business round the world would have been expropriated because of the existing regulations pertaining to them.

147. It is also patently clear that the Investor's corporate officers have not been and are not now under the supervision of the state. There is no government administrator in place, nor is there any measure that might amount to the state watching over the business decisions of those officers. The observance of and compliance with the log export regime in no way approximates the sort of interference that might affect the independence and professional conduct of those officers. The same holds true of the management and shareholders activities, whose respective duties and rights have been determined independently by the company's decision-making bodies and processes.

148. In the end, the claim, as framed by the Investor, comes down to whether it could have obtained better profits in exporting logs to the international market, and whether its inability to achieve this profit level because of Notice 102 results in some form of taking of the proceeds of its sales. The Tribunal must first note in this respect that no argument has been made about the company operating at a loss as a consequence of government measures. If this were in fact the case, the value of the investment and its essential objectives would have been seriously compromised and this conceivably might amount to a taking. However, to the

contrary, Canada points out that the Investor operates at a significant profit in spite of the regulations complained of, and that the volume of its exports still constitutes by far the largest part of the Investor's operations. The Tribunal is satisfied that this is the case indeed.

149. As for the proceeds from the Investor's future sales, as explained above, such proceeds are only a potential future benefit that cannot be the subject of a taking because the Investor is not contractually entitled to them. The situation would be totally different if an existing contract for a certain volume of logs, at a certain price, had been interfered with by the government to the requisite extent. This is the kind of intangible property right protected under NAFTA and international law. But absent interference with rights of this sort, the state cannot guarantee a profit which is no more than an expectation on the drawing board and which may or may not actually be realized.

150. Legitimate expectations are no doubt an important element of a business undertaking, but for such expectation to give rise to actionable rights requires there to have been some form of representation by the state and reliance by an investor on that representation in making a business decision. And here there is no evidence whatsoever that Canada made any sort of representation to the Investor that it would enjoy a certain price level at the international market or the making of a certain profit thereon.

151. The Tribunal must conclude accordingly that the use, enjoyment or disposition of the property concerned have not been affected in this case so as to amount to an expropriation. While regulatory measures usually imply a long decision process, a rather typical situation in the forestry sector worldwide, the normal time period for completing an export permit in this case is not excessively long,

as reflected in the 35-45 day approval delay and the operation of the automated online application procedures. A lengthy delay could of course result in undue interference, but this is not the case here, except in limited and unusual circumstances.

152. The arguments made by the Investor in respect of losing control over its logs during the process of export approval, the encouragement of the practice of "blockmailing" as a consequence of the regulations, the satisfaction of domestic length preferences for cutting logs, and the deterioration of logs during the waiting time, are, if correct, inconveniences indeed, but they do not meet the standard of substantial deprivation so as to qualify for a compensable expropriation under NAFTA.

153. The fact that no individual contract right might have been affected or that no substantial deprivation has taken place, so as to constitute an expropriation, does not mean that the regime is necessarily in compliance with the broader standard of fair and equitable treatment, which is a separate matter. One argument in particular, made in the context of expropriation, is examined in greater detail below in the context of fair and equitable treatment. That is the Investor's view that the whole regime is geared towards providing low cost raw material for domestic sawmills in British Columbia.

2.7 THE CLAIM CONCERNING FAIR AND EQUITABLE TREATMENT

2.7.1 The Investor's Arguments

154. The Investor also claims that the Log Export Control Regime is in breach of the international law standard of treatment contained in Article 1105(1) as Canada fails to provide fair and equitable treatment and full protection and security. Article 1105(1) provides as follows:

IV. OPERATIVE PART

[491] In the light of the above considerations the Tribunal **ORDERS** and **AWARDS** as follows:

1. The claim is dismissed.
2. The parties shall bear the costs of the Arbitration in equal shares and any remaining balance will be refunded to the parties equally by the administering institution.
3. Pursuant to Article 40(3) of the UNCITRAL Arbitration Rules, the Tribunal fixes the following amounts as costs of the arbitration:

    Administering institution charges and expenses: US$ 138,595.25

    Tribunal's fees and expenses: US$ 820,904.75

        Professor Orrego Vicuña's fees: US$ 365,200.00

        Professor Dam's fees: US$ 169,675.00

        Mr. Rowley's fees: US$ 235,895.00

        Tribunal's expenses: US$ 50,134.75

    Total costs of the arbitration: US$ 959,500.00

Place of Arbitration: Washington D. C., United States of America.

Date of the Award: March 31, 2010.