

International Centre for Settlement of Investment Disputes

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July 28, 1999

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Re: Metalclad Corporation v. United Mexican States (ICSID
Case No. ARB(AF)/97/1).

Dear Members of the Tribunal,

Please find attached copies of the Submission of the Government of Canada under Article 1128 of the NAFTA, which we have received today under cover of the attached letter of July 28, 1999, from Mr. Joseph de Pencier.

Sincerely yours,


Alejandro A. Escobar
Secretary of the Tribunal

Attachments

cc (with attachments):
United Mexican States
c/o Mr. Hugo Perezcano Diaz

cc (without attachments):
Mr. Joseph de Pencier

Metalclad Corporation
c/o Mr. Clyde C. Pearce

INTERNATIONAL TRADE LAW DIVISION
NOV 1999 11:30 AM

Metalclad Corporation v. The United Mexican States

(ICSID Case No. ARB(AF)/97/1)

Submission of the Government of Canada

1. Pursuant to NAFTA Article 1128, the Government of Canada ("Canada") makes this submission to address a question of interpretation of NAFTA Article 1110 ("Expropriation and Compensation") raised by the Claimant Metalclad Corporation ("Metalclad").
2. Canada disagrees with Metalclad's approach to the basic interpretation of that provision.
3. Metalclad's argument claiming a breach of NAFTA 1110 begins at paragraph 237 of its Memorial. In paragraph 238, it argues:

"In Mexico's negotiation of an increased opportunity for foreign investment, she accepted the codification of the U.S. position on expropriation and compensation."

4. Metalclad elaborates this position in its Reply Memorial. In paragraph 431 of that document, Metalclad describes "the rudiments of expropriation law" with reference to a single source: American Iran-U.S. Claims Tribunal Judge George Aldrich, *The Jurisprudence of the Iran-United States Claims Tribunal*. A number of fourteen "rules" according to Judge Aldrich are recited. Although other sources are cited in the ensuing pages of argument, Metalclad places primary reliance on this one source.
5. Canada submits that both bases of Metalclad's interpretation are faulty.
6. In response to the argument that NAFTA Article 1110 is merely a codification of a U.S. position, Canada says that NAFTA Article 1110 represents a trilaterally-agreed obligation of three sovereign countries, and not the imposition by one of them of its legal norms on the other two. The fundamental term is "expropriation", and not, for example, the constitutional language of the United States.¹ Had the negotiators intended that this NAFTA obligation be merely a recapitulation of the substantive law of one of the Parties, they would have so indicated.
7. In response to the application of the jurisprudence of the Iran-U.S. Claims Tribunal, and one view of it at that, Canada says that the application by a NAFTA Chapter Eleven

¹Neither the wording of the Fifth Amendment ("nor shall private property be taken for public use,"), nor of the Fourteenth Amendment ("...nor shall any State deprive any person of...property,"), uses the term "expropriation".

Tribunal of the jurisprudence of the Iran-U.S. Claims Tribunal must be made with caution. NAFTA Article 1110 authorises a Chapter Eleven Tribunal to consider claims for expropriation. The Iran-U.S. Claims Tribunal had a wider authority: to decide claims that arose "out of debts, contracts ... expropriation or other measures affecting property rights". (emphasis added)²

8. The need for caution in relying on the jurisprudence of the Iran-U.S. Claims Tribunal is summarised by M. Somarajah:

"The awards of the Iran-US Claims tribunal have been a fruitful recent source for the identification of such takings ["indirect takings", or "disguised" or "creeping expropriation"]. But the Iran-US Claims Tribunal dealt with takings that took place in the context of a revolutionary upheaval and the propositions the tribunal formulated may not have relevance outside the context of the events that attended the Iranian upheaval following the overthrow of the Shah of Iran. Also, one has to be cautious in the making of any generalisation on the basis of dicta in the awards of this tribunal as its constituent documents gave the tribunal power to deal not only with direct takings of physical assets but "all measures affecting property rights". It is clear that such a wide definition of taking will not be acceptable in international law for the simple reason that many normal activities of states, such as taxation, affect property rights and cannot be expected to give rise to international concern." (footnotes omitted)³

9. Similar concern is expressed by A. Mouri, reflecting on decisions that ignored the relatively settled requirements in international law of "expropriation" of property and that applied as its synonym the more elastic and less well-settled concept of "deprivation" of property:

"The first question to be addressed is whether the term *expropriation* is synonymous with the term *deprivation*, the latter being used when one looks at the issue from the perspective of the owner of the property. Although the term "expropriation" has a relatively more settled and established meaning in this field of law, in comparison with the portions of Article II of the CSD [Claims Settlement Declaration, which authorised the Iran-U.S. Claims Tribunal] that speak about "measures affecting property rights", the concept and definition of "expropriation" often seemed to be confused. In many awards and opinions [of the Iran-U.S. Claims Tribunal] on the subject, the term "expropriation" has been mistakenly interchanged with the concept of "deprivation". The confusion is not caused because of the ambiguity of the word but, if not due to laxity, because some

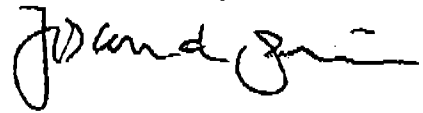
²As cited in Allahyar Mouri, *The International Law of Expropriation as Reflected in the Work of the Iran-U.S. Claims Tribunal*, (1994), at 34.

³*The International Law on Foreign Investment*, (1994), at 282-3.

arbitrators seem to be influenced by some recent writings which favour replacing the term expropriation with "deprivation", because to them it is the loss to the aggrieved, and not the gain of the government, which matters. To them this would avoid concern as to the Government ownership or the passage or distribution of the title.

...
"Yet some awards deliberately confused these terms. These awards seem to be labouring under the misperception that they have a free choice to prefer the term "deprivation", admitted to have a particular and different connotation, over another term, "expropriation", which is specifically used in Article II (1) of the CSD and carries with it all its legal consequences." (footnotes omitted)⁴

Respectfully Submitted



Joseph de Pencier
Counsel for the Government of Canada
July 28, 1999


⁴*The International Law of Expropriation as Reflected in the Work of the Iran-U.S. Claims Tribunal*, (1994), at 65-66.

THE
INTERNATIONAL
LAW ON FOREIGN
INVESTMENT

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INTERNATIONAL LAW ON FOREIGN INVESTMENT

the destruction of the rights of ownership of the foreign investors in the industry. Nationalisation involves such takings and they constitute the paradigm for the discussion of the law on nationalisation. There have been unsuccessful efforts to confine the definition of nationalisation and the effects of such nationalisation in international to such takings alone.⁹

Though it is clear that there are categories of takings outside the outright acts of nationalisation, the problem lies in formulating a single general principle that identifies all these takings. If one general criteria is to be attempted, it will have to involve some broad notion of governmental interference with the peaceful enjoyment of the rights of use, enjoyment and control of the property by the alien. But it is clear that not all such interferences amount to taking which attracts the concern of international law. The lesser types of taking have been identified as "disguised expropriation"¹⁰ or as "creeping expropriation".¹¹ Such descriptions, while providing a label for takings outside the obvious situation of direct takings of physical property, do little to further the identification of indirect takings which will attract the application of international law on nationalisation. The best approach to discussion is to group the types of indirect takings that have been discussed in the literature and the arbitral awards that have dealt with the question. The awards of the Iran-US Claims tribunal have been a fruitful recent source for the identification of such takings.¹² But the Iran-US Claims Tribunal dealt with takings that took place in the context of a revolutionary upheaval and the propositions the tribunal formulated may not have relevance outside the context of the events that attended the Iranian upheaval following the overthrow of the Shah of Iran. Also, one has to be cautious in the making of any generalisations on the basis of dicta in the awards of this tribunal as its constituent documents gave the tribunal power to deal not only with direct takings of physical assets

⁹ Iranian arbitrators in some early disputes before the Iran-US Claims Tribunal sought to narrow the definition of nationalisation to outright takings accomplished by legislation.

¹⁰ Judge Fitzmaurice in *Beverton Traction Case* [1971] ICJ Rpt 1.

¹¹ For example, B. H. Weston, "Constructive Takings under International Law" (1975) 16 *Virginia JIL* 103.

¹² For discussions, see R. Khan, *The Iran-United States Claims Tribunal: Controversies, Cases and Contributions* (1990) pp. 179-202; W. D. Mapp, *The Iran-United States Claims Tribunal, 1981-1987: An Assessment of the Tribunal's Jurisprudence and its Contribution to International Arbitration* (Unpublished PhD thesis, University of Cambridge, 1988).

TAKING OF FOREIGN PROPERTY

but "all measures affecting property rights".¹³ It is clear that such a wide definition of taking will not be acceptable in international law for the simple reason that many normal activities of states, such as taxation, affect property rights and cannot be expected to give rise to international concern.

The increase in concern with "creeping expropriation" in modern literature and arbitral awards is that a state could diminish property rights sometimes without affecting direct ownership of the investment. Thus, where the management of a company is taken over, the company, its assets and shareholdings are not affected but the foreign investors' interests are diminished. With the increase of regulatory control over foreign investments, there has been an increase in the use of such techniques of interference with the rights of the foreign investor. The response has been to create a category of "creeping expropriations" which are to be subject to the same rules as for direct expropriations.¹⁴

Leaving aside direct takings, it is clear that there could be other instances of interferences with property rights which could amount to takings of the property of the alien which could involve the host state in responsibility. The problem arises simply because it is conceded that there is another category of interference, such as taxation, export controls, and the requisitioning of a failing company, which does not amount to takings engaging the responsibility of the state. The latter types of takings, which are frequently practised in the developed states because of the greater regulatory control that is present through anti-trust, consumer protection, securities, environmental protection, land planning and other legislation, are non-compensable takings. These regulatory takings are regarded as essential to the efficient functioning of the state. The problem is to find a rational basis for the distinction. It is easier to identify the types of takings that have been regarded as compensable takings than to devise a criterion for such identification.

The types of takings, other than the obvious situation of a direct taking of physical assets, that could amount to nationalisations attracting the concern of international law, have been identified in literature

¹³ Article 2(1) of the Claims Settlement Declaration (19 January 1981).

¹⁴ In *Biloune v. Ghana Investment Centre* (1990) para. 75, the tribunal said that no distinction should be drawn between direct and creeping expropriations.

The International Law of Expropriation
as Reflected in the Work
of the Iran-U.S. Claims Tribunal

by

Allahyar Mouri

Iran-U.S. Claims Tribunal

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BOOK ONE

What Constitutes Expropriation or Measures Affecting Property Rights

As stated earlier (Section C, *supra*), the Iran-United States Claims Tribunal derives its subject-matter jurisdiction from the provisions of Article II of the CSD, the applicable *lex specialis*. Accordingly, most of the decisions of the Tribunal must be evaluated and weighed with particular reference to the provisions of the Algiers Declarations.

To the extent relevant to this Chapter, Article II provides that the Tribunal has jurisdiction to decide claims and counterclaims which:

1. ... arise out of debts, contracts ... expropriation or other measures affecting property rights, excluding claims described in Paragraph 11 of the Declaration of the Government of Algeria of January 19, 1981, and claims arising out of the actions of the United States in response to the conduct described in such paragraph ... ¹⁰⁴

2. The Tribunal shall also have jurisdiction over official claims of the United States and Iran against each other arising out of contractual arrangements between them for the purchase and sale of goods and services.

By this Article, the Tribunal is empowered to entertain and decide a variety of claims. The Tribunal's jurisdiction extends to claims of "expropriation", a term relatively settled in the field of international law, as well as "other measures affecting property rights" which has proved to be subject to great debates.

Given the way that subject-matter jurisdiction in the above-cited paragraphs of Article II is stipulated, the Tribunal must resolve a number of

¹⁰⁴ *Op cit.*, fn. 15.

CHAPTER II

What Constitutes Expropriation

II.A) Definition

The first question to be addressed is whether the term *expropriation* is synonymous with the term *deprivation*, the latter being used when one looks at the issue from the perspective of the owner of the property. Although the term "expropriation" has a relatively more settled and established meaning in this field of law, in comparison with the portions of Article II of the CSD that speak about "measures affecting property rights", the concept and definition of "expropriation" often seem to be confused. In many awards and opinions on the subject, the term "expropriation" has been mistakenly interchanged with the concept of "deprivation". The confusion is not caused because of the ambiguity of the word but, if not due to laxity, because some arbitrators seem to be influenced by some recent writings which favour replacing the term "expropriation" with "deprivation", because to them it is the loss to the aggrieved, and not the gain of the government, which matters.¹⁹⁷ To them this would avoid concern as to the Government

¹⁹⁷ See, e.g., Weston, "Constructive Taking Under International Law: A Modest Foray into the Problem of 'Creeping Expropriation'", 16 *V.J. Int'l L.*, (No. 4, Summer 1976), p. 22; Weigel and Weston, "Valuation upon the Deprivation of Foreign Enterprise: A Policy-Oriented Approach to the Problem of Compensation Under International Law", in Lulich (editor), *Valuation Of Nationalized Property*, p. 3; and Soldi-Hohevelde, "Semantics of Wealth Deprivation and Their Legal Significance", in D. Dicko (editor) *2 Foreign Investment in the Present and a New International Economic Order* (1987), 218. It is worth noting that none of the United Nations General Assembly Resolutions on the issue, neither the 1962 Resolution No. 1803 (XVII) on the Permanent Sovereignty over Natural Resources (17 UN GAOR Supp., No. 17, at 15, UN Doc. A/5217, reprinted in 2 *ILM* 223, 1963) nor the 1963 I. Brownlie, *Basic Documents in International Law*, 3rd ed. p. 230), which is unanimously considered to represent the *opinio juris*, nor any other Resolutions adopted after that, preferred the term "deprivation" over the term "expropriation" or equated "deprivation" to "expropriation". Instead they consistently define the latter as being assimilated to "nationalization", "requisitioning" or "transfer of private (continued...)"

ownership or the passage or distribution of the title.

The synonymy of the terms "expropriation" and "taking", and their distinction from "deprivation", appears to have been understood in a number of awards and separate opinions. As put by Judge Brower, an arbitrator appointed by the Government of the United States, the term "expropriation" ordinarily implies:

that the State involved has itself acquired the benefit of the affected alien's property or at least has been the instrument of its redistribution.¹⁹⁸

Yet some awards deliberately confused these terms. These awards seem to be labouring under the misperception that they have a free choice to prefer the term "deprivation", admitted to have a particular and different connotation, over another term, "expropriation", which is specifically used in Article II (1) of the CSD and carries with it all its legal consequences.

The award in *TAMS-AFFA*, often referred to in other awards and opinions as a settled and "eloquent"¹⁹⁹ precedent, recognized the distinction and yet stated that it:

prefers the term "deprivation" to the term "taking", although they are largely synonymous, because the latter may be understood to imply that

¹⁹⁷(...continued)

property" (See, e.g., U.N. Resolutions: No. 1803 (XVII); No. 3171 (XXVIII) Permanent Sovereignty Over Resources, reprinted in 19 ILM (1974), p. 238; No. 3201 (S-VI) Declaration on the Establishment of a New International Economic Order, S-6 UN GAOR Supp. (No. 1) at 3, UN Doc. A/9559 (1974); and No. 3281 (XXIX), Charter of Economic Rights and Duties of States, 29 UN GAOR Supp., No. 31, at 50, UN Doc. A/9631, reprinted in 14 ILM 251, 1975.)

¹⁹⁸ *Eastman Kodak Company*, *op cit*, fn. 167, Concurring and Dissenting Opinion of Judge Brower, 173, 181. See, also, *Starrett Housing Corporation*, *op cit*, fn. 31; Concurring Opinion of Judge Holtzmann, p. 162 and footnote 1; and Higgins, *op cit*, fn. 3, p. 322.

¹⁹⁹ *Motorola, Inc. and Iran National Airlines Corporation, et al.*, Award No. 374-481-3, Dissenting Opinion of Judge Brower, reprinted in 19 Iran-U.S. CTR, 93,95.