

**IN THE MATTER OF AN ARBITRATION UNDER CHAPTER ELEVEN OF  
THE NORTH AMERICAN FREE TRADE AGREEMENT  
AND THE UNCITRAL ARBITRATION RULES**

**BETWEEN:**

**MERRILL & RING FORESTRY L.P.**

**Claimant/Investor**

**AND:**

**GOVERNMENT OF CANADA**

**Respondent/Party**

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**GOVERNMENT OF CANADA**

**REJOINDER MEMORIAL**

**March 27, 2009**

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Departments of Justice and of  
Foreign Affairs and  
International Trade  
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CANADA

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## **I. INTRODUCTION**

### **A. Overview of the Case**

1. In the present arbitration proceedings, Merrill & Ring Forestry L.P. (the “Investor”) challenges the federal Log Export Control Regime (the “Regime”) which has been in place in British Columbia (“B.C.”) in one form or another for decades. Notwithstanding the fact that the Investor has operated profitably under the Regime for years, it now attempts to convince this Tribunal that the Regime is in violation of NAFTA Chapter 11. Yet, even if the Tribunal accepts all the factual allegations made by the Investor, they are not capable of constituting a breach of any of the obligations set out in NAFTA Chapter 11.

2. In order to escape this reality, the Investor is left with no option but to grossly alter the meaning of the NAFTA provisions it invokes. For example:

- The Investor turns the national treatment provision into a blanket protection for foreign investors from “measures that have almost any sort of negative impact on them.”<sup>1</sup> This is obviously not what Article 1102 stands for. Article 1102 protects foreign investors from nationality-based discrimination.
- The Investor transforms the nature of the treatment owed to foreign investments under Article 1105 into a protection against measures the Investor feels are

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<sup>1</sup> *Investor’s Reply*, ¶ 189.

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unreasonable.<sup>2</sup> This allows the Investor to raise a number of trivial allegations regarding the application of the Regime. However, one cannot establish a breach of Article 1105 merely by showing that an act is “unreasonable.” It requires a demonstration that the alleged measures violate the high threshold of the minimum standard of treatment under customary international law.

- The Investor interprets Article 1106 as if the term “requirement” did not exist. None of the allegations made by the Investor come close to being a requirement imposed by Canada that fits within the list of prohibited performance requirements.
- The Investor alleges that its investment has been expropriated notwithstanding the fact that it remains in control of its lands and logs in British Columbia and continues to operate profitably. In fact, the only “investment” it now alleges has been expropriated is its “interest” in realizing fair value for its logs on international markets. Such “interests” are not investments protected by NAFTA Chapter 11.

3. Not only are the Investor’s allegations not capable of constituting breaches of NAFTA Chapter 11, but the claim should also be dismissed at the outset because it is time-barred. In this Rejoinder, Canada will demonstrate that the Investor’s failure to bring its claim until 2006, despite having operated under the Regime for nearly ten years, is *fatal*.

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<sup>2</sup> The Investor alleges that “[w]here there is no reasonable relationship between Canada’s actions and a rational policy, it fails to act reasonably, thereby violating its duty to provide ‘fair and equitable treatment’” under Article 1105 (*Investor’s Reply*, ¶ 343).



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4. The language of Article 1116(2) is straightforward and its aim is clear. It bars claims submitted more than *three years* after an investor *first* acquired knowledge of breach and loss. Canada received the Investor's Notice of Arbitration on December 27, 2006. As a result, Merrill & Ring's claim is time-barred if it acquired actual or constructive knowledge of the alleged breaches and loss before December 27, 2003. Canada has shown that Merrill & Ring had actual knowledge of the alleged breaches and loss arising from the Regime throughout the decade before it commenced this arbitration and, in any event, well before 2003.

5. The Investor does not contest these facts. Instead, it puts forward an interpretation of Article 1116(2) intended to circumvent them. However, its interpretation is unsustainable. The Investor argues that the Regime constitutes a "continuing breach" of NAFTA and that each and every single routine application of the Regime constitutes *in itself* a separate "non-continuing" measure in breach of the Treaty. This is nonsensical. Every routine application of a continuing measure cannot also constitute a new and separate non-continuing measure which may be challenge independently: that would render the time bar provision meaningless.

6. Moreover, under the Investor's interpretation, an investor would have "first" knowledge of a measure *every time* it is routinely applied. Since the Investor alleges that it suffers a "new" damage "every day" that the Regime has been in place since 1998,<sup>3</sup> presumably it "first" acquired knowledge of such damage more than three thousand

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<sup>3</sup> For instance, the Investor mentions one such "non-continuing measure" as "each time" that it "was required to subject its federal logs to the Federal Surplus Testing Procedure and sell those logs on the B.C. market" (*Investor's Reply*, ¶ 98). The Investor also mentions that the alleged illegal "log industry-style blackmail, secret decisions [and] avoiding written communication" are all "part of the *daily* business environment in which Merrill & Ring is forced to operate" under the Regime (*Investor's Reply*, ¶ 2, emphasis added).

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times! Such a construction is both absurd and patently incompatible with the plain meaning of Article 1116(2). It also flies in the face of the ordinary meaning of the word “first.”

7. The Investor’s interpretation would render the time bar totally ineffective. An investor might challenge “continuing” measures several years or even decades after they were first adopted. It would mean that any claim involving the application of a regulatory measure could *never* be time-barred. This was clearly not the NAFTA Parties’ intention.

8. Canada therefore submits that the Tribunal should reject Merrill & Ring’s claim in its entirety as it is time-barred under Article 1116(2). Canada will also show that the Investor has failed to provide any evidence that establishes a breach of NAFTA Chapter 11.

9. On the merits, the Investor alleges that the Regime breaches four provisions of the NAFTA, resulting in damages. Canada demonstrated in its Counter-Memorial that all four alleged breaches are groundless and that it is in full compliance with its NAFTA obligations. In this Rejoinder, Canada will respond to the various new allegations and legal theories advanced by the Investor.

10. Merrill & Ring alleges that *Notice 102* violates the national treatment standard of Article 1102. To establish a breach of Article 1102, Merrill & Ring must compare the treatment it receives under the Regime with the treatment accorded to domestic Canadian investors that are “in like circumstances.” In the present case, there are *identical* domestic comparators. Therefore, Merrill & Ring must compare the treatment it receives with that of Canadian log companies operating *in B.C.* who are also seeking to export timber harvested from their *federal* land. For the small portion of the Investor’s business where it operates on *provincial* land in B.C., it must compare the treatment it receives with that of Canadian companies also operating in B.C. on *provincial* land.

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11. There is no discrimination between foreign and Canadian companies under the federal or provincial regimes. To make its case, the Investor must ignore all the Canadian investors operating in circumstances identical to its own. These domestic companies receive the exact same treatment as the Investor.

12. The Investor suggests that all that is required to establish a breach of Article 1102 is to show that it receives treatment less favourable than that afforded by *any jurisdiction* in Canada, to *any other log producer*, provided they compete with the Investor. These comparisons are improper because they compare treatment accorded to log producers by *different* jurisdictions and in *different* circumstances. For instance, the Investor compares the treatment it receives on its *federal* land to the treatment of log producers on *provincial* land in British Columbia. Merrill & Ring also compares itself with log producers doing business in another province, Alberta, where the Regime does not apply and where different conditions exist. Finally, with respect to certain allegations the Investor compares itself to companies operating in the B.C. Interior, but once again, the comparison is inapposite with respect to the treatment at issue.

13. Moreover, the Investor picks and chooses elements from the federal and provincial regimes that it prefers, ignoring the application of these regimes as a whole. The Investor's "à-la-carte" approach would result in according the Investor "better" treatment than that accorded to Canadian investors. This is not consistent with the purpose of Article 1102, which is to protect foreign investors against nationality-based discrimination.

14. Merrill & Ring also claims that the Regime violates Article 1105. Under Article 1105, the Investor must prove that Canada breached a rule of customary international law that is recognized as part of the international minimum standard for the treatment of aliens. To avoid this, the Investor contends that the 2001 FTC Interpretative Note is not binding. The Investor's purpose is to convince the Tribunal to apply the stand-alone fair

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and equitable standard developed by arbitral tribunals *outside* the context of NAFTA Chapter 11, rather than the standard set out in Article 1105. However, the decisions of arbitral tribunals convened under other treaties are irrelevant in the context of NAFTA proceedings.

15. The Investor seeks to lower the applicable standard because none of the trivial irritants it complains of reach the high threshold for a breach of the customary international law minimum standard of treatment of aliens. The Regime is transparent, based on clear and well understood rules, and does not create an insecure legal and business environment. The Investor's allegations of so-called "blockmailing" are largely unsubstantiated and the Investor has failed to demonstrate that Canada's response to improper actions of private companies is inadequate.

16. In addition, Merrill & Ring contends that Canada has imposed "performance requirements" in violation of Article 1106. However, the Regime does not impose any requirement to achieve a given level of export, to accord a preference to goods produced in Canada, or to purchase services from persons in Canada. Further, it does not impose any restriction on the Investor's sale of goods in Canada. What the Investor complains of are incidental effects of the Regime, not requirements that, in any event, do not fall within any of the listed prohibited measures under Article 1106.

17. Finally, the Investor claims that it has been the victim of unlawful expropriation. Canada has already established in its Counter-Memorial that the Regime has not expropriated Merrill & Ring's investment. Merrill & Ring continues to harvest logs on its lands in British Columbia. It has maintained control of its investment at all times while earning substantial profit and exporting almost all of the logs it sought to export.

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The Investor now claims that the only investment at issue here is its “interest to realize fair market value for its logs on the international market.”<sup>4</sup> Such an “interest” is not an investment protected by Chapter 11 and therefore not capable of being expropriated.

18. In its Counter-Memorial, Canada argued that the Investor’s damages claim was unsupported, riddled with methodological errors, faulty assumptions, and that it failed to establish that any alleged losses were caused by Canada’s Regime. The Investor has conceded to Canada’s criticisms by withdrawing its original damages claim.<sup>5</sup> Instead, the Investor’s Reply advances a new damages claim based on entirely new evidence and new expert reports: the Witness Statement of Douglas A. Ruffle (the “*Ruffle Report*”) and the Expert Witness Report of Robert Low of Deloitte (the “*Deloitte Report*”).

19. The new damages claim advanced by the Investor still fails to establish any loss caused by the Regime. The claim is fundamentally flawed, in particular because it fails to establish any causal link between the different allegations of breach of NAFTA obligations and the alleged damages. It is premised on a single “but for” scenario, notwithstanding that the violations relate to many different aspects of the Regime. In addition, the Investor’s “but for” scenario is Utopian. It assumes that the Investor alone is no longer subject to the application of the Regime, while other private landowners in B.C. (*i.e.* its competitors) remain subject to it. In addition, the Investor fails to establish that the costs of compliance and lost alleged “export premium” it claims result from the Regime.

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<sup>4</sup> *Investor’s Reply*, ¶ 22.

<sup>5</sup> The supportive PriceWaterhouseCooper’s Report by Mr. Sandy (the “*PwC Report*”) and the Mason, Bruce & Girard Report by Messers Cox and Rasmussen (the “*MBG Report*”).

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20. The Investor's damages calculations are also incorrect. The Investor and its new experts improperly select the data on which their calculations are based which leads to a grossly exaggerated quantification of loss. In particular, the Investor makes significant errors in its identification of a "Best Market Price" which it describes as the price it would have obtained had it been able to freely export its logs. While the Investor presents these prices as sale prices [REDACTED] many of these so-called "Best Market Prices" are actually prices *the Investor itself* achieved while operating under the Regime. Not only is the Investor's calculation of its alleged lost "export premiums" based on incorrect data, but it also fails to take into account other factors that may account for any higher prices in export sale prices.

21. As Canada's experts demonstrate, a correct analysis of the Investor's claims results in nominal loss, if at all. In short, the Investor has neither proved it suffered a loss nor that such loss was caused by the Regime. Therefore, it has failed to make out its damages claim.

22. For all these reasons, Canada respectfully submits that Merrill & Ring's claim should be dismissed, with costs.

**B. Material Submitted by Canada**

23. Canada's Rejoinder is accompanied by a compilation of relevant legal authorities. As well, Canada submits the following affidavits in support of its Rejoinder:

- KORECKY SUPPLEMENTAL AFFIDAVIT: Judy Korecky is the Deputy Director of the Export Controls Division ("ECD") of the Department of Foreign Affairs and International Trade ("DFAIT") and the federal representative on the Federal Timber Export Advisory Committee

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(“FTEAC”). Her supplemental affidavit responds to various points raised by the Investor and Tony Kurucz, Richard Ringma, Paul Stutesman, and Dr. Christian Schadendorf in their respective reply statements.

- **COOK SUPPLEMENTAL AFFIDAVIT:** John Cook is the Export Policy Forester for the British Columbia Ministry of Forests and Range (“BCMof”) as well as the Secretary of the Timber Export Advisory Committee (“TEAC”) and FTEAC. He responds to various points raised by the Investor and Tony Kurucz, Richard Ringma, Paul Stutesman and Stuart Macpherson in their respective reply statements.
- **TAPP AFFIDAVIT:** Darren Tapp is the Senior Manager of the Forest Tenure and Fibre Management Section of Alberta Sustainable Resource Development. He oversees the authorization for transport of primary timber products from Alberta provincial public land to destinations outside of Alberta. He responds to points raised by the Investor and its witnesses Robert Boeh and Keith Branter concerning the destination markets of Alberta log exports, and Alberta’s uniform scaling requirements.
- **BUSTARD AFFIDAVIT:** Brian Bustard is the president of Vanlog Forestry Services, Ltd., a forest industry consulting company that specializes in log related issues in coastal British Columbia. He has many years experience working both for log producers and domestic sellers. His affidavit responds to the Investor’s allegations with respect to so-called “blockmail.”
- **REISMAN SUPPLEMENTAL OPINION:** Professor W. Michael Reisman, the Myres S. McDougal Professor of International Law at Yale University, responds to the Investor’s interpretation of the time bar in Article 1116(2) of NAFTA and to Professor Howse’s Report.

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- REISHUS SUPPLEMENTAL AFFIDAVIT: David Reishus, Ph.D, economist specialising in natural resource and international trade regulation, is Senior Vice President at Compass Lexecon. He explains the economics of the forestry sector in B.C. and Canada. He deconstructs the economic analysis underlying the Investor’s new damages claim.
- JENDRO SUPPLEMENTAL AFFIDAVIT: David Jendro, of Jendro and Hart LLC, comments on the *Deloitte* and *Ruffle Reports* submitted by the Investor. Mr. Jendro is an expert on log and timberland valuation. In particular, Mr. Jendro challenges the assumptions in the *Ruffle Report*, which are the foundation of Deloitte’s damage assessment relied upon by the Investor.
- BOWIE SUPPLEMENTAL REPORT: Michael D. Bowie of KPMG LLP demonstrates that the *Deloitte Report* significantly overstates the losses the Investor claims.



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## II. THE MERRILL & RING CLAIM IS TIME-BARRED

### A. Summary of Canada's Position

24. Article 1116(2) provides that a claim is time-barred if more than three years have elapsed since the Investor first acquired or should have first acquired knowledge of the alleged breach and resulting damage. Merrill & Ring concedes that it knew of the Regime more than three years before making its claim. The Investor also knew of the damages it allegedly incurred as a result of the Regime. In order to avoid these facts, the Investor argues that “[e]ach application of the various rules and policies of the Regime (i.e. the ‘continuing’ measures) to Merrill & Ring constitutes a separate ‘non-continuing’ measure in-and-of-itself.”<sup>6</sup>

25. The Tribunal should reject the theoretical construct advanced by the Investor because there is no basis in fact or in law for distinguishing between the measures and their routine and recurring application to Merrill & Ring. It is true that the application of a regulatory measure in a specific instance may constitute a separate “measure” which can be challenged as such. However, the Investor’s arguments clearly reveal that, in this case, the regulatory measures and their applications are really one and the same. Furthermore, the Investor’s assertion that the measures are *both* continuing and non-continuing is nonsensical. It cannot be that *every* routine application of a continuing measure *also* constitutes a new separate non-continuing measure which may be challenged independently. Such an interpretation would render the time bar in Article 1116(2) totally ineffective.

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<sup>6</sup> *Investor’s Reply*, ¶ 120.

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26. The other arguments advanced by the Investor are equally unsupported by the terms of Article 1116. Article 1116(2) is a provision which limits jurisdiction, not damages. Moreover, nothing in Article 1116(2) supports the argument that damages must be fully quantified before a claim can be made.

**B. The Investor’s Emphasis on the Definition of “Measure” Is Misplaced**

27. In its Reply, the Investor attempts to demonstrate that the term “measure” is defined broadly in NAFTA, and that a particular application of a regulatory regime can constitute a measure.<sup>7</sup> It relies on the Opinion of Professor Howse, largely based on WTO law, to argue that measures are more often challenged “as applied”, rather than on the basis that they are violations “as such” of the WTO agreements.<sup>8</sup>

28. This is not controversial. Canada does not dispute that a regulatory measure and the way in which it is applied can both give rise to breaches of NAFTA obligations.

29. The real issue here is that the Investor is not really challenging specific applications of the Regime. For example, the Tribunal has only to compare the Investor’s allegations regarding *Notice 102* in the Reply, under paragraph 91 (continuing measures) and paragraph 98 (non-continuing measures) to see that the only difference between the two sets of allegations is in the preface “each time ....” There is *nothing* different in substance between the allegations. In fact, the Investor only complains *generally* about the Regime’s different requirements, relating to advertisement, surplus testing, cutting, sorting and scaling. The Tribunal is not presented with any evidence of individual NAFTA breaches; rather the Regime *itself* and its requirements are under attack. Nor are

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<sup>7</sup> *Investor’s Reply*, ¶¶ 66-82.

<sup>8</sup> See Expert Opinion of Robert Howse, ¶¶ 22-23.

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any of the damages claimed related to a particular application of the Regime. The Investor's claim is a systemic challenge to the Regime as a whole.

30. The Investor's approach (*i.e.* that the application of the Regime can be separated into "continuing" and "non-continuing" measures) is flawed not only in fact, but also in law. The following paragraph by the Investor reveals how artificial the legal distinction is:

It is precisely at this point where the concept of continuing breach dovetails with that of non-continuing breach. (...) And since the application of continuing measures in particular circumstances constitute separate "non-continuing" measures in-and-of-themselves, the clocks on both continuing and non-continuing measures start to run at exactly the same time. It is here where continuing breaches and non-continuing breaches elide one into the other and become, for all practical intents and purposes, indistinguishable.<sup>9</sup>

31. "Indistinguishable" is indeed the right word to qualify the continuing and non-continuing measures identified by the Investor as the basis for its claim. The Investor's attempt to repackage its claim to avoid the fact that it is time-barred should be rejected by the Tribunal.

**C. The Investor Disregards the Terms of Article 1116(2)**

32. The Investor's claim challenges regulatory measures routinely applied to it for over three years prior to the commencement of this arbitration. The issue in dispute is the proper application of the three year limitation of Article 1116(2) to these measures.

33. The starting point for the Tribunal's consideration of whether the Investor's claim is time-barred must be the terms of Article 1116(2), not, as the Investor and Professor

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<sup>9</sup> *Investor's Reply*, ¶ 119.

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Howse suggest, general international law or the WTO. In his Supplementary Opinion, Professor Reisman criticizes this disregard of proper treaty interpretation rules:

Hence, rather than begin, as one would expect, by quoting the language of Article 1116(2) and considering its ordinary meaning in context and in the light of the NAFTA's object and purpose, the Howse Opinion immediately turns to what it claims to be the "underlying principle" of VCLT Article 31(3) (c), which that subsection of the VCLT supposedly "Reflects," viz., "a broader principle of "systemic integration". This allows Professor Howse to disregard the *lex specialis* explicitly agreed by the Parties to the NAFTA and to attempt to bring in inapposite concepts from the World Trade Organization (WTO) jurisprudence and general rules of state responsibility.<sup>10</sup>

34. Canada's Counter-Memorial sets out the proper interpretation of the limitation provision in Article 1116(2) by applying the principles of the *Vienna Convention on the Law of Treaties* ("VCLT").<sup>11</sup> The jurisdictional provision in NAFTA Article 1116(2) is *lex specialis* that is clear on its face and does not contain any lacunae that require recourse to customary international law.

35. The language of Article 1116(2) establishes that the date on which the Investor "first acquired, or should have first acquired, knowledge of the alleged breach and

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<sup>10</sup> *Reisman's Supplementary Opinion*, ¶ 5. In its Reply, the Investor challenges "as a matter of form" the legal expert opinion of Professor Reisman. It argues that "[it] is highly improper to submit expert evidence about the governing law to a tribunal who must decide under that law" (*Investor's Reply*, ¶ 65). It is not uncommon for expert advice to be considered by international tribunals on applicable law, whether domestic or international. Many arbitral tribunals have accepted expert legal opinions submitted by the parties in relation to questions of international law. See for example: *CME Czech Republic B.V. v. Czech Republic* (UNCITRAL) Final Award, 14 March 2003 ("*CME - Final Award*") (Tab 26), expert opinions of Prof. Dr. Christoph Schreuer (referred to, *inter alia*, ¶¶ 84, 398) and August Reinisch (¶ 84)); *CMS Gas Transmission Company v. The Argentine Republic* (ICSID No. ARB/01/8) Final Award, 25 April 2005, ("*CMS Final Award*") (Tab 28), expert opinions of Dean Anne Marie Slaughter and Professor José Alvarez, at ¶ 334 onwards. There is nothing improper about this practice. It is for the Tribunal to weigh the expert opinion offered and draw its own conclusions as to the proper interpretation of the law.

<sup>11</sup> *Canada's Counter-Memorial* ¶¶ 144-178; *Vienna Convention on the Law of Treaties*, 23 May 1969, Can. T.S. 1980 No. 37 ("VCLT") (Tab 155).

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knowledge that the investor has incurred loss or damage” is the relevant one for jurisdictional purposes. Of particular importance is the reference to the date on which the Investor “first acquired” knowledge of the breach and damages. The Investor fails in its Reply to explain how knowledge could be “first” acquired repeatedly in the case of non-continuing measures. Knowledge of a measure can only be “first” acquired *once*; not *every time* the measure is subsequently routinely applied.

36. In its submission pursuant to Article 1128, the United States summarized its position with respect to the application of Article 1116(2) to continuing measures as follows:

All claims under NAFTA Chapter Eleven must be brought within the three-year time limitations period set out in Article 1116(2) and Article 1117(2). Although a legally distinct injury can give rise to a separate limitations period under NAFTA Chapter Eleven, a continuing course of conduct does not renew the limitations period under Article 1116(2) or Article 1117(2).<sup>12</sup>

Thus, the United States’ interpretation of Article 1116(2) is consistent with Canada’s interpretation of the provision.

**D. The Investor’s Ability to Challenge Continuing Violations of Chapter 11 Is Limited by the Time Bar**

37. Canada submits that the NAFTA Parties anticipated claims for continuing violations.<sup>13</sup> They drafted the time bar in Article 1116(2) accordingly, starting the clock at the time when the investor “first acquired ... knowledge of the alleged breach...” Thus, contrary to what the Investor asserts, continuing violations do not escape the time

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<sup>12</sup> United States Article 1128 Submission, July 14, 2008, ¶ 2.

<sup>13</sup> *Canada’s Counter-Memorial*, ¶¶ 161-165.

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bar contained in the provision. An investor can still challenge a continuing measure, so long as it does so within the three year window provided by Article 1116(2).

38. The Investor attempts to use NAFTA reservations applicable through Article 1108 as evidence that the Parties knew how to shield continuing measures from certain claims under NAFTA Chapter 11. In particular it states: “This provides conclusive evidence that the drafters did not intend to nullify the principle of continuing breach in its entirety in the context of the NAFTA, but rather chose to manage that principle in particular contexts through the use of reservations.”<sup>14</sup> This argument, supported by the Opinion of Professor Howse, misunderstands the role of reservations as well as the role of the time bar provision and should be rejected.

39. When the NAFTA Parties agreed on Article 1108, they knew some of their existing laws and regulations might run afoul of NAFTA disciplines. They therefore provided for reservations to ensure that such existing measures (which would continue to be in place after the entry into force of NAFTA) could not be challenged for breaching specific obligations, including Articles 1102, 1103, 1106 and 1107.<sup>15</sup> Article 1108 deals with existing non-conforming measures; it has nothing to do with the period of time during which a “continuing” measure can be challenged by investors under Chapter 11.

40. Continuing measures were considered by the *Feldman* Tribunal in its Interim Decision (on which the Investor relies). The Tribunal considered the case of measures applied to an Investor continuously *before* and *after* NAFTA’s entry into force. Notably,

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<sup>14</sup> *Investor’s Reply*, ¶ 86.

<sup>15</sup> The same applied to the “continuation or prompt renewal of any non-conforming measure.” (NAFTA Article 1108(1)(b)). This would, for instance, cover a case where a law is abrogated and immediately replaced by a new one which contains certain similar provisions.

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the Tribunal limited itself to declaring that it would have jurisdiction for the “post-January 1, 1994” breaches, while not addressing the issue of time bar at all. *If it had*, the proper application of Article 1116(2) would have led to a three year time bar as of 1997. Contrary to the Investor’s suggestions, the analysis contained in the *Feldman* Award is consistent with Canada’s position.<sup>16</sup>

41. In the present case, the Tribunal could decide that Merrill & Ring’s claim was time-barred in 1997 (*i.e.* three years after NAFTA’s entry into force) since the Investor has been subject to the Regime, substantively unchanged, since 1986. Or, it could decide that the claim was time-barred in 2001 (three years after *Notice 102*’s entry into force) or at the latest in 2002 regarding the B.C. export procedures which came into force in 1999. The ultimate effect on the claim is nonetheless the same: it was already time-barred when the Investor brought the claim in 2006.

**E. NAFTA Case Law Does Not Support the Investor’s Theory of “Non-Continuing Measures”**

42. The awards in *Grand River*, *Feldman* and *Mondev* all support the position advanced by Canada. To allow the Investor to challenge continuing measures long past the three year time bar, by qualifying each routine application of the Regime as a “non-continuing” measure, would render the time bar meaningless. Canada has already explained why the *UPS* decision, the only case to support the Investor’s position, should not be followed by this Tribunal.<sup>17</sup> In its Reply, the Investor alleges that the *UPS*

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<sup>16</sup> See *Feldman v. Mexico* (ICSID No. ARB(AF)/99/1) Award, 16 December 2002 (“*Feldman – Award*”) ¶ 63 (Tab 49) referring to the “clear-cut period of three years” cited in *Canada’s Counter-Memorial* at ¶ 235.

<sup>17</sup> *Canada’s Counter-Memorial*, ¶¶ 242-252. Notably, the *UPS* Tribunal ignored the fact that this was a jurisdictional provision and failed to give proper consideration to the word “first” in Article 1116(2).

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Tribunal, by not referring to *Grand River*, “obviously chose to disregard that case.”<sup>18</sup> If anything, the fact that the *UPS* Tribunal did not even confront the thorough and highly relevant reasoning of the *Grand River* Tribunal undermines the *UPS* Tribunal’s decision.

43. In its Reply, the Investor attempts to distinguish the *Grand River* decision on the basis that, unlike the present case, the measures at issue did not involve administrative decisions pursuant to laws or regulations, but rather the laws and regulations themselves. However, it is precisely when the Tribunal considered the claimant’s arguments that the “limitations periods ... applied separately to *each* contested measure taken by *each* state implementing the MSA” that it concluded this argument would render the time bar in Article 1116(2) “ineffective.” This is because “a claimant would be free to base its claim on the most recent transgression, even if it had knowledge of earlier breaches and injuries.”<sup>19</sup> This statement is fully applicable here. Allowing the Investor to base its claim on the most recent application of the Regime would render Article 1116(2) ineffective.

**F. Article 1116(2) Is a Jurisdictional Provision Not a Provision Limiting Quantum of Damages**

44. The Investor suggests that the purpose of Article 1116(2) is to limit the liability of NAFTA Parties to “three years of damages”<sup>20</sup> before the submission of a claim to arbitration. Nothing in the wording or context of Article 1116(2) supports this interpretation.

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<sup>18</sup> *Investor’s Reply*, ¶ 114.

<sup>19</sup> *Grand River Enterprises Six Nations Ltd. v. United States* (UNCITRAL) Decision on Objections to Jurisdiction, 20 July 2006 (“*Grand River – Jurisdiction Decision*”) (Tab 57) ¶ 81, cited in *Canada’s Counter-Memorial* at ¶ 232.

<sup>20</sup> *Investor’s Reply*, ¶ 125.



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45. Moreover, the structure of Article 1116 indicates that both sub-paragraphs (1) and (2) are jurisdictional provisions. Article 1116(1) sets out the jurisdiction *rationae materiae* of Chapter 11 tribunals; in other words, the type of claims that a Tribunal can hear. Article 1116(2) sets out the jurisdiction *rationae temporis* of Chapter 11 tribunals by providing a clear time limitation for an investor to bring a claim.

46. The plain meaning of Article 1116(2) establishes that its purpose is to limit the right of an investor to bring a claim (“an investor may not make a claim if more than three years have elapsed...”), *not* to limit the extent of damages that can be claimed.

47. Reading Article 1116(2) as merely a limit on the time period for which damages can be claimed does not make “practical sense.”<sup>21</sup> Nor does it represent “a balanced approach to the limitation period envisaged by Article 1116(2),” as the Investor suggests.<sup>22</sup> The Investor ignores the text, context and purpose of the provision. Had the Parties intended to merely limit the time period for which damages could be claimed, they would have used explicit and specific language to do so.

**G. Actual Knowledge of Quantifiable Loss Is Not Required to Make a Claim under Article 1116(2)**

48. In its Reply, the Investor argues that, “[t]here was nothing clear and precise about the losses Merrill & Ring would suffer at the time the [sic] *Notice 102* and the *B.C. Export Procedures* were adopted. Such losses could only be quantified with any degree of predictability or precision at the time these measures were applied to Merrill & Ring in

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<sup>21</sup> *Investor's Reply*, ¶ 121.

<sup>22</sup> *Id.*, ¶ 121.

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specific instances.”<sup>23</sup> Merrill & Ring has operated under *Notice 102* since 1998 (and prior to that under the analogous *Notice 23*) and under the provincial regime since at least 1999. Given its long experience with such measures, it is implausible that Merrill & Ring could not determine what costs and losses it might suffer as a result of *Notice 102* shortly after its implementation. In fact, as Canada pointed out in its Counter-Memorial, Mr. Schaaf freely admits that Merrill & Ring knew exactly how much loss was incurred as a result of the Regime.<sup>24</sup>

49. It is one thing to argue that uncertainty existed when the Regime was adopted, but quite another to argue that after years of application, the Investor still did not know of the losses it had already allegedly incurred and was presumably incurring on a regular basis. It is particularly difficult to see how the Investor could not know of losses it incurred in the past, yet purport to quantify *future* losses in its damages claim with some certainty.

50. More generally, the Investor provides no authority to support its argument that “actual knowledge of quantifiable loss” is required prior to a claim being made.<sup>25</sup> This interpretation does violence to the text of Article 1116(2) and contradicts all other authorities on this point.<sup>26</sup>

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<sup>23</sup> *Id.*, ¶ 112.

<sup>24</sup> *Canada’s Counter-Memorial*, ¶ 199 (citing *Schaaf Affidavit* ¶ 32).

<sup>25</sup> *Investor’s Reply*, ¶ 118.

<sup>26</sup> See for example *Mondev International Ltd. v. United States* (ICSID No. ARB(AF)/99/2) Award, 11 October 2002 (“*Mondev – Award*”), ¶ 87 (Tab 87); *Grand River-Jurisdictional Decision* ¶ 78 (Tab 57).

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## **H. Conclusion**

51. Canada submits that the Tribunal should reject Merrill & Ring's claim as it relates to the Regime, which has been in place and routinely applied to the Investor for nearly a decade before it initiated its claim. As such, the claim is time-barred under Article 1116(2).

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### **III. THERE IS NO VIOLATION OF NAFTA ARTICLE 1102**

#### **A. Summary of Canada's Position**

52. The Investor's national treatment claims are not about differences in treatment between foreign and domestic investors. They are about regulatory differences in the federal and provincial regimes.

53. Article 1102 protects investors against nationality-based discrimination. The Investor's Reply reveals a continued misunderstanding of the purpose of the national treatment provision. Not only does the Investor fail to allege any nationality-based discrimination, but it fails to acknowledge that domestic investors are accorded the same treatment. Its own witness, Mr. Ringma of Island Timberlands, one of the Canadian log producers operating on federal land in B.C., admits they are receiving the same treatment as Merrill & Ring.

54. To support its claim, the Investor puts forward flawed interpretations of the terms "like circumstances" and "no less favourable treatment." As Canada will explain, each of the allegations of differential treatment made by the Investor in the Reply ignores Canadian investors in identical circumstances that receive identical treatment. Instead, the Investor chooses improper comparators. For example, it compares itself with domestic investors operating in different jurisdictions. Once the Tribunal properly applies Article 1102, it is clear that there is no violation of that provision.

#### **B. The Proper Meaning of Article 1102**

55. The Investor's national treatment theory can be summarized as follows:

- The Investor argues that in applying the national treatment test, the Tribunal need not first consider the treatment at issue as it makes "little

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practical sense”;<sup>27</sup>

- Instead, according to the Investor, the Tribunal must first determine whether the Investor and/or its investments are in like circumstances to certain domestic investors and/or their investments. This, the Investor suggests, can be answered simply by examining if investors compete in some fashion, without any consideration of the treatment at issue. According to the Investor, this interpretation is consistent with the interpretation of national treatment provisions in the WTO Agreements and should be applied in the NAFTA context on the basis of a so-called theory of “systemic integration”;
- Furthermore, the Investor argues, the Tribunal should not consider whether differences are based on legitimate public policy considerations rather than on nationality. In other words, the Investor takes the absurd position that *national treatment* has nothing to do with nationality-based discrimination; and
- Finally, the Investor advances an interpretation of “treatment no less favourable” that equates it with the best treatment provided to any investor in any jurisdiction. The Investor suggests that “no less favourable treatment” guarantees it equal competitive opportunities with other log producers. This leads it to adopt the extreme position that NAFTA 1102 is meant to “protect foreign investors from measures that have almost any sort of negative impact on them.”<sup>28</sup>

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<sup>27</sup> *Investor’s Reply*, ¶ 160.

<sup>28</sup> *Investor’s Reply*, ¶ 189.

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56. As Canada will explain, the Investor's approach is deeply flawed and does not withstand even a basic reality-check. The effect of the Investor's interpretation of national treatment would be to prevent governments from making almost any kind of regulation, given that regulations inevitably affect those that are subject to them differently. Governments could not adjust their policies to take into account different circumstances or legitimate policy objectives. Moreover, to comply with the Investor's national treatment test, all levels of government in Canada would have to adopt exactly the same regulations concerning products or enterprises that might potentially compete in the market-place.

57. Merrill & Ring would turn Article 1102 into an across-the-board protection for foreign investors from "measures that have almost any sort of negative impact on them."<sup>29</sup> The Tribunal should reject an approach that so evidently leads to such an absurd result. This is clearly not the intent of a national treatment provision. Article 1102 was intended to ensure that foreign investors did not receive less favourable treatment than domestic investors because of the fact that they are foreign.

**1. Article 1102 Protects Investors from Nationality-Based Discrimination**

58. Canada has explained that the purpose of Article 1102 is to protect investors from nationality-based discrimination. This has been consistently recognized by NAFTA Chapter 11 tribunals.<sup>30</sup> In its Reply, the Investor suggests that "Canada misconstrues the

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<sup>29</sup> *Id.*, ¶ 189.

<sup>30</sup> For example, see *Feldman – Award* ¶ 166 (Tab 49); *Loewen Group Inc. and Raymond L. Loewen v. United States* (ICSID No. ARB/98/3) Award on the Merits, 25 June 2003 ("*Loewen – Award on Merits*") ¶ 139 (Tab 73); *GAMI Investments Inc. v. Mexico* (UNCITRAL) Final Award, 15 November 2004 ("*GAMI – Award*") ¶¶ 111-115 (Tab 54); see also *Canada's Counter-Memorial* ¶ 343.

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jurisprudence on this matter” and that tribunals have found nationality-based discrimination to be only an “interpretative hurdle.”<sup>31</sup> To advance its case, the Investor then selectively quotes from the *Feldman* award. Canada reproduces the passage in full below.

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 *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, at 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.<sup>32</sup> (Emphasis in original text)

The *Feldman* Tribunal then went on to say:

However, in this case there is evidence of a nexus between the discrimination and the Claimant’s status as a foreign investor.<sup>33</sup>

59. It is evident from this passage that the Tribunal did not find that nationality-based discrimination was merely an “interpretative hurdle” as the Investor suggests. Rather, the Tribunal was addressing the burden of proof for establishing nationality-based discrimination.

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<sup>31</sup> *Investor’s Reply*, ¶ 207.

<sup>32</sup> *Feldman – Award*, ¶ 181 (Tab 49); the Investor omits the word “explicitly” which is emphasized in the original text thereby misrepresenting the Tribunal’s finding.

<sup>33</sup> *Id.*, ¶ 182.

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60. Canada's position is not, as the Investor suggests, that the Investor must prove a separate discriminatory intent. However, the Tribunal must still ascertain whether there is discrimination "by reason of nationality." As Canada has already explained, in the absence of clear evidence that a State discriminated against an investor because of its foreign nationality, a proper application of the "like circumstances" test will help distinguish between cases of legitimate government regulation of an industry and cases of nationality-based discrimination.<sup>34</sup> The fact that domestic investors in the same situation as the foreign investor receive the same treatment will be a strong indication that there is no nationality-based discrimination. In addition, the fact that there are legitimate public policy considerations explaining the differences in treatment between investors, will indicate there is no breach of national treatment. Comparing only the treatment accorded to investors that compete in the same market, as the Investor suggests, does not assist the Tribunal in determining whether there is nationality-based discrimination. Each of these points is addressed in turn below.

**a) Treatment Accorded to Domestic Investors in the Same Circumstances Is Relevant**

61. For the purpose of applying the national treatment test, the treatment accorded to domestic investors in the same situation as the Claimant is most relevant.<sup>35</sup> As the

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<sup>34</sup> *Canada's Counter-Memorial*, ¶¶ 298-310.

<sup>35</sup> *Id.*, ¶ 298; *Methanex Corp. v. United States* (UNCITRAL) Final Award of the Tribunal on Jurisdiction and the Merits, 3 August 2005 ("*Methanex - Award*"), Part IV-Chapter B, ¶¶ 17, 19 (Tab 85); *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc. v. Mexico* (ICSID Case No. ARB(AF)/04/5), Award, ¶ 202, ("*ADM - Award*") (Tab 165).



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*Methanex* Tribunal found, “it would be... perverse to ignore identical comparators if they [are] available and ... use comparators that [are] less ‘like’.”<sup>36</sup>

62. The Investor takes issue with this simple proposition on the basis that Canada’s approach amounts to requiring that foreign and domestic investors be “identical twins” before any comparison can be made. This misconstrues Canada’s position. Where identical comparators are available, the Tribunal must use them. Where no identical comparators exist it may be appropriate to look at less “like” comparators. The reference to “identical” does not mean domestic investors must be identical to foreign investors in every respect.

63. The comparison with domestic investors in identical situations, where such investors exist, is most likely to disclose whether there is any nationality-based discrimination. It is therefore the most logical starting point for the Article 1102 analysis. However, the Investor seeks to avoid a comparison to domestic investors in identical circumstances because this would defeat its case.

**b) Policy Considerations Underpinning Different Treatment of Investors Are Relevant to the “Like Circumstances” Determination**

64. In its Counter-Memorial, Canada pointed to the many NAFTA Chapter 11 tribunals that have taken policy considerations into account in determining whether alleged differences in treatment were a violation of national treatment.<sup>37</sup> Canada also explained that policy considerations are the basis for the differences in treatment raised

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<sup>36</sup> *Methanex - Award*, Part IV-Chapter B, ¶ 17.

<sup>37</sup> *Canada’s Counter-Memorial*, ¶¶ 303-309.

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by the Investor. For example, advertising requirements differ in remote areas from those on non-remote areas to ensure that the surplus test is not circumvented.<sup>38</sup> While the Investor recognizes in its Reply that tribunals have taken into account policy considerations in determining “like circumstances”, it submits, without providing any explanation, that these tribunals were wrong in doing so. This is simply not convincing.

65. The Investor advances another equally weak proposition: it suggests that taking policy considerations into account “would run counter to the objectives of the NAFTA itself.”<sup>39</sup> Not only is this proposition wholly unsupported, it is also plainly wrong.

66. The NAFTA Parties did not intend to abandon their ability to regulate by adopting NAFTA Article 1102. The Investor’s position that policy considerations are irrelevant to the Tribunal’s determination of what constitutes relevant “like circumstances” would leave no basis for tribunals to determine whether legitimate regulatory distinctions are at issue. This is why NAFTA Chapter 11 tribunals have taken into account policy considerations.

67. To support its position, the Investor suggests that accepting policy considerations would amount to creating a “self-judging” exception.<sup>40</sup> It also argues that, the Government cannot make any distinctions in its regulations that would differently affect companies in the forestry sector because Canada did not take a reservation in this sector.<sup>41</sup>

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<sup>38</sup> *Canada’s Counter-Memorial*, ¶ 373.

<sup>39</sup> *Investor’s Reply*, ¶190.

<sup>40</sup> *Id.*, ¶ 191.

<sup>41</sup> *Id.*, ¶ 188.

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68. The Investor confuses two concepts. Policy considerations may provide an explanation for differences in regulation that are *not based on nationality*. But policy considerations cannot provide an “exception” for *nationality-based* differences, unless a NAFTA Party took a reservation to Article 1102 in its list of Reservations. The examples cited by the Investor illustrate this confusion.<sup>42</sup> These examples are reservations that allow the government to discriminate on *the basis of nationality* in certain sectors (telecommunications, air services, etc.), for example by imposing limitations on foreign ownership.

69. Again, the effect of the Investor’s position would be to impose an undue limitation on a government’s ability to regulate. Only where reservations were taken could a government make regulations that affect industry participants differently, whether based on nationality or not. This is not the purpose of Article 1102.

**c) “Like Circumstances” Does Not Mean “in Competition”**

70. To support its allegation of differential treatment, the Investor argues that the “like circumstances” analysis of Article 1102 requires a comparison between investors in competition with one another.<sup>43</sup> According to the Investor, this interpretation of the term “like circumstances” in NAFTA Article 1102 is supported by the interpretation that WTO panels have given to the terms “like products” in the GATT and “like service providers” in the GATS. The Investor’s interpretative approach is premised on Prof. Howse’s bizarre theory of “systemic integration” that allows it to ignore the precise words of

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<sup>42</sup> The Investor cites Canada’s Reservations in telecommunications, government finance, minority affairs, social services, air transportation and water transportation (*Investor’s Reply*, ¶ 187).

<sup>43</sup> *Investor’s Memorial*, ¶¶ 289-290; *Investor’s Reply*, ¶¶ 163-173.

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Chapter 11 of NAFTA in favour of different terms used in national treatment obligations under different agreements.

71. In his Supplementary Opinion, Prof. Reisman takes issue with this flawed methodology:

... in the context of this arbitration, the real purpose of the “principle of ‘systemic integration’” is to liberate Professor Howse from the ordinary meaning of the specific provisions of NAFTA at issue in this dispute<sup>44</sup>

72. In its Counter-Memorial, Canada explained why GATT and GATS law should not apply to NAFTA Article 1102. Similar reasons were also clearly set out by the *Methanex* panel. In particular, the Tribunal observed that the NAFTA Parties were well aware of the textual differences between the terms “like goods” and “in like circumstances”:

[i]t is thus apparent from the text that the drafters of NAFTA were careful and precise about the inclusion and the location of the respective terms, “like goods”, “any like, directly competitive or substitutable goods, as the case may be”, and “like circumstances.” “Like goods” is never used with respect to the investment regime of Chapter 11 and “like circumstances”, which is all that is used in Article 1102 for investment, is used with respect to standards-related measures that might constitute technical barriers to trade only in relation to services; nowhere in NAFTA is it used in relation to goods.”<sup>45</sup>

Thus, Article 1102 should not be read as though it contained the words “any like, directly competitive or substitutable goods.”<sup>46</sup>

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<sup>44</sup> *Reisman Supplementary Opinion*, ¶ 9.

<sup>45</sup> *Methanex – Award*, Part IV-Chapter B, ¶ 33 (Tab 85).

<sup>46</sup> *Id.*, ¶ 37.

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73. The Investor attempts to minimize the *Methanex* Tribunal’s finding by arguing that it rejected the substitution of “any like, directly competitive or substitutable goods” simply because Article 1102 also applies to services.<sup>47</sup> However, the Tribunal’s critique goes deeper than that:

International law directs this Tribunal, first and foremost, to the text; here, the text and the drafters’ intentions, which it manifests, show that trade provisions were not to be transported to investment provisions. Accordingly, the Tribunal holds that Article 1102 is to be read on its own terms and not as if the words “any like, directly competitive or substitutable goods” appeared in it.<sup>48</sup>

74. The Investor has not advanced a single case in which a tribunal came to the conclusion that “in like circumstances” only means investors “in competition with one another.”<sup>49</sup> In their analysis of the term “like circumstances,” NAFTA Chapter 11 tribunals have considered the existence of a competitive relationship between two investors to be a relevant factor. But they have never confined their analysis to this one factor. As Canada has demonstrated, policy considerations have routinely been part of this analysis and as such this Tribunal must have the liberty to consider them.

75. In a final attempt to justify the use of WTO precedents to interpret Article 1102, the Investor repeatedly mentions that the NAFTA and the WTO were negotiated concurrently.<sup>50</sup> However, it fails to explain why provisions that use different wording and that appear in different contexts should be given an identical meaning. The Investor’s

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<sup>47</sup> *Investor’s Reply*, ¶ 143.

<sup>48</sup> *Methanex – Award*, Part IV-Chapter B, ¶ 37 (Tab 85).

<sup>49</sup> *Investor’s Reply*, ¶¶ 163-167. The Investor refers only to the dissenting opinion of Ronald Cass in *United Parcel Service v. Canada* (UNCITRAL), Award on Merits and Dissenting Opinion, 24 May 2007 (“*UPS – Award*”) (Tab 144).

<sup>50</sup> *Investor’s Reply*, for ex., ¶¶ 145-147, 155.

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reliance on the *Cross Border Trucking Case* is similarly flawed. The Tribunal in that case did not limit itself to determining whether Mexican trucking service providers competed with U.S. trucking service providers.<sup>51</sup>

76. In addition, the Investor's approach is flawed because it requires the Tribunal to consider "like circumstances" in isolation from the treatment at issue. Indeed, the Investor is arguing that whether investors are in competition should be determinative of like circumstances regardless of the treatment at issue (which the Investor suggests should not even be considered). In the present case, this would mean that the Regime would have to be designed according to whether log producers compete against one another, instead of being based on legitimate policy objectives. For example, the sorting requirements of the Regime could not be customized to reflect the different market practices existing in the B.C. Interior and on the B.C. Coast. This approach is contrary to the terms of Article 1102, which indicate that the determination of "like circumstances" is intimately related to the determination of the treatment at issue. The "like circumstances" analysis cannot proceed in a factual vacuum and independently from the treatment at issue, as the Investor suggests.

2. **"No Less Favourable Treatment" Does Not Mean Best Treatment**

77. The Investor claims "no less favourable treatment" is an obligation to provide the "best" treatment that *any investor* receives. The Investor makes this claim irrespective of the requirement that the comparison be made with investors "in like circumstances."

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<sup>51</sup> In addition, most of the reasoning in the case related to the interpretation of Article 1202 not Article 1102. The Investor mischaracterizes the position of the NAFTA Parties at ¶ 155 of the Award (*Re Cross Border Trucking Services (United States v. Mexico)* (2008), Mex-98-2008-01, (Ch. 20 Panel) in the Investor's Book of Authorities (Tab 34).

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This interpretation is contrary to the terms of Article 1102 and would lead to an absurd result: any differentiation between investors would constitute a breach of Article 1102. The Investor's interpretation is also contrary to the principle that terms of a treaty be interpreted according to their ordinary meaning, in their context.<sup>52</sup> Here, the terms "no less favourable treatment" must be read in the context of the other terms of NAFTA Article 1102, in particular, the terms "in like circumstances."

78. In another attempt to avoid the requirements of Article 1102, the Investor suggests that the term "no less favourable treatment" means equal competitive opportunity.<sup>53</sup> The Investor does not explain what implications would follow from such an interpretation or what this means in concrete terms. In any event, while equal competitive opportunities between domestic and foreign investors in like circumstances is one of the objectives of Article 1102, the requirement that Canada accord the Investor "no less favourable treatment in like circumstances" is not a guarantee that Merrill & Ring will never be inconvenienced by any government measure.

### 3. Treatment Accorded by Different Jurisdictions Cannot Be Compared

79. The Investor's case rests in large part on a comparison between treatment accorded by different jurisdictions. While there is no doubt that Article 1102 covers both federal and provincial measures, comparing measures adopted by different governments in Canada is entirely inappropriate to establish a national treatment violation.

80. Article 1102(3) contradicts the Investor's approach to national treatment. It reads:

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<sup>52</sup> VCLT, Article 31(1).

<sup>53</sup> *Investor's Reply*, ¶¶ 142, 172.

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...the treatment, accorded by a Party under paragraphs 1 and 2 means, with respect to a state or province, treatment no less favourable than the most favourable treatment accorded, in like circumstances, by *that* state or province to investors, and to investments of investors, of the Party of which it forms a part. (emphasis added)

81. The plain language of Article 1102(3) refers to treatment by “*that* state or province,” which indicates that the treatment cannot be compared to treatment accorded by another state or province. Thus, it is inappropriate to make a comparison, as the Investor does, between treatment accorded by the province of British Columbia and treatment accorded by the province of Alberta. The same is true with respect to comparing treatment accorded by the federal government and the province. All three NAFTA Parties are federations. To accept the Investor’s position would be to impose a requirement of uniformity and homogeneity that is fundamentally at odds with the very purpose of federalism. For example, it would require Vermont and Texas to have the same taxation regime because some of their investors compete against each other, or require that all states adopt corporate laws as friendly as those of Delaware.

82. Moreover, the Investor does not explain how comparing regulatory measures of different levels of government, or even regulatory measures of different sub-national governments, can reveal any nationality-based discrimination. It goes without saying that not all governments will have identical regulatory measures, yet it does not follow that there is necessarily a national treatment breach as a result.

**C. The Federal and Provincial Regimes Do Not Violate Article 1102**

83. In its Counter-Memorial Canada identified the factual inaccuracies upon which the Investor’s national treatment allegations were based. Canada also highlighted that domestic investors in the same situation, were receiving the same treatment as Merrill & Ring. Yet in its Reply, the Investor continues to ignore the fact that domestic federal and provincial log exporters in British Columbia receive the same treatment as Merrill &



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Ring on its federal and provincial lands respectively. Instead, the Investor identifies a number of different comparators that are not in like circumstances because they operate outside the province of B.C., in different regions of B.C., or under different jurisdictions in British Columbia.

84. In its Reply, the Investor alleges eight differences in treatment that result in a breach of Article 1102:

- a) Merrill & Ring is “forced” to observe the requirements of *Notice 102* while other log producers in B.C. and Alberta are not;<sup>54</sup>
- b) Merrill & Ring is “forced” to sell its logs domestically while log producers in Alberta are not;<sup>55</sup>
- c) Merrill & Ring is “forced” to sell its logs under “blockmail” while log producers in Alberta are not;<sup>56</sup>
- d) Merrill & Ring is “forced” to cut, sort, and scale its logs in a particular way while log producers in the B.C. Interior and Alberta are not;<sup>57</sup>
- e) Merrill & Ring is “forced” to observe the so-called “remoteness rule” while other log producers on the South B.C. Coast are not;<sup>58</sup>

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<sup>54</sup> *Investor’s Reply*, ¶¶ 243-244.

<sup>55</sup> *Id.*, ¶¶ 245-247.

<sup>56</sup> *Id.*, ¶¶ 248-250.

<sup>57</sup> *Id.*, ¶¶ 251-255.

<sup>58</sup> *Id.*, ¶¶ 256-262.

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- f) Merrill & Ring is “forbidden” from receiving standing exemptions while log producers on provincial lands are not;<sup>59</sup>
- g) Merrill & Ring is “forbidden” from advertising standing timber, while log producers in the B.C. Interior are not;<sup>60</sup> and
- h) Merrill & Ring is required to pay a fee-in-lieu to export its provincial logs, while federal log producers are not.<sup>61</sup>

85. In essence, the alleged differential treatment results from two measures: the federal Regime, more specifically *Notice 102*, and the provincial regime, more specifically the *B.C. Forest Act*. The allegations can be grouped into three types: (1) *Notice 102* accords different treatment depending on where logs are situated in B.C.; (2) The federal Regime (i.e. *Notice 102*) treats log producers in B.C. differently than the provincial regime; and (3) The federal and B.C. regimes treat B.C. log producers differently than the federal and Alberta governments treat Alberta log producers.

86. For the most part (and to the extent that these allegations can be understood), Merrill & Ring seems to be comparing treatment accorded by different jurisdictions instead of comparing treatment accorded to domestic and foreign investors. This is best illustrated by the fact that the Investor complains of differences between the federal and the provincial regimes in British Columbia, while the Investor itself operates both on federal and provincial land in British Columbia and is subject to both regimes. In some cases, the Investor argues that the provincial regime provides more favourable

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<sup>59</sup> *Investor's Reply*, ¶¶ 263-269.

<sup>60</sup> *Id.*, ¶¶ 270-273.

<sup>61</sup> *Id.*, ¶ 274.

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treatment<sup>62</sup>, while in other cases it claims that the federal Regime is more advantageous.<sup>63</sup> Clearly, the issue is not a difference between treatment of domestic and foreign investors. Consequently, the Investor's complaint is outside the scope of Article 1102.

87. Moreover, the Investor's attempt at singling out and comparing different elements of the federal and provincial regimes is fundamentally flawed. In practice, no domestic investor receives the treatment the Investor seeks to obtain. For instance, domestic investors on provincial lands in B.C. are subject to the provincial regime as a whole, including the fee-in-lieu of manufacture. Domestic investors on federal land in B.C. are subject to the federal Regime and are not allowed to invoke elements of the provincial regime that they would prefer.

88. It seems that the Investor would like to operate in B.C. but not be subject to federal or provincial regime that applies to B.C. producers. Similarly, it invokes certain aspects of Alberta regulations that it deems more favourable, again without considering the regulations as a whole. What the Investor is seeking is an "à la carte" regulatory regime where it can pick elements that it prefers from any jurisdiction in Canada, regardless of where it actually operates. The Tribunal must reject this approach as it would amount to providing the Investor with better treatment than *any* domestic investor in Canada.

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<sup>62</sup> For instance, the Investor argues that standing exemptions provide provincial log producers more favourable treatment (*Investor Reply*, ¶¶ 263-269).

<sup>63</sup> For instance, the Investor argues that the absence of the fee-in-lieu under the federal regime provides federal log producers more favourable treatment (*Investor's Reply*, ¶ 274).

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**1. The Investor Ignores Domestic Federal and Provincial Land Owners in British Columbia that Receive the Same Treatment**

89. With respect to each of the allegations raised by the Investor, Canadian investors in like circumstances receive the exact same treatment as foreigners. The Investor chooses to disregard this.

90. All federal private land owners in B.C. are subject to the surplus test under *Notice 102*. They are accorded the same treatment that Merrill & Ring receives for its logs produced from its federal lands. The Investor continues to disregard this despite the fact that its own witness, Richard Ringma, the Director of Marketing and Distribution of Island Timberlands, attests that this Canadian company - the second largest private forest landholder on the Coast of B.C.<sup>64</sup> - is equally subject to *Notice 102*.<sup>65</sup>

91. The Investor also ignores the fact that all domestic provincial land owners in British Columbia are equally subject to the provincial regime, as is Merrill & Ring for logs produced from its provincial land.

92. These facts alone defeat the Investor's national treatment claim. Yet the Investor has not provided any basis for looking beyond the treatment these domestic investors receive. The Investor appears to rely on an unsupported claim that it is entitled to "the most favourable treatment" accorded to any domestic investor anywhere in Canada. This authorizes the Investor to look beyond the treatment accorded to domestic investors most obviously in like circumstances with Merrill & Ring. Quite apart from the fact that the text of Article 1102 does not mandate so-called "most favourable treatment", but rather

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<sup>64</sup> *Ringma Statement*, ¶ 2.

<sup>65</sup> *Id.*, ¶ 3.

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“no less favourable treatment”, a proper comparison of treatment can only be made with domestic investors in like circumstances.

**2. The Investor Chooses Comparators that Are Not “in Like Circumstances”**

93. Instead of comparing the treatment that it receives under the federal and provincial regimes to the treatment received by domestic investors operating under the same regime, the Investor advances different comparators for each of its allegations to support its claim of differential treatment. The choice of these comparators ignores the relevant circumstances underlying the treatment at issue including policy considerations that explain differences in treatment between some regions of British Columbia.

**a) Merrill & Ring Is “Forced” to Observe the Requirements of *Notice 102* While Other Log Producers in B.C. and Alberta Are Not**

94. The Investor states that “other log producers” in B.C. are not subject to *Notice 102*. That is incorrect. As its title indicates, *Notice 102* applies to the “Export of logs from British Columbia.” Section 2.0 of *Notice 102* details the procedures to export logs from ‘Federal/Private Lands,’ while section 6.0 applies to the export of logs from ‘Provincial Lands’ and requires that any potential exporter of provincial logs follow the procedures in Part 10 of the *B.C. Forest Act*.<sup>66</sup>

95. The Investor seeks to compare treatment the federal government accords to federal land owners in British Columbia under *Notice 102*, to the treatment the B.C. government accords to provincial private land owners under Part 10 of the *B.C. Forest*

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<sup>66</sup> *Korecky Affidavit*, Exhibit 9.

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*Act*. It also compares its treatment to the treatment accorded to private land owners in Alberta.<sup>67</sup> This approach is fundamentally flawed because it seeks to compare treatment accorded to investors in different jurisdictions and in different circumstances.

**(i) Comparison with Log Producers in Alberta**

96. Log producers in Alberta and those in British Columbia are not in like circumstances. Canada details in its Counter-Memorial the policy rationale for *Notice 102* and its application to British Columbia. Federal log export controls were directed at British Columbia in order to “ensure that there is an adequate supply and distribution of (logs) in Canada” and “to ensure that any action taken to promote the further processing in Canada of a natural resource that is produced in Canada is not rendered ineffective by reason of the unrestricted exportation of that natural resource.”<sup>68</sup> As such, it complements the provincial local use and manufacture requirement in British Columbia.

97. Many factors distinguish British Columbia from other provinces: it is the only province which is a large net exporter of logs.<sup>69</sup> Coastal B.C. is located close to cost-effective water transportation to the Pacific Rim market,<sup>70</sup> and the logging industry is critical to the provincial economy.<sup>71</sup> These conditions do not exist in Alberta, making a “surplus test” for log exports from that province unnecessary.

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<sup>67</sup> *Investor’s Reply*, ¶¶ 216-222.

<sup>68</sup> *Korecky Affidavit*, ¶ 21 and Exhibit 1.

<sup>69</sup> *Reishus Affidavit*, ¶ 130, figure 20.

<sup>70</sup> *Reishus Affidavit*, ¶¶ 74-75.

<sup>71</sup> *Canada’s Counter-Memorial*, ¶¶ 358-362.

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98. As described in the *Tapp Affidavit*, transportation costs for Alberta log exports are prohibitive.<sup>72</sup> Since 2004, only 27 export permits were issued to logs from Alberta.<sup>73</sup> All logs exported from Alberta's provincial public lands over that time have been fire-kill timber (i.e. logs affected by forest fires). As Mr. Tapp explains, these logs are drier and weigh less than green logs, and therefore are less expensive than green logs to transport by truck.<sup>74</sup>

**(ii) Comparison with Log Producers on Provincial Lands**

99. With respect to its federal lands, the Investor is not in like circumstances to domestic investors on provincial lands in B.C. While the treatment under *Notice 102* and the treatment under Part 10 of the *B.C. Forests Act* is somewhat similar, investors under different jurisdictions are not in like circumstances. The treatment accorded to federal and provincial land owners in B.C. cannot therefore be compared.

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<sup>72</sup> *Tapp Affidavit*, ¶¶ 3-4.

<sup>73</sup> *Korecky Supplemental Affidavit*, ¶¶ 35-36. By contrast, over 3,000 export permits have been issued for the export of B.C. logs in the last two years alone.

<sup>74</sup> *Tapp Affidavit*, ¶ 9.

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**(iii) Summary**

100. In the table below, Canada summarizes the improper comparators proposed by the Investor, together with the correct comparators that should be used by the Tribunal.

| MEASURE AT ISSUE  | MERRILL & RING COMPARATORS                      | PROPER COMPARATORS                           |
|-------------------|---|--|
| <i>Notice 102</i> | <i>Alberta</i> log producers                    | Log producers on federal land in <u>B.C.</u> |
|                   | Log producers on <u>provincial</u> land in B.C. | Log producers on <u>federal</u> land in B.C. |

**b) Merrill & Ring Is “Forced” to Sell its Logs Domestically While Log Producers in Alberta Are Not**

101. This allegation repeats the previous allegations. The treatment at issue is the application of *Notice 102* and its surplus test to Merrill & Ring but not to log producers in other provinces such as Alberta. The Investor characterizes this treatment as being “forced to sell its logs domestically” notwithstanding the fact that only rarely have the Investor’s logs been denied surplus status.<sup>75</sup>

102. As set out in the previous section, it is inappropriate to compare treatment accorded by different jurisdictions. Moreover, log producers in British Columbia and log

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<sup>75</sup> Since *Notice 102* has been in force, over [REDACTED] of the Investor’s logs were immediately available for export because no offer was made on them; *Korecky Supplemental Affidavit Exhibit 84; Canada’s Counter-Memorial*, ¶¶ 110-116.



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producers in other provinces are not in like circumstances with respect to *Notice 102* and the surplus test. The need for log export controls, including the “surplus test,” stems from the particular situation in British Columbia.

103. In the table below, Canada summarizes the improper comparator proposed by the Investor together with the correct comparator that should be used by the Tribunal.

| MEASURE AT ISSUE                     | MERRILL & RING COMPARATOR                                 | PROPER COMPARATOR            |
|--------------------------------------|---|------------------------------|
| Surplus Test under <i>Notice 102</i> | Log producers in <u>other provinces</u> including Alberta | Log producers in <u>B.C.</u> |

**c) Merrill & Ring Is “Forced” to Sell its Logs Under “Blockmail” While Log Producers in Alberta Are Not**

104. While the Investor characterizes the treatment as being “forced” to sell its logs domestically under “blockmail,” what is really at issue is the application of *Notice 102* and the surplus test to Merrill & Ring. Again, for the reasons set out in the previous sections, the comparison between the regime in B.C. and the regime in Alberta is inappropriate. Treatment accorded by different jurisdictions cannot be compared and, in any event, log producers outside the province of B.C. are not in like circumstances.

105. Further, to the extent that the Investor is challenging the conduct of private companies that make offers on logs that Merrill & Ring advertises for sale, there is no treatment accorded by Canada that can be the basis of a national treatment comparison.

106. In the table below, Canada summarizes the improper comparator proposed by the Investor together with the correct comparator that should be used by the Tribunal.

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| MEASURE AT ISSUE                               | MERRILL & RING COMPARATOR                                 | PROPER COMPARATOR            |
|--|---|------------------------------|
| “Blockmail” i.e. Surplus Test Under Notice 102 | Log producers in <i>other provinces</i> including Alberta | Log producers in <i>B.C.</i> |

**d) Merrill & Ring Is “Forced” to Cut, Sort, and Scale its Logs in a Particular Way While Log Producers in the B.C. Interior and Alberta Are Not**

107. The Investor groups two different types of “treatment” under this allegation: (1) the *Notice 102* requirement that log producers in B.C. cut and scale their logs according to the B.C. Metric System; and (2) the *Notice 102* requirement that log producers in B.C. sort their logs according to “normal market practices” which are reflected in the *B.C. Coast End-Use Sort Descriptions* for coastal log producers.

**(i) Cutting and Scaling**

108. With respect to the requirement to cut and scale logs in B.C. in accordance with the B.C. Metric System, this provincially mandated scaling system applies to all log producers in British Columbia. The Investor compares this treatment with the treatment received by out of province log producers. This comparison of treatment accorded by different jurisdictions is inapposite. Log producers in other provinces are not in like circumstances: other provinces have their own requirements. All B.C. logs must be scaled according to the B.C. scaling requirements,<sup>76</sup> while Alberta has its own

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<sup>76</sup> *Cook Affidavit*, ¶¶ 65-69.

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provincially-mandated scaling system.<sup>77</sup> Province-wide scaling systems are necessary for the proper, fair and uniform administration of the province's annual allowable harvest level and assessment of any applicable provincial taxes. In B.C., uniform scaling is also necessary for the bi-weekly advertising process as it ensures that domestic purchasers can correctly assess the value of the log.<sup>78</sup>

109. In the table below, Canada summarizes the improper comparator proposed by the Investor together with the correct comparator that should be used by the Tribunal.

| <b>MEASURE AT ISSUE</b>                           | <b>MERRILL &amp; RING<br/>COMPARATOR</b>                  | <b>PROPER COMPARATOR</b>     |
|---|---|------------------------------|
| Cutting and scaling requirements under Notice 102 | Log producers in <i>other provinces</i> including Alberta | Log producers in <u>B.C.</u> |

**(ii) Sorting**

110. With respect to sorting requirements, the Investor alleges that Merrill & Ring (whose timberlands are on the B.C. Coast) is in like circumstances to log producers in the B.C. Interior and logs producers in Alberta.

111. Insofar as the Investor compares sorting requirements in British Columbia and Alberta, the comparison is inappropriate because it compares treatment accorded by

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<sup>77</sup> Tapp Affidavit, ¶¶ 13-15.

<sup>78</sup> Cook Affidavit, ¶ 65; Cook Supplemental Affidavit, ¶ 47.

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different jurisdictions and under different circumstances. To the extent that the Investor compares sorting requirements for log producers in the Interior and on the Coast, the comparison is also inappropriate because these log producers are not in like circumstances.

112. The requirement to sort to “normal market practices of not less than 90% of a single species and recognized domestic end use sort by volume” applies to all log producers in British Columbia.<sup>79</sup> However, because market practices are different in different regions of B.C.,<sup>80</sup> sorting requirements in the B.C. Interior are different from those for the B.C. Coast. Market practices are affected by the level of variability in log quality, size and species, and market demands. Descriptions of these market practices have been developed by log traders, mill exporters and the government.<sup>81</sup> Contrary to the Investor’s assertion, the use of these descriptions benefits all market participants: they facilitate private transactions of logs, assigning maximum value to a variable commodity.<sup>82</sup>

113. “Normal market practices” on the B.C. Coast are reflected in the *Coast Domestic End Use Sort Descriptions*. As explained by John Cook, the *Coast Domestic End Use Sort Descriptions* take into account the large variability in grade, species and size of logs

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<sup>79</sup> *Korecky Affidavit*, Exhibit 9.

<sup>80</sup> *Reishus Affidavit*, ¶¶ 25-26.

<sup>81</sup> *Cook Affidavit*, ¶¶ 54-55.

<sup>82</sup> *Id.*, ¶ 62.

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unique to B.C.'s log market and are designed to enable log marketers to assess and receive the best possible value for a boom of logs on the Vancouver Log Market.<sup>83</sup>

114. The situation is quite different in the B.C. Interior and in Alberta. Log sorts in B.C.'s Interior and in Alberta do not have the same variability in the grade, species and size of logs as compared to the Coast.<sup>84</sup> Both of these regions have a much greater homogeneity in species and sort mixes than the logs grown on B.C.'s Coast and have developed less elaborate sorting practices than what is necessary on the Coast.<sup>85</sup> For instance, log producers located in B.C.'s Interior sort their logs according to their own market practices.<sup>86</sup> In light of the uniformity in Alberta logs, sorting of Alberta logs is generally unnecessary.<sup>87</sup>

115. In the table below, Canada summarizes the improper comparators proposed by the Investor together with the correct comparators that should be used by the Tribunal.

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<sup>83</sup> *Id.*, ¶ 62.

<sup>84</sup> *Canada's Counter-Memorial*, ¶¶ 376-383; *Reishus Affidavit*, ¶¶ 38-46.

<sup>85</sup> *Canada's Counter-Memorial*, ¶ 381; *Tapp Affidavit*, ¶ 16.

<sup>86</sup> *Reishus Affidavit*, ¶ 50.

<sup>87</sup> *Tapp Affidavit*, ¶ 16.

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| MEASURE AT ISSUE   | MERRILL & RING COMPARATORS         | PROPER COMPARATOR               |
|--|------------------------------------|---------------------------------|
| Sorting requirements<br>( <i>Coast Domestic End Use Descriptions</i> ) | B.C. <i>Interior</i> log producers | B.C. <i>Coast</i> log producers |
|  | <i>Alberta</i> log producers       | <i>B.C. Coast</i> log producers |

e) **Merrill & Ring Is “Forced” to Observe the So-Called “Remoteness Rule” While Other Log Producers on the B.C. South Coast Are Not**

116. The Investor challenges the application of the *Notice 102* minimum and maximum volume requirements for advertising logs that are located on its remote lands as a violation of national treatment. It identifies “domestic investors with lands in ‘non-remote’ areas” of B.C. as the relevant comparator.<sup>88</sup>

117. All log producers that operate on federal private land in B.C. are subject to the requirement in *Notice 102* with respect to advertising logs located in remote areas. Whether booms are subject to this requirement depends on the location of the booms at issue, not on the identity of the log producer.<sup>89</sup>

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<sup>88</sup> *Investor’s Reply*, ¶ 262.

<sup>89</sup> Indeed, Merrill & Ring does not allege that all its lands are considered “remote.”

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118. B.C. log producers that advertise their logs from non-remote locations on the Federal Bi-Weekly List are not “in like circumstances” with those that advertise non-remote from remote locations. Transportation is not an impediment for potential buyers that are considering making an offer on advertised booms.

119. Thus, the log producers from remote lands advertising are not in the same situation as log producers advertising from non-remote lands because without the minimum volume requirement, they may easily circumvent the very purpose of the surplus test.

120. In the table below, Canada summarizes the improper comparator proposed by the Investor together with the correct comparators that should be used by the Tribunal.

| MEASURE AT ISSUE  | MERRILL & RING COMPARATOR                                  | PROPER COMPARATOR                                      |
|---|--|--|
| Minimum volume requirement for advertising (remote areas) | Log producers in B.C. operating in <i>non-remote</i> areas | Log producers in B.C. operating in <i>remote</i> areas |

**f) Merrill & Ring Is “Forbidden” from Receiving Standing Exemptions While Log Producers on Provincial Lands Are Not**

121. The Investor compares the availability of certain standing exemptions for provincial land owners under the B.C. *Forest Act* to the absence of such exemptions for federal land owners under *Notice 102*. This is another case where the Investor seeks to compare the treatment accorded by two different jurisdictions. While the Investor may

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be in like circumstances to log producers on provincial lands with respect to its provincial lands,<sup>90</sup> it is not in like circumstances with respect to its federal lands.

122. In support of the allegation that Merrill & Ring receives less favourable treatment because it is not allowed standing exemptions on its federal land, the Investor suggests that Canada “has in fact granted [standing] exemptions to Merrill & Ring’s competitors on the B.C. Coast.”<sup>91</sup> This allegation is based on the Macpherson Statement which refers to certain standing exemptions granted by the Province.<sup>92</sup> Again, the Investor is seeking to compare treatment accorded by two different jurisdictions.

123. The Investor also refers to the fact that First Nations log producers have been granted standing exemptions by the province on federal lands. This is wrong: the province cannot grant standing exemptions on federal lands. The Federal Department of Indian and Northern Affairs approves the removal of logs from reserve lands.<sup>93</sup>

124. Nor are First Nations log producers in like circumstances to other log producers in B.C., for constitutional reasons. In any event, the allegation of breach of national treatment based on differential treatment accorded to First Nations is not admissible

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<sup>90</sup> If, like other provincial log producers, it meets the criteria to obtain a standing exemption under the *B.C. Forest Act*. However it appears that even if Merrill & Ring’s lands were subject to provincial jurisdiction, it would probably not qualify for a standing exemption. Growth conditions on B.C.’s South Coast where Merrill & Ring’s logs are located simply do not support receipt of a standing exemption. No provincial log producer has received a standing exemption since 2003. See *Cook Supplementary Affidavit*, ¶¶ 19-23.

<sup>91</sup> *Investor’s Reply*, ¶ 267.

<sup>92</sup> *Macpherson Report*, ¶ 20.

<sup>93</sup> *Korecky Affidavit*, ¶¶ 59-61.



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given that Canada has taken a reservation from its national treatment obligations with respect to Aboriginal Affairs.<sup>94</sup>

125. In the table below, Canada summarizes the improper comparators proposed by the Investor together with the correct comparator that should be used by the Tribunal.

| MEASURE AT ISSUE                                    | MERRILL & RING COMPARATORS                      | PROPER COMPARATOR                                   |
|---|---|---|
| Standing exemptions (unavailable to Merrill & Ring) | Log producers on <i>provincial</i> land in B.C. | Log producers on <i>federal</i> land owners in B.C. |
|   | First Nations log producers                     | Not Applicable                                      |

**g) Merrill & Ring Is “Forbidden” from Advertising Standing Timber While Log Producers in the B.C. Interior Are Not**

126. The Investor challenges the fact that in administering *Notice 102*, DFAIT has allowed log producers in the B.C. Interior, but not log producers on the B.C. Coast, to advertise on the Bi-Weekly List while their timber is still standing. The Province has a similar practice of allowing producers in the Interior, but not on the Coast, to advertise their standing timber. The Investor’s expert cites four FTEAC meetings in which

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<sup>94</sup> NAFTA, Annex II-C-1.

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standing applications were approved for log producers on the Coast.<sup>95</sup> This assertion is incorrect. John Cook, the Secretary of FTEAC has reviewed the records of these meetings and found that no standing surplus applications were considered at the meetings cited by the Investor's expert.<sup>96</sup>

127. Both the federal and B.C. governments' policies have evolved to allow standing applications in the B.C. Interior due to inadequate transportation, lack of available storage and rapid deterioration of logs in the region. In addition, the roads in the B.C.'s Interior are only passable in certain seasons. These conditions do not generally exist on the B.C. Coast. As a result, log producers in the Interior and coastal log producers are not in like circumstances.<sup>97</sup>

128. In the table below, Canada summarizes the improper comparator proposed by the Investor together with the correct comparator that should be used by the Tribunal.

| MEASURE AT ISSUE      | MERRILL & RING COMPARATOR          | PROPER COMPARATOR               |
|-----------------------|------------------------------------|---------------------------------|
| Standing applications | B.C. <i>Interior</i> log producers | B.C. <i>Coast</i> log producers |

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<sup>95</sup> Macpherson Report, ¶ 18(d).

<sup>96</sup> Cook Supplemental Affidavit, ¶ 26.

<sup>97</sup> Canada's Counter-Memorial, ¶¶ 402-404; Korecky Affidavit, ¶¶ 82-83.

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**h) Merrill & Ring Is Required to Pay a Fee-in-Lieu to Export its Provincial Logs While Federal Log Producers Are Not**

129. The Investor challenges the requirement under the *B.C. Forest Act* to pay a fee-in-lieu of local use and manufacture for logs grown on its provincial lands that are exported. Contrary to its earlier submissions with respect to this allegation, the Investor now argues that log producers on federal lands, including itself, receive better treatment. For the reasons submitted above, the Tribunal must reject the Investor's proposed comparison between treatment accorded by different jurisdictions.<sup>98</sup>

130. In the table below, Canada summarizes the improper comparator proposed by the Investor together with the correct comparator that should be used by the Tribunal.

| MEASURE AT ISSUE           | MERRILL & RING COMPARATOR                            | PROPER COMPARATOR                               |
|----------------------------|--|---|
| Fee-in-lieu of manufacture | Log producers on <i>federal</i> private land in B.C. | Log producers on <i>provincial</i> land in B.C. |

<sup>98</sup> In any event, to the extent that the Investor alleges that the fee-in-lieu of local use and manufacture provided by Part 10 of the *B.C. Forest Act* breaches NAFTA Article 1102, it would be exempt under Article 1108(1)(a)(ii) as a provincial non-conforming measure. Article 1108(1)(a)(ii) provides: "Articles 1102, 1103, 1106 and 1107 do not apply to: any existing non-conforming measure that is maintained by a state or province, for two years after the date of entry into force of this Agreement, and thereafter as set out by a Party in its Schedule to Annex I in accordance with paragraph 2, (...)." In a 1996 exchange of letters, the NAFTA Parties agreed that any state or provincial non-conforming measures in place at the time of NAFTA's accession are exempt from Articles 1102, 1103, 1106 and 1107. Given that the provincial fee-in-lieu has been in place for decades, it falls within the reservation for existing non-conforming provincial measures.

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**i) Conclusion: The Investor Ignores Canadian Investors in Identical Circumstances and Selects Improper Comparators to Make its Claim**

131. There are dozens of Canadian log producers that are operating in identical circumstances to the Investor. The Regime applies to these Canadian log producers in exactly the same way as it applies to the Investor. As a result, the Investor's has no choice but to select unlike comparators in different jurisdictions to make its national treatment claim. The Investor's approach is entirely misguided and must be rejected.

**D. In Any Event, the Investor Fails to Meet its Own "Like Circumstances" Test: Log Producers from the B.C. Coast, the B.C. Interior and Alberta Rarely Compete**

132. To avoid the fact that domestic private land owners in B.C. receive the exact same treatment as Merrill & Ring – the Investor equates the "like circumstances" test to a "like product" test. Canada submits that this is not the appropriate test and that the issue of whether logs from the B.C. Coast, B.C. Interior and Alberta compete is irrelevant. However, even if the Tribunal were to accept this test, the Investor fails to meet it: it relies on anecdotal evidence to establish that logs from coastal British Columbia, logs from the Interior region of British Columbia and logs from other provinces compete "on occasion" in export markets. Canada has clearly demonstrated that this is not the case. Indeed, B.C. coastal logs very rarely end up in the same markets as B.C. Interior or Alberta logs.<sup>99</sup>

133. To make its case that its logs compete with logs from B.C.'s Interior (the so-called "wet belt") and Alberta, the Investor presents a statement from a log processor in

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<sup>99</sup> *Korecky Supplemental Affidavit*, ¶¶ 35-37.

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Idaho. Idaho Forest Group states that it uses logs from the three regions “interchangeably.”<sup>100</sup> This anecdotal account is not proof that the Investor’s logs *compete* with logs from B.C.’s Interior and Alberta. In fact, Alberta log producers rarely export.<sup>101</sup> In 2000, Alberta was the third-ranking province for log exports by total value, accounting for 3.07% of exports. Since then, Alberta log exports have steadily fallen, such that it was the last-ranking province for log exports by total value, representing only 0.01% of total log exports in 2007.<sup>102</sup> As Judy Korecky notes, Alberta only exports logs in “a few isolated cases.”<sup>103</sup>

134. The Investor’s contention that logs from B.C.’s Interior (wet belt) compete with B.C.’s coastal logs is false. Mr. Jendro points out that log trading between the two regions is an exception.<sup>104</sup> Even the Investor’s own expert, Douglas Ruffle, acknowledges that trade between B.C.’s Interior and coastal regions is “small and infrequent.”<sup>105</sup> As noted by Mr. Ruffle, it is not economical to move logs east-west across the mountains in both B.C. and the United States. Consequently, “competition usually runs north-south.”<sup>106</sup> Mr. Jendro confirms that transportation costs and available routes

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<sup>100</sup> Boeh Letter to Barry Appleton of December 3, 2008.

<sup>101</sup> *Korecky Affidavit*, ¶ 10 and attached Exhibit 3; *Korecky Supplemental Affidavit*, ¶ 35; *Tapp Affidavit*, ¶ 8.

<sup>102</sup> *Reishus Affidavit*, ¶ 129, Figure 20, *Log Exports and Imports by Province 2005-2007*.

<sup>103</sup> *Korecky Supplemental Affidavit*, ¶ 34.

<sup>104</sup> *Jendro Supplemental Affidavit*, ¶ 7.2.20.

<sup>105</sup> *Ruffle Report*, ¶ 4.6.2.

<sup>106</sup> *Id.*, ¶ 4.1: “The competition usually runs north-south across the border not east-west along it.” “Long transportation distances and high trucking and rail costs usually make it uneconomical to move logs from west to east across the mountains in both BC and the US. The sawmills in the US Inland and BC Interior therefore source only small volumes of logs from the BC Coast.”

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through the mountains present “insurmountable” obstacles to the creation of overlapping markets between the two regions.<sup>107</sup>

135. Unable to establish competition, the Investor claims that its logs and logs from Alberta and B.C.’s Interior are “substitutable.”<sup>108</sup> Again, the Investor ignores important differences that make the logs inherently non-substitutable to log processors.<sup>109</sup> The coastal log processors have developed discrete capabilities to process coastal logs, which have a much greater variability in quality, value and size than other Canadian logs.<sup>110</sup> Similarly, the log processing industry in B.C.’s Interior and Alberta have developed their own unique processes according to the characteristics of the logs that are grown in these regions. For instance, the sawmilling industry in B.C.’s Interior is characterised by efficient, modern high volume mills that produce lumber typically used in home construction.<sup>111</sup> As a result, logs from B.C.’s Coast, Interior and Alberta, are not “substitutable” to log processors in each region.

**E. Conclusion**

136. The Investor has not proved any breach of Article 1102. Article 1102 only prohibits nationality-based discrimination. There is no evidence of such discrimination. In fact, all federal private landowners in B.C. are equally subject to *Notice 102*. The Investor points to differences in treatment based on inappropriate comparisons. Most of

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<sup>107</sup> *Jendro Supplemental Affidavit*, ¶ 7.2.20.

<sup>108</sup> *Investor’s Reply*, ¶ 218.

<sup>109</sup> *Reishus Affidavit*, ¶¶ 47-49.

<sup>110</sup> *Id.*, ¶ 40.

<sup>111</sup> *Id.*, ¶ 47.

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the Investor's allegations of "different" treatment rest on a comparison of treatment accorded by different jurisdictions (federal/provincial or B.C./Alberta) and are therefore fundamentally flawed. In other cases, the comparison is with treatment accorded to log producers in different regions of B.C. (Coast/Interior) and, as such, not in like circumstances. The Tribunal should therefore reject the Investor's allegations that it has not been accorded national treatment.

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#### IV. THERE IS NO VIOLATION OF NAFTA ARTICLE 1105

##### A. Summary of Canada's Position

137. Under Article 1105, the Investor must prove that Canada breached a rule of customary international law that is recognized as part of the international minimum standard for the treatment of aliens. To avoid the application of this high threshold, the Investor has put forward a series of creative but flawed arguments. The Investor aims to convince this Tribunal to follow arbitral awards rendered *outside* the context of NAFTA Chapter 11. However, these decisions are irrelevant in the context of proceedings convened under NAFTA Chapter 11. The Tribunal cannot disregard the binding Note of Interpretation as the Investor urges it. The Tribunal must apply the Note, which reflects the Parties' intention to limit their obligations to the minimum standard of treatment of aliens under customary international law ("custom").

138. In any event, Canada will demonstrate that the Regime does not breach Article 1105 because it is transparent and not arbitrary. In this respect, the Investor's complaint is now reduced to rather trivial irritants, such as not being consulted on the selection of new FTEAC members, not being allowed to make "oral submissions" at FTEAC meetings, not knowing the relevant factors considered by the Minister when choosing to disregard an FTEAC recommendation, and the cancellation of one FTEAC meeting out of more than a hundred in the last 10 years. These alleged administrative irregularities, taken separately or collectively, do not breach Article 1105(1).

139. The Investor still claims to be the victim of so-called "blockmailing." However, the Investor does not identify any instances of "blockmailing" other than the single example identified in its Memorial and to which Canada has already responded. In any event, Canada is not responsible for the actions of private log companies. Moreover, Canada has already explained that it takes all necessary measures to prevent and sanction any wrongful actions by private companies.



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140. The Investor's Article 1105 claim should therefore be dismissed.

## **B. The Proper Meaning of Article 1105**

### **1. Introduction**

141. The ultimate goal of the Investor's Article 1105 claim is to convince this Tribunal to follow the conclusions of arbitral awards rendered *outside* the context of NAFTA Chapter 11. The reason is simple. The Investor considers these decisions to be more favourable to its case than those rendered by NAFTA Chapter 11 tribunals.

142. The Tribunal must refuse the Investor's approach as it is contrary to the governing law of this arbitration. Contrary to some BITs that have a stand-alone "fair and equitable treatment" clause, the NAFTA minimum standard clause is tied to customary international law. The NAFTA Parties intended to limit their obligations to the minimum standard of treatment of aliens under customary international law ("custom"). This intent was made clear by the Parties through the Free Trade Commission ("FTC") Interpretive Note issued in 2001 ("the Note"). The Note explicitly states that the terms "fair and equitable treatment" and "full protection and security" were not intended to add anything to existing obligations under custom.<sup>112</sup> The reasoning of non-NAFTA tribunals is therefore irrelevant to this case.

143. Rightly fearing that this interpretation of Article 1105(1) would defeat its claim, the Investor attempts to convince this Tribunal otherwise. In doing so it has put forward a number of surprising—and troubling—arguments, and has not hesitated to misrepresent and distort key source material.

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<sup>112</sup> NAFTA Free Trade Commission, *Notes of Interpretation of Certain Chapter Eleven Provisions*, 31 July 2001 ("*NAFTA FTC Notes*") (Tab 92).

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- In its opening salvo, the Investor argues that this Tribunal should simply *disregard* the Note. It contends that it is “*impossible*” that the NAFTA Parties really meant “custom” although they expressly used that term in the Note.<sup>113</sup> The Investor explains that the Parties’ “true intention” was to include “all sources of international law.” The Investor invites the Tribunal to find that the Note is not binding, despite the fact that Article 1131(2) explicitly makes it so.
- In a follow-up argument, the Investor changes gears and dismisses the Note as irrelevant. Instead, it suggests that there is a rule of “custom” that requires the Tribunal to apply *all sources* of international law.
- Based on this fictitious rule of “custom”, the Investor argues that nothing prevents the Tribunal from examining non-NAFTA decisions to inform the proper meaning of Article 1105(1). In another example of circular reasoning, the Investor contends that this approach is justified because the meaning of “fair and equitable treatment” in Article 1105(1) is exactly the same as that given to other differently drafted clauses by non-NAFTA tribunals.
- In a final attempt to convince this Tribunal to apply these non-NAFTA decisions, the Investor asserts, without the slightest shred of evidence to support its view, that the minimum standard of treatment of foreign investors under custom has “converged” with the expansive stand-alone standard of fair and equitable treatment found in some BITs. In other words, the Investor argues that there is now only *one* standard and that the

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<sup>113</sup> *Investor’s Reply*, ¶ 297.

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Tribunal is therefore entitled simply to disregard the 2001 Note as anachronistic.

144. Canada will demonstrate that these arguments are not only based on faulty logic, but are also in conflict with basic principles of treaty interpretation. The Tribunal should recognize the argument as a manoeuvre to distract it from the fact that none of the Investor’s allegations, even if true, would amount to a breach of the minimum standard of treatment provided for by Article 1105. The Investor has failed to prove that any of the acts and omissions allegedly committed by Canada constitutes a breach of the minimum standard of treatment of aliens under customary international law.

## 2. The Note Is Clear and Binding

145. The Note is explicit and clear: the minimum standard of treatment to be accorded to foreign investors under Article 1105 is the one existing under *custom*. Pursuant to Article 1131(2), the Note constitutes the definitive interpretation of Article 1105(1), and NAFTA tribunals must apply that provision in a manner consistent with the Note.

146. The Investor did not even mention the Note in its Memorial and now argues that the Tribunal should simply disregard it in favour of a more expansive reading of Article 1105. The Investor submits three distinct reasons for ignoring the Note, which will be examined separately.

### a) There Is No Conflict Between Article 1131(1) and the Note

147. The Investor’s first argument is that there is an “irresolvable conflict” between Article 1131(1) and the Note since the former requires the Tribunal to consider “all

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applicable rules of international law”, whereas the latter restricts it “to applying only rules of customary international law.”<sup>114</sup>

148. What the Investor conveniently omits is that, under Article 1131(1), a tribunal must first and foremost decide a dispute “in accordance with this Agreement”, that is, NAFTA. Article 1131 describes the sources of law to be applied by a Chapter 11 tribunal. Article 1105 is of a different nature: it outlines the *content* of a specific obligation, the minimum standard of treatment that is to be understood by reference to customary international law. There is, therefore, no conflict at all between the Note and 1131(1).

**b) The Note Is Not Contrary to the Plain Meaning of Article 1105(1)**

149. The Investor’s second argument is that “Canada’s interpretation”<sup>115</sup> of the Note is contrary to the plain meaning of Article 1105(1). This is because the latter refers to “*all sources* of international law listed in Article 38 of the I.C.J. Statute”, and not only to custom.<sup>116</sup> The Investor goes so far as to claim that “it is simply *impossible* that the Notes accurately reflect the Parties’ true intention at the time they drafted the NAFTA” and that, consequently, the Tribunal should simply disregard it and “interpret NAFTA Article 1105(1) in accordance with its original wording.”<sup>117</sup> For the Investor, any other

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<sup>114</sup> *Investor’s Reply*, ¶ 291.

<sup>115</sup> *Id.*, ¶ 289.

<sup>116</sup> *Id.*, ¶ 292 (emphasis added).

<sup>117</sup> *Id.*, ¶ 297 (emphasis added).

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interpretation would deprive the words “fair and equitable treatment” in NAFTA Article 1105(1) of any meaning and lead to an “absurd or unreasonable result.”<sup>118</sup>

150. As one of the Parties to the NAFTA, Canada is well-positioned to speak to the issue of the “true intention” of the Parties when drafting Article 1105. Canada reiterates that the intent was to incorporate the standard existing under custom. This “true intention” is unambiguously confirmed by the *Statement on Implementation* issued by Canada in 1994. In it, Canada clearly explains that Article 1105 “provides for a minimum absolute standard of treatment, *based on long-standing principles of customary international law.*”<sup>119</sup> That was, and still is, the “true intention” behind Article 1105(1).

151. The NAFTA Parties have repeatedly explained their intent in other arbitration proceedings, and they adopted a binding interpretive Note which expresses this intent. Far from being an “amendment” as the Investor claims,<sup>120</sup> the Note simply *confirms* the original intention of the Parties. Whatever ambiguities may have previously existed have

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<sup>118</sup> *Investor’s Reply*, ¶ 295.

<sup>119</sup> *Canadian Statement on Implementation*, 1 January 1994, at 149 (emphasis added) (“*Canada’s Statement*”) (Tab 19).

<sup>120</sup> *Investor’s Reply*, ¶ 301.

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been definitively resolved by the 2001 Note. Since then, NAFTA Chapter 11 tribunals have consistently referred to the Note and applied the minimum standard of treatment.<sup>121</sup>

152. The Investor claims to have found support for its absurd reading of Article 1105(1) in the writings of various scholars. However, the Investor grossly misrepresents the opinions of the authors it cites, even going so far as to deliberately distort the meaning of certain passages through selective pruning.<sup>122</sup> For instance, the Investor claims that the work of Professor Schreuer supports the view that it is “inherently implausible” that a treaty would use the words “fair and equitable treatment” if the intention were to refer to the minimum standard of treatment in custom.<sup>123</sup> However, the Investor omits to mention that, in the very same text, Professor Schreuer takes a view exactly opposite to what the Investor suggests, stating that Article 1105(1) refers only to custom: “Therefore, it may now be regarded as established that, in the context of Article

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<sup>121</sup> For instance, in *ADF Group Inc. v. United States* (ICSID No. ARB(AF)/00/1) Final Award, 6 January 2003 (“*ADF – Award*”), ¶ 178 (Tab 2), the Tribunal explained that the Note “specifies that the ‘treatment in accordance with international law’ referred to in Article 1105(1) is the minimum standard of treatment of aliens prescribed in customary international law.” See also: *Mondev International Ltd. v. United States* (ICSID No. ARB(AF)/99/2) Award, 11 October 2002 (“*Mondev – Award*”), ¶ 121 (Tab 87) (“[the Notes] makes it 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.”); *United Parcel Service of America Inc. v Canada*, Award on Jurisdiction, ¶ 97 (Tab 146), (“We do not address the question of the power of the Tribunal to examine the Interpretation of the Free Trade Commission. Rather, we agree in any event with its conclusion that the obligation to accord fair and equitable treatment is not in addition to or beyond the minimum standard.”).

<sup>122</sup> It should be added that the Investor’s reference (*Investor’s Reply*, ¶ 294) to a UNCTAD report, “Fair and Equitable Treatment” is completely irrelevant to this claim since this report does *not* even deal with the NAFTA and, in any event, was published in 1999, i.e. before the Parties issued the interpretative Note.

<sup>123</sup> This is the original quote found in the *Investor’s Reply*, at ¶ 292: “As a matter of textual interpretation, it is inherently implausible that a treaty would use an expression such as ‘fair and equitable treatment’ to denote a well known concept such as the ‘minimum standard of treatment in customary international law.’ If the parties to a treaty want to refer to customary international law, it must be presumed that they will refer to it as such rather than using a different expression” (Schreuer, Christoph H., “*Fair and Equitable Treatment in Arbitral Practice*”, 6 J. World Invest. & Trade (June 2005), at 360 (“*Schreuer – FET Practice*”) (Tab 125).

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1105(1) NAFTA, the concept of fair and equitable treatment is equivalent to the minimum standard of treatment under customary international law.”<sup>124</sup>

153. In a similar vein, the Investor misrepresents the opinion of Professor Dolzer and Margrete Stevens. It claims, falsely, that in their view the words “fair and equitable treatment” in Article 1105(1) provide an obligation in addition to the existing standard under customary international law.<sup>125</sup> Again, reading the passage in its entirety demonstrates that the authors hold the exact opposite view,

It is submitted here that the fact that parties to BITs have considered it necessary to stipulate this standard as an express obligation rather than relied on a reference to international law and thereby invoked a relatively vague concept such as the minimum standard, is probably evidence of a self-contained standard. Further, some treaties refer to international law in addition to the fair and equitable treatment, thus appearing to reaffirm that international law standards are consistent with, but complementary to, the provisions of the BIT. A reference to international law is common not only in U.S. treaties but also in several of the treaties concluded by Belgium-Luxembourg, France and Switzerland. In both U.S. and Swiss practice this reference is often combined with a reference to the applicable provisions of domestic legislation. *However, in the North American Free Trade Agreement (NAFTA), the fair and equitable standard is explicitly subsumed under the minimum standard of customary international law.*<sup>126</sup>

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<sup>124</sup> *Id.*, at 363.

<sup>125</sup> This is the original quote found in the *Investor's Reply*, ¶ 293: “[S]ome treaties [like the NAFTA] refer to international law in addition to the fair and equitable treatment, thus appearing to reaffirm that international law standards are consistent with, but complementary to, the provisions of the [treaty]” (Dolzer, R. & Stevens, M., *Bilateral Investment Treaties* (London: Martinus Nihoff Publishers, 1995) at 60) (Investor's Schedule of Documents, Tab 150) (“*Dolzer & Stevens*”).

<sup>126</sup> *Id.*, at 60 (emphasis added).

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**c) The Note Is an Interpretation of Article 1105, Not an Amendment**

154. The Investor submits a third argument for disregarding the Note. It alleges that the Note constitutes an “amendment” rather than an “interpretation” of Article 1105. The Note would therefore be *ultra vires* of the FTC’s mandate and, consequently, “not binding on this Tribunal.”<sup>127</sup>

155. The Investor cannot seriously dispute that the word “binding” expressly used at Article 1131(2) has any meaning other than just that. Any other interpretation would fly in the face of the “most basic tenets of treaty interpretation”<sup>128</sup> and would render this provision superfluous. No NAFTA tribunal, not even the *Pope & Talbot* Tribunal (contrary to what the Investor suggests<sup>129</sup>), has ever held the Note to be anything other than a binding interpretation of Article 1105(1). For instance, the *Methanex* Tribunal considered the Note to be “entirely legal and binding on a tribunal seized with a Chapter 11 case.”<sup>130</sup> In the *ADF* arbitration, the Investor attempted to disqualify the Note based on the same argument. The *ADF* Tribunal summarily refused even to consider the argument based on the ground that it *lacked jurisdiction* to make a ruling on the validity of the Note. The Tribunal explained that,

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<sup>127</sup> *Investor’s Reply*, ¶ 300.

<sup>128</sup> The expression is used by the Investor in: *Investor’s Reply*, ¶ 295.

<sup>129</sup> In *Pope & Talbot Inc. v. Canada* (UNCITRAL) Award in Respect of Damages, 31 May 2002 (“*Pope & Talbot – Damages Award*”), ¶ 47 (Tab 111) the Tribunal concluded that it was unnecessary to determine whether the Note is an “amendment” or an “interpretation”; it made its analysis based on the fact that the Note was an *interpretation*. It was critical of the Note, but this was merely *obiter dicta*.

<sup>130</sup> *Methanex - Award*, Part IV-Chapter C, ¶¶ 9, 20 (Tab 85).



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Nothing in NAFTA suggests that a Chapter 11 tribunal may determine for itself whether a document submitted to it as an interpretation by the Parties acting through the FTC is in fact an ‘amendment’ which presumably may be disregarded until ratified by all the Parties under their respective internal law.<sup>131</sup>

156. For the Tribunal, the Note was an “interpretation” and not an amendment:

We observe in this connection that the FTC Interpretation of 31 July 2001 *expressly purports to be an interpretation* of several NAFTA provisions, including Article 1105(1), *and not an “amendment,”* or anything else. No document purporting to be an amendment has been submitted by either the Respondent or the other NAFTA Parties. There is, therefore, no need to embark upon an inquiry into the distinction between an “interpretation” and an “amendment” of Article 1105(1).<sup>132</sup>

157. In sum, this Tribunal is *not* “at liberty”<sup>133</sup> to interpret the meaning of Article 1105 in a manner not consistent with the Note.

**3. Customary International Law Does Not Require that International Tribunals Apply All Sources of International Law**

158. Having expended much effort to convince the Tribunal that the Note is wrong and not binding, the Investor changes gears to argue that all of this *does not matter*.<sup>134</sup> The

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<sup>131</sup> *ADF - Award*, ¶ 177 (Tab 2). The Tribunal also rejected the claimant’s argument about the Tribunal’s “implied power” to examine the validity of the Note: “We do not find persuasive the Investor’s submission that a tribunal is impliedly authorized to do that as part of its duty to determine the governing law of a dispute. A principal difficulty with the Investor’s submission is that such a theory of implied or incidental authority, fairly promptly, will tend to degrade and set at naught the binding and overriding character of FTC interpretations. Such a theory also overlooks the systemic need not only for a mechanism for correcting what the Parties themselves become convinced are interpretative errors but also for consistency and continuity of interpretation, which multiple ad hoc arbitral tribunals are not well suited to achieve and maintain.”

<sup>132</sup> *ADF – Award*, ¶ 177 (emphasis added) (Tab 2).

<sup>133</sup> *Investor’s Reply*, ¶ 302.

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Investor's new argument is as follows: "[r]espondent States always engage in [international legal] disputes knowing that they will be decided in accordance with the rules and principles of international law" and that "[t]hey always do so in the belief that they are legally required to do so."<sup>135</sup> Believing that this satisfies the requirement to prove custom, the Investor concludes that "[r]esolving international legal disputes in accordance with all the rules and principles of international law" has become "a part of customary international law."<sup>136</sup>

159. This is a preposterous argument. Canada does not intend to rebut each of the statements leading to this absurd conclusion, but notes that the Investor has failed to understand what custom means at international law. The Investor confuses the legal term of art "customary international law" with the colloquial meaning of the word "customary."<sup>137</sup> It is one thing to say that tribunals *usually* or *typically* resolve disputes based on all sources of law; it is quite another to assert the existence of a rule of customary international law to that effect. In any event, the Investor fails to understand another basic facet of international law: rules of custom impose obligations *on States*, and not on tribunals.

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<sup>134</sup> The Investor explains that "[e]ven if the Tribunal decides that the Notes are valid and binding or otherwise decides to demur on the matter it should still interpret the "fair and equitable treatment" standard contained in NAFTA Article 1105(1) with reference to all sources of international law." (*Investor's Reply*, ¶ 303, emphasis added).

<sup>135</sup> *Investor's Reply*, ¶ 305.

<sup>136</sup> *Investor's Reply*, ¶ 305.

<sup>137</sup> The Investor's gross misunderstanding of the expression is clear when it states that "*it is customary to resolve international legal disputes in accordance with all the rules and principles laid out in Article 38(1) of the ICJ Statute*" (*Investor's Reply*, ¶ 307, emphasis added). Such misconception is also clear in the title of the relevant section of the Investor's Reply on this point ("It is Customary to Interpret Treaties in Accordance with All Sources of International Law", *Investor's Reply*, at 116).

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160. The Investor also seems to believe that decisions of arbitral tribunals can contribute to the actual “formation” of customary international law in and of themselves.<sup>138</sup> This is wrong. Under Article 38 of the *I.C.J. Statute*, “judicial decisions” are placed on an equal footing with the “writings of eminent publicists” and both are considered as a subsidiary source of law.

161. It is true that awards can play an important evidentiary role in elucidating the content of international law. For instance, arbitral awards sometimes contain valuable analysis of State practice and *opinio juris* in relation to a specific area of law, and future tribunals may choose to be guided by this analysis. Arbitral awards may thus have persuasive value for other tribunals. However, tribunal awards cannot create law or contribute in any way to the “formation” of custom. Custom can only be established by the actual practice of States, and not by the practice of international tribunals. Similarly, the relevant *opinio juris* is that of States, and not that of judges or arbitrators. This is, again, a very basic rule of international law; it is not “nonsensical” nor is it “formalistic.”<sup>139</sup> The Investor’s reference to the *ADF* award is not convincing.<sup>140</sup>

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<sup>138</sup> *Investor’s Reply*, ¶¶ 308-309.

<sup>139</sup> The Investor believes that “proving that the ‘fair and equitable treatment’ standard in non-NAFTA investment treaties has ‘crystallized’ into a rule of customary international law without reference to international jurisprudence is *not only nonsensical, but also highly impractical.*” (*Investor’s Reply*, ¶ 312, emphasis added).

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Similarly, the other quote from the I.C.J. *Gulf of Main Case* is taken out of context and not representative of the I.C.J. case law as explained by I.C.J. Judge Shahabuddeen.<sup>141</sup>

162. In short, this Tribunal *must* apply the Note, the meaning of which is clear: Canada's treatment of foreign investors is to be assessed according to the minimum standard of treatment existing under *custom*.

4. **Decisions Interpreting Stand-Alone Fair and Equitable Treatment Clauses Are Not Relevant to Article 1105(1)**

163. In an effort to broaden the content of the “fair and equitable treatment” (“FET”) standard under Article 1105(1), the Investor relies on non-NAFTA decisions. The Investor claims this is appropriate because there are no material differences between the

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<sup>140</sup> The Investor relies on a short passage from the *ADF* award to support its view. However, this case offers no support for its position. The Investor quotes the Tribunal as saying: “[A]ny general requirement to accord ‘fair and equitable treatment’ must be disciplined by being based upon State practice and judicial or arbitral case law or other sources of customary or general international law.” (*ADF – Award*, ¶ 184 (Tab 2)). This quote is taken out of context. In making those comments, the Tribunal was expressing its agreement with a proposition put forward by the *Mondev* Tribunal, to the effect that a general requirement to provide fair and equitable treatment does not empower a tribunal to dispose of a case *ex aequo et bono* based on its own “idiosyncratic” standard of what constitutes fair and equitable treatment. Contrary to what the Investor suggests, the *ADF* Tribunal was not endorsing the Investor’s view that a NAFTA Tribunal is “required” “to inform the meaning of ‘fair and equitable treatment’ in Article 1105(1) with reference to international jurisprudence” (*Investor’s Reply*, ¶ 309). Indeed, the claimant in *ADF* had advanced virtually the same argument as the Investor, yet the tribunal *explicitly declined* to rule on the matter because it was unnecessary to resolve the issues before it.

<sup>141</sup> Shahabuddeen, Mohamed, *Precedent in the World Court* (1996), at 71, (“*Shahabuddeen*”) (Tab 175); “It is difficult to regard a decision of the Court [or an international tribunal] as being in itself an expression of State practice... A decision made by it is an expression not of the practice of the litigating States, but of the judicial view taken of the relations between them on the basis of legal principles which must necessarily exclude any customary law which has not yet crystallised. The decision may recognise the existence of a new customary law and in that limited sense it may no doubt be regarded as the final stage of development, but, *by itself, it cannot create one*. It lacks the element of repetitiveness so prominent a feature of the evolution of customary international law.”

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content of Article 1105 and that of stand-alone FET Bilateral Investment Treaty (“BIT”) provisions under which these awards were rendered.<sup>142</sup> This is obviously wrong.

164. The wording of NAFTA Article 1105 is different from that of a “stand-alone” (or “autonomous”) FET clause contained in some BITs.<sup>143</sup> Article 1105(1) is *narrower* than the stand-alone standard contained in many BITs. While a stand-alone FET clause contained in a BIT generally “describes a higher standard that is *additional* to the customary law minimum standard”,<sup>144</sup> under NAFTA the FET standard is limited to customary norms. This is not an opportunistic assertion intended to frustrate the Investor’s claim: it is the openly acknowledged position of all the NAFTA Parties.<sup>145</sup> This is also the position taken by several arbitral tribunals.<sup>146</sup>

165. As a result, the reasoning of other tribunals on what is fair and equitable under BITs with different standards is irrelevant to this Tribunal’s analysis of Article 1105.

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<sup>142</sup> *Investor’s Reply*, ¶ 310.

<sup>143</sup> By “stand-alone” FET clauses, Canada refers to provisions which do *not* contain any reference to “international law.” These provisions must be clearly distinguished from other FET clauses which make reference to “international law” such as those found in several BITs entered into by Canada with other States in the 1990s. These FET clauses referring to international law must be interpreted according to the minimum standard of treatment under *custom*.

<sup>144</sup> Schreuer, Christoph H., “*Fair and Equitable Treatment (FET): Interactions with other Standards*” (2007) 4 *Transnational Dispute Management*, at 17 (“*Schreuer – FET Interactions*”) (Tab 124).

<sup>145</sup> For instance, the United States’ position in its Rejoinder, 15 March 2007, 147 *et seq.*, in: *Glamis Gold Ltd. v. United States* (UNCITRAL) (“*Glamis – US Rejoinder*”) (Tab 170).

<sup>146</sup> For instance, *Saluka Investments BV (The Netherlands) v. The Czech Republic* (UNCITRAL) Partial Award, 17 March 2006, ¶¶ 291-294 (“*Saluka – Partial Award*”) (Tab 123).

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5. **The Minimum Standard of Treatment Under Custom Has Not Converged with the Stand-Alone FET Standard Under Some BITs**

166. Recognising that decisions to which it refers are based on different stand-alone FET clauses, the Investor claims that the minimum standard of treatment under customary law has “converged” with the stand-alone FET standard found in some BITs. What the Investor really means to say is that custom has evolved “upwards” so as to provide foreign investors with exactly the same level of protection as provided by BITs containing a stand-alone FET clause. The “convergence” thesis must be rejected.

167. In 2001, the Parties’ issued the Note to clarify that the scope of Article 1105 must be limited to rules of custom regarding the treatment of aliens. In other words, that it was not a stand-alone standard. As explained by the *Mondev* Tribunal, for the Parties the terms “fair and equitable treatment” was a reference to “*existing elements* of the customary international law standard and [is] *not intended to add novel elements* to that standard.”<sup>147</sup> Differences in the standard at custom and the stand-alone standard still exist to this day.

168. The Investor has not proved its claim that custom has somehow evolved “upwards” so as to converge with the stand-alone FET standard. The Investor must show that such an evolution took place *since 2001* (when the Note was issued). This is an extraordinarily short period of time for the emergence of a new and higher standard. It is not surprising then that the Investor has not been able to provide a single example of state

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<sup>147</sup> *Mondev – Award*, ¶ 122 (emphasis added) (Tab 87).

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practice to support its claim. Worse, a 2007 UNCTAD report expressed doubt that such an evolution has occurred,<sup>148</sup> and this view is echoed by a number of authors.<sup>149</sup>

169. The Investor's reference to the *CMS Gas* award in this connection is yet another attempt to conceal inconvenient portions of a passage. The full passage of the award reads as follows:

While the choice between requiring a higher treaty standard and that of equating it with the international minimum standard *might have relevance in the context of some disputes*, the Tribunal is not persuaded that it is relevant *in this case*. In fact, the Treaty standard of fair and equitable treatment and its connection with the required stability and predictability of the business environment, founded on solemn legal and contractual commitments, is not different from the international law minimum standard and its evolution under customary law.<sup>150</sup>

170. Clearly the Tribunal's intention in this case was *not* to enunciate a *general proposition* equating the minimum standard of treatment under custom with the one

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<sup>148</sup> UNCTAD, *Investor-State Dispute Settlement and Impact on Investment Rulemaking*, UN Doc. UNCTAD/ITE/IIA/2007/3 (2007) at 75 (“UNCTAD – Investor State Rulemaking”) (Tab 142): “The inclusion of language clarifying the content and scope of the minimum standard of treatment in new [international investment agreements] may be particularly relevant to counterbalance two recent trends in [investor–State dispute settlement] practice. First, the clarification concerning the meaning of customary international law included in, for example, Annex A of the Australia–United States FTA is important for providing guidance as to how to interpret the fair and equitable treatment standard properly. *Some recent arbitration panels have granted themselves a certain degree of freedom in this respect*. Given the evolutionary nature of customary international law, the content of the fair and equitable treatment standard no longer requires bad faith or “outrageous” behaviour on behalf of the host country. *By eliminating these requirements, some arbitral decisions had the effect of equating the minimum standard under customary international law with the plain meaning approach to the text*. However, it is not self-evident that customary international law has evolved to such a degree.” (emphasis added).

<sup>149</sup> Kill, Theodore, “*Don’t Cross the Streams: Past and Present Overstatement of Customary International Law in Connection with Conventional Fair and Equitable Treatment Obligations*”, 106 Michigan Law Review, at 853, at 857-858 (“Kill”) (Tab 173); Van Harten, Gus, “*Investment Treaty Arbitration and Public Law*”, (Oxford, 2007), at 89 (“Van Harten”) (Tab 176).

<sup>150</sup> *CMS – Final Award*, ¶ 284 (emphasis added) (Tab 28).

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existing under BITs. Rather, the Tribunal stated that *under the circumstances of the case at hand*, the distinctions between the two standards were immaterial. In doing so, the Tribunal also acknowledged that such a distinction exists and that it may be relevant in other cases.<sup>151</sup> This passage therefore does not support any general “convergence” argument in the context of NAFTA.

**6. The Investor Must Prove a Breach of Customary International Law**

171. The Tribunal’s analysis of any allegation of breach of Article 1105 must begin and end with an assessment of whether the Investor has established a violation of a crystallized rule of customary international law regarding the treatment of aliens. The Investor has failed to meet its burden of demonstrating that the standards referred to in its Reply<sup>152</sup> are part of the customary international law minimum standard of treatment.<sup>153</sup>

172. That does not mean, contrary to what the Investor suggests, that Canada believes Article 1105(1) to be “virtually devoid of any content at all.”<sup>154</sup> For instance, denial of justice is clearly part of the minimum standard of treatment under custom. In any event,

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<sup>151</sup> In fact, in the same section the Tribunal made express reference to the specific situation under NAFTA: “The Tribunal is mindful of the discussion prompted by these arguments, particularly with reference to the NAFTA Free Trade Commission’s Note of Interpretation identifying fair and equitable standard with that of customary international law. This development has led to further treaty clarification as in the Chile-United States Free Trade Agreement.” (*Id.*, ¶ 283) (Tab 28).

<sup>152</sup> The obligations of fairness and good-faith; treatment free from arbitrary and discriminatory conduct; the obligation to fulfil the Investor’s legitimate expectations; the obligation of transparency; the obligation to provide a secure legal environment; and the obligation to prevent abuse of rights (*Investor’s Memorial*, ¶ 198).

<sup>153</sup> *Investor’s Reply*, ¶ 321.

<sup>154</sup> *Id.*, ¶ 323. The Investor is therefore completely wrong when it argues that “[i]f Canada’s approach were to be followed, there would be no effective protection for rule of law and fundamental fairness issues within the NAFTA” (*Investor’s Reply*, ¶ 14).



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even if this Tribunal were to conclude that under custom Canada is required to “act in a non-arbitrary manner,”<sup>155</sup> it still remains to be determined whether the alleged acts or omissions exceed the *high threshold* set by international law for breach of the minimum standard of treatment.

173. Such a high threshold has been repeatedly affirmed by NAFTA tribunals.<sup>156</sup> As explained by the *S.D. Myers* Tribunal, a breach “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*.”<sup>157</sup> In other words, “arbitrary” conduct needs to be “grave enough to shock a sense of judicial propriety” in order to “give rise to a breach of the minimum standard of treatment.”<sup>158</sup>

174. The assessment must be global in scope, taking into account all the relevant circumstance of the case.<sup>159</sup> For instance, an isolated instance of arbitrary conduct does not constitute a breach of Article 1105 *per se*, only “manifestly arbitrary or unfair”

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<sup>155</sup> *Id.*, ¶ 321.

<sup>156</sup> For instance, recently the *Thunderbird* Tribunal observed that under NAFTA “the threshold for finding a violation of the minimum standard of treatment still remains high.” *International Thunderbird Gaming Corporation v. Mexico* (UNCITRAL), Arbitral Award, 26 January 2006 (“*Thunderbird – Award*”), ¶ 194 (Tab 136).

<sup>157</sup> *S.D. Myers Inc. v. Canada* (UNCITRAL), First Partial Award, 13 November 2000 (“*S.D. Myers – First Partial Award*”), ¶ 263 (emphasis added) (Tab 120).

<sup>158</sup> *Thunderbird – Award*, ¶ 200 (Tab 136).

<sup>159</sup> *GAMI – Award*, at ¶ 103: “the record as a whole – not dramatic incidents in isolation – which determines whether a breach of international law has occurred.” (Tab 54).

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conduct does.<sup>160</sup> In other words, it must be shown that the conduct, in general, is “wholly arbitrary” or “in a way that [is] grossly unfair.”<sup>161</sup>

175. Canada will demonstrate in the next section that none of the administrative irregularities cited by the Investor have reached the high threshold necessary to constitute a breach of Article 1105.

### **C. The Regime Does Not Violate Article 1105(1)**

#### **1. Introduction**

176. In its Reply, the Investor repeats the various complaints set out in its Memorial. It reiterates that the Regime is non-transparent and arbitrary. It also renews its objection to “blockmailing.” However, the Investor has not been able to provide any examples of the latter, aside from the *single incident* already mentioned in its Memorial.

177. The Investor has now dropped its dubious claim that the Regime breaches its “legitimate expectations” and that it constitutes an abuse of rights.<sup>162</sup> Instead, these allegations have been replaced by a plethora of trivial accusations that clearly would not rise to the level of a breach of Article 1105 even if they were true. For instance, the Investor now claims that the “federal Government is not legally limited from granting standing exemptions” and that doing so is a “political choice,”<sup>163</sup> yet it does not explain

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<sup>160</sup> *Thunderbird – Award*, ¶ 197 (Tab 136).

<sup>161</sup> *Waste Management II Inc. v. Mexico* (ICSID No. ARB(AF)00/3) Award, 30 April 2004 (“*Waste Management II – Award*”), at ¶ 115 (Tab 157).

<sup>162</sup> *Investor’s Memorial*, ¶ 352.

<sup>163</sup> *Investor’s Reply*, ¶ 368.

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why this constitutes a breach of the minimum standard of treatment of aliens under customary international law. The Investor also makes a series of new allegations: that the Regime “discriminates against log producers in favour of log processors”,<sup>164</sup> that it “discriminates against federal and coastal log producers in favour of provincial and interior log producers”,<sup>165</sup> and that it also “discriminates against provincial log producers.”<sup>166</sup> The Investor does not explain how these different instances of “discrimination” are capable of constituting a breach of Article 1105.

## 2. The Regime is Transparent and Not Arbitrary

178. In its Reply, the Investor complains that the Regime is “administered in a highly secretive and non-transparent manner that flies in the face of the most fundamental aspects of the rule of law”<sup>167</sup> and even raises “serious questions about the natural justice and due process” of the Regime.<sup>168</sup> In fact, despite the sense of outrage, the bulk of its complaint on Article 1105 is now reduced to rather trivial irritants. The petty nature of these alleged irregularities is clear from the list of the Investor’s latest grounds of complaint:

- Despite evidence to the contrary, the Investor still complains that no private landowners have been invited to be a member of FTEAC and that it is never consulted on the selection of new members;

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<sup>164</sup> *Id.*, ¶ 375.

<sup>165</sup> *Id.*, ¶ 385.

<sup>166</sup> *Id.*, ¶ 392.

<sup>167</sup> *Id.*, ¶ 16.

<sup>168</sup> *Id.*, ¶ 18.

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- Faced with solid documentary evidence showing that FTEAC is implementing strict guidelines to prevent any situations of conflict of interest for its members, the Investor now suggests that these documents may not be reliable;
- The Investor complains about *one* cancelled FTEAC meeting out of more than one hundred, even though this cancellation had no effect on the Investor;
- The Investor complains that FTEAC’s practice to consider an offer as fair market value whenever it closely matches (+/- 5%) the prevailing domestic market price is too “subjective”;
- Backtracking from its initial false statement that it had never been allowed to make any “submissions” to TEAC/FTEAC regarding the fairness of offers being made on its logs, the Investor now raises concern that it cannot make any “oral submissions.” This, despite never having asked to make such submissions in the first place;
- The Investor complains that it does not know the relevant factors to be addressed when asking the Minister to disregard an FTEAC recommendation; yet documentary evidence shows that it knows exactly what these factors are and has been successful in using them; and
- The Investor complains that the concept of “remote” areas is unclear, but fails to prove that such (alleged) “uncertainty” had any effect on its business.

179. Canada will demonstrate that these alleged administrative irregularities, taken separately or collectively, do not breach Article 1105(1).

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**a) Private Landowners Have Been Invited to Join TEAC/FTEAC and the Investor Has Been Consulted on the Matter**

180. In its Memorial, the Investor stated that “[t]here has never been anyone on FTEAC with any significant private federal landholdings.”<sup>169</sup> In his first Affidavit, Mr. Cook points to several documented examples in which FTEAC sought candidates from private landowners, who declined.<sup>170</sup> The Investor repeats its claim in its Reply that “[n]o private log producers are *permitted* to sit on this body.”<sup>171</sup> The Investor knows that this is not accurate and that no rule prohibits them from sitting on FTEAC. Indeed, a current TEAC member once represented a company with significant private land interests in the B.C. Interior.<sup>172</sup>

181. In its Reply, the Investor also continues to assert that FTEAC has never consulted with private landowners about the appointment of committee members.<sup>173</sup> This is false. Mr. Cook explained in his first Affidavit that he has personally consulted with private stakeholders, including Merrill & Ring, on FTEAC membership.<sup>174</sup> For example, he discussed the nomination of a private landowner [REDACTED] to FTEAC with Ms.

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<sup>169</sup> *Investor’s Memorial*, ¶ 123.

<sup>170</sup> *Cook Affidavit*, ¶¶ 47-48.

<sup>171</sup> *Investor’s Reply*, ¶ 18 (emphasis added).

<sup>172</sup> *Cook Supplemental Affidavit*, ¶ 18.

<sup>173</sup> *Investor’s Reply*, ¶ 355.

<sup>174</sup> *Cook Affidavit*, ¶ 49; *Cook Supplemental Affidavit*, ¶¶ 16-17.

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██ who informed him that Merrill & Ring supported the nomination.<sup>175</sup>

**b) TEAC/FTEAC Have Appropriate Conflict of Interest Procedures**

182. In its Reply, the Investor states that FTEAC “has no guidelines on conflict of interest”<sup>176</sup> and that “[t]he lack of criteria for selecting TEAC/FTEAC members is also the reason why no proposed member of TEAC/FTEAC has ever been excluded on the basis of conflict of interest.”<sup>177</sup> These allegations are misguided for a number of reasons.

183. First, conflicts of interest are almost never an issue at the selection stage because individuals with too many potential conflicts of interest are simply never nominated.<sup>178</sup> TEAC/FTEAC members are not meant to act as “agents” or “representatives” of companies for whom they presently work or have worked for in the past. They are appointed because of their experience and knowledge of the industry.

184. Second, TEAC/FTEAC does, in fact, have procedural guidelines to deal effectively with conflicts of interest that arise in the normal course of business. While these guidelines are not documented, it remains true that they are known and understood by all FTEAC members.<sup>179</sup> The TEAC/FTEAC minutes demonstrate that they are respected in practice. As already explained by Mr. Cook, whenever a TEAC/FTEAC

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<sup>175</sup> *Cook Affidavit*, ¶ 49.

<sup>176</sup> *Investor’s Reply*, ¶ 356.

<sup>177</sup> *Id.*, ¶ 355.

<sup>178</sup> *Cook Affidavit*, ¶ 41.

<sup>179</sup> *Cook Supplemental Affidavit*, ¶ 11.

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member has any kind of business relationship with the company advertising its logs or the sawmill making an offer, the member will invariably be asked to leave the meeting before any discussion takes place. The member will be invited back into the room only after the end of the discussion on this matter.<sup>180</sup> This is not a “self-serving” explanation. This procedure was explained by Mr. McCutcheon, the chairman of FTEAC, in his testimony to the Federal Court of Canada in *TimberWest v. Canada*.<sup>181</sup>

185. In his first Affidavit, Mr. Cook refers to several documented instances in which these procedures were put into practice.<sup>182</sup> For example, the minutes of meeting no. 267 of November 13, 2003 show that “John J. McCutcheon relinquished the chair and excused himself from the meeting citing possible conflict of interest.”<sup>183</sup> Faced with such undisputable documentary evidence, the Investor is left making the outrageous accusation that nothing proves that the Minutes are actually telling the truth.<sup>184</sup>

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<sup>180</sup> *Cook Affidavit*, ¶ 42; *Cook Supplemental Affidavit*, ¶ 13.

<sup>181</sup> *TimberWest v. Canada*, excerpt from the Cross-Examination Transcript of the Proceedings before Justice O’Keefe, *TimberWest Forest Corp. v. Her Majesty the Queen, in Right of Canada*, 2007 FC 148, testimony of John McCutcheon (“*Timberwest – Transcript*”), at 745-757 (Tab 137).

<sup>182</sup> *Cook Affidavit*, ¶¶ 43-44. See also *Cook Supplemental Affidavit*, ¶ 13 for another example.

<sup>183</sup> *Cook Affidavit*, Exhibit 19.

<sup>184</sup> Thus, the Investor argues that “[t]here is also no way to verify whether conflicted members actually excuse themselves from the meetings *at the appropriate times*.” (*Investor’s Reply*, ¶ 357, emphasis added).

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**c) TEAC/FTEAC Meetings Are Not Arbitrarily Cancelled**

186. In its Memorial, the Investor complained that “TEAC/FTEAC is prone to cancelling meetings without prior notice.”<sup>185</sup> Again, this is a gross exaggeration.

187. In her Affidavit, Ms. Korecky explains that only *three* meetings have been cancelled in ten (10) years.<sup>186</sup> What is more, in only in one of these cases was consideration of offers delayed. The August 2006 meeting was cancelled for lack of quorum, and consideration of the outstanding offers was deffered to the following month.<sup>187</sup> Although the September 2003 meeting was technically cancelled, its business was nevertheless dealt with by means of survey questionnaire sent to committee members.<sup>188</sup> One of the Investor’s own booms was declared surplus in this way, meaning that the cancellation of this meeting had no effect on the Investor.<sup>189</sup> Finally, while a meeting was cancelled in November 2007, this was because there were no offers to consider.

188. Thus, in reality, the Investor’s complaint consists of a single cancelled meeting (August 2006) in more than ten (10) years. This is hardly the stuff of “erratic behaviour”

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<sup>185</sup> *Investor’s Memorial*, ¶ 353(g). It also alleged (*Id.*, ¶ 155) that “it will sometimes cancel meetings arbitrarily and without notice, creating unexpected delays.”

<sup>186</sup> *Korecky Affidavit*, ¶ 179.

<sup>187</sup> *Korecky Supplemental Affidavit*, ¶¶ 15-16.

<sup>188</sup> *Id.*, ¶ 15.

<sup>189</sup> *Id.*, ¶ 15. Indeed, Merrill & Ring did not even apply for an export permit for its surplus boom.



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leading to “uncertainty [in] the business environment.”<sup>190</sup> The fact is that the Investor has suffered no prejudice whatsoever as a result of meeting cancellations.

**d) FTEAC Uses Concrete Criteria to Make Recommendations**

189. In its Memorial, the Investor alleges that FTEAC “makes its decisions based on subjective judgment, and employs loosely formulated criteria to determine if an offer is ‘fair’.”<sup>191</sup> In its Reply, the Investor again complains that it is “unable to ascertain in any detail the basis upon which TEAC/FTEAC makes its decisions.”<sup>192</sup>

190. Canada must first reiterate that FTEAC does not render “decisions”; it only makes “recommendations” to the Minister. Second, as Canada has already explained, *Notice 102* sets out the standard to determine whether an offer is valid.<sup>193</sup> The basic criterion is whether an offer is fair in light of the market price for logs of a similar type and quality in the domestic market (the “fair market value criterion”). The general practice adopted by FTEAC is that an offer is considered fair market value whenever it closely matches (+/- 5%) the prevailing domestic market price.<sup>194</sup> The Investor, which has been operating under *Notice 102* for some 10 years, knows these criteria. While Mr. Stutesman, in his second affidavit, states that he only “learned over the course of these proceedings” about this 5% margin practice,<sup>195</sup> this contradicts the first affidavit of Mr. Kurucz, in which he

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<sup>190</sup> *Investor’s Reply*, ¶ 352.

<sup>191</sup> *Investor’s Memorial*, ¶ 353(e).

<sup>192</sup> *Investor’s Reply*, ¶ 353.

<sup>193</sup> *Notice 102*, section 4.4 (Tab 101).

<sup>194</sup> *Korecky Affidavit*, ¶ 101.

<sup>195</sup> *Stutesman Reply Witness Statement*, ¶ 13.

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explicitly refers to the 5% guideline.<sup>196</sup> What is more, the Investor's Memorial itself refers to a prior instance in which Merrill & Ring was informed of this practice.<sup>197</sup>

191. The Investor argues that the 5% range is overly broad and leads to “subjective judgements.”<sup>198</sup> The “subjective” element that the Investor complains about allows FTEAC a certain degree flexibility which prevents unfair results. Thus, FTEAC's recommendations take into consideration other important factors about the ‘fairness’ of any given offer, such as weather conditions and the location of logs, which both affect transportation costs. In her first Affidavit, Ms. Korecky provided a concrete illustration of how such factors are used in practice to mitigate unfair results.<sup>199</sup> The “subjectivity” complained about by the Investor is ultimately beneficial to protect its own interests.

**e) The Investor Frequently Makes Submissions  
Concerning Offers Made on its Logs**

192. In its Memorial, the Investor complained that it “has *never* been allowed to make submissions regarding the ‘fairness’ of offers made on its logs to TEAC/FTEAC.”<sup>200</sup> In

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<sup>196</sup> *Kurucz Witness Statement*, ¶ 51: “I asked John Cook, a member of FTEAC, how it could justify this decision. He told me that as long as the price was somewhere within 5% of the current domestic market value – even if it is 5% below current domestic market value –that is good enough for FTEAC to approve the offer and deny the export application.”

<sup>197</sup> *Investor's Memorial*, ¶ 126: “On one occasion, one of [TEAC/FTEAC] members advised that as long as the offer price is within 5% of the domestic market value, that would merit TEAC's/FTEAC's acceptance of the offer.”

<sup>198</sup> *Investor's Reply*, ¶ 353.

<sup>199</sup> *Korecky Affidavit*, ¶ 113, Exhibit 76.

<sup>200</sup> *Investor's Memorial*, ¶ 353(f) (emphasis added).

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its Counter-Memorial, Canada demonstrated that this is false.<sup>201</sup> The Investor has made numerous submissions to FTEAC and DFAIT regarding the fairness of offers made on its logs. In her first Affidavit, Ms. Korecky provided documentary evidence that such submissions had been made.<sup>202</sup> She also pointed to several instances where the Investor had *successfully* argued to FTEAC that an offer made on its logs should be rejected.<sup>203</sup>

193. Faced with such evidence, in his latest Witness Statement, Mr. Stutesman now admits that “it is true that we have on occasion been able to convince the [Minister] to disregard an FTEAC determination.”<sup>204</sup> The Reply now merely complains of not being allowed to make “oral” submissions to FTEAC.<sup>205</sup>

194. However, as explained by Ms. Korecky in her second Affidavit, the Investor has *never* asked to make such oral submissions.<sup>206</sup> To protect business-confidential information, FTEAC meetings are, in principle, not open to the public.<sup>207</sup> In any event, given that FTEAC is not a decision-making body there is no reason why it should allow

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<sup>201</sup> *Canada's Counter-Memorial*, ¶ 606 *et seq.* Soon after *Notice 102* came into force DFAIT sent a letter to the Investor explaining the regime and specifically inviting it to make submissions on the fairness of offers. See *Korecky Affidavit*, ¶ 126, Exhibit 43.

<sup>202</sup> *Korecky Affidavit*, ¶ 136. One example, amongst many, is the letter of June 6, 2006 sent by Mr. Stutesman to Ms. Korecky (*Id.*, Exhibit 51).

<sup>203</sup> *Id.*, ¶ 137. One illustration is a letter sent by the Investor to FTEAC on January 8, 2008 concerning an offer made by ██████████ on its logs in which it “requested” that the offer be rejected and the boom declared surplus (*Id.*, Exhibit 53). On January 11, 2008, FTEAC agreed with the Investor’s assessment and recommended that the logs be deemed surplus because the offer was below the fair market value (*Id.*, Exhibit 79).

<sup>204</sup> *Stutesman Reply Witness Statement*, ¶ 9.

<sup>205</sup> *Investor's Reply*, ¶ 351.

<sup>206</sup> *Korecky Supplemental Affidavit*, ¶ 20.

<sup>207</sup> *Id.*, ¶ 18.

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oral submissions. DFAIT has nevertheless allowed log producers to make oral submissions to FTEAC when asked to do so.<sup>208</sup> For instance, Ms. Korecky in her second Affidavit explains that [REDACTED] made a presentation at the April 4, 2008 FTEAC meeting.<sup>209</sup> The Investor could have asked to present orally, but it did not. This is truly a trivial ground of complaint.

**f) The Minister Does Not Rubber-Stamp TEAC/FTEAC Recommendations**

195. In its Memorial, the Investor complained that “TEAC/FTEAC recommendations are almost invariably accepted by BCMoF and DFAIT.”<sup>210</sup> This is not accurate. The Minister does not “rubber-stamp”<sup>211</sup> TEAC/FTEAC recommendations. Pursuant to *Notice 102*, such recommendations are only *one factor* to be considered by the Minister when making his/her decision on whether to issue an export permit.<sup>212</sup> As Ms. Korecky explained in her first affidavit, other factors are also relevant.<sup>213</sup> In its Counter-Memorial, Canada provided several examples of instances where the Minister disregarded FTEAC

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<sup>208</sup> *Id.*, ¶ 19.

<sup>209</sup> *Id.*, ¶ 19.

<sup>210</sup> *Investor’s Memorial*, ¶ 353(f).

<sup>211</sup> *Id.*, ¶ 113.

<sup>212</sup> *Notice 102* states that the Minister “will review the FTEAC recommendation and other relevant factors in determining whether or not adequate supply exists.” *Notice 102*, ¶ 4.4(a) (Tab 101).

<sup>213</sup> *Korecky Affidavit*, ¶ 150. Ms. Korecky explains that these other factors include the price of offers, and, more generally, the interests of all domestic log processors in Canada. The Minister will also consider and examine other booms advertised during a given period of time, the number and nature of offers made by offering companies and any offers made. Any concerns expressed by log exporters about “blockmailing” practices are also taken into account by the Minister in his/her final decision.

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recommendations based on such other relevant factors.<sup>214</sup> Some of these cases involved the Investor.<sup>215</sup>

196. In its Reply, the Investor persists in claiming not to know anything about such factors.<sup>216</sup> Yet, out of all the log producers to have advertised on the Bi-Weekly list, the Investor has, proportionally, challenged the greatest number of FTEAC determinations.<sup>217</sup>

197. The Investor's knowledge of the process and of the relevant factors is evidenced by its letter of July 30, 1998 to DFAIT. In it, the Investor explained why several offers made by two different companies [REDACTED] on its logs should be rejected by FTEAC.<sup>218</sup> Mr. Stutesman lists a number of reasons why the Investor's logs should be granted surplus status: there was no shortage of supply of timber in the industry; [REDACTED] had sufficient inventory to operate its sawmill at full capacity; the price offered on the logs was below fair market value; the cost of transporting the logs was high; and Merrill & Ring was being discriminated against.<sup>219</sup> These are exactly the type of factors that are considered relevant by the Minister when deciding whether to grant surplus status. In this case, as a result of Mr. Stutesman's letter, FTEAC's recommendation was not accepted by the Minister. Very little weight should therefore be given to his latest assertion that, because these factors are unknown to him, it is "very

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<sup>214</sup> *Canada's Counter-Memorial*, ¶¶ 619-622.

<sup>215</sup> *Id.*, ¶¶ 619-622.

<sup>216</sup> *Investor's Reply*, ¶ 359.

<sup>217</sup> *Korecky Affidavit*, ¶¶ 127, 132.

<sup>218</sup> *Korecky Affidavit*, Exhibit 45.

<sup>219</sup> *Id.*, Exhibit 46. In this case, DFAIT was convinced by the arguments advanced by Mr. Stutesman and recommended that the Minister disregard the offer made on the Investor's logs.

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difficult for [the Investor] to make [its] case.”<sup>220</sup> Mr. Stutesman is not the neophyte amateur he pretends to be.

198. Moreover, the Minister’s decision can be challenged. The Investor fails to mention its right to seek judicial review of a final decision taken by the Minister under the *Export and Import Permits Act* pursuant to s.18.1 of the *Federal Court Act*.<sup>221</sup> Among the grounds of review that may be brought to the Federal Court of Canada are that the decision at issue was without jurisdiction, contrary to procedural fairness, an error of law, an error of fact or otherwise contrary to law. As mentioned in Canada’s Counter-Memorial,<sup>222</sup> such judicial review has been taken on three occasions in the past by log companies. One recent Federal Court decision, rendered on December 17, 2008, in the Case of *Island Timberland LP v. The Ministry of Foreign Affairs* was brought to the Tribunal’s attention by the Investor. In that case, Justice Campbell set aside the Minister’s decision rejecting one of that company’s applications for log export.<sup>223</sup> This case shows that there is ample opportunity before Canadian courts to *successfully* challenge a Minister’s permit decision.

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<sup>220</sup> *Stutesman Reply Statement*, ¶ 10.

<sup>221</sup> The Federal Court has jurisdiction “(a) to issue an injunction, writ of *certiorari*, writ of prohibition, writ of *mandamus* or writ of *quo warranto*, or grant declaratory relief, against any federal board, commission or other tribunal” and “(b) to hear and determine any application or other proceeding for relief in the nature of relief contemplated by paragraph (a), including any proceeding brought against the Attorney General of Canada, to obtain relief against a federal board, commission or other tribunal.” *Federal Court Act*, R.S., 1985, c. F-7 (“*FCA*”) (Tab 169).

<sup>222</sup> *Canada’s Counter-Memorial*, ¶ 627.

<sup>223</sup> *Island Timberland LP v. The Ministry of Foreign Affairs*, Reasons for Order and Order, 17 December 2008 (“*Island Timberland - Order*”) (Tab 172).

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**g) The Concept of “Remoteness” Is Well-Defined and Known to All Log Exporters**

199. In its Memorial, the Investor complained that the concept of “remote” areas, referred to in *Notice 102*, is nowhere specified and that no rules concerning this issue have been made publicly available. The Investor alleges that these factors make *Notice 102* “non-transparent” because it is - supposedly - difficult for log producers to ascertain whether their lands are considered remote or not.<sup>224</sup>

200. As Canada explained in its Counter-Memorial, the requirement to advertise a minimum volume in remote areas is clear and well-understood by industry players as set out in the still-applicable TEAC policy document dated December 5, 1986.<sup>225</sup> Thus, an area is generally considered remote if it is more than six (6) hours driving time or more than two hours flying time from Vancouver.<sup>226</sup> Canada has explained the reason for its policy of requiring minimum volumes of 2,800 m<sup>3</sup> to advertise from remote areas.<sup>227</sup> In the vast majority of instances, this policy is applied with little difficulty, and the Investor has never challenged or complained of the manner in which it was applied.

201. In his second Witness Statement, Mr. Kurucz, the Investor’s log broker, claims to have obtained a determination by telephone from BCMoF—at some unspecified date in 1999—that the status of Theodosia Inlet was “remote.”<sup>228</sup> He also claims that the Investor

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<sup>224</sup> *Investor’s Memorial*, ¶ 354(a).

<sup>225</sup> *Cook Affidavit*, Exhibit 28.

<sup>226</sup> *Cook Affidavit*, ¶¶ 76-81. In the *Investor’s Reply*, ¶ 364, the Investor plays with words and selectively quotes the Cook and Korecky Affidavits to make it seem as though the policy is unclear and that they apparently contradict each other. In fact, both Affidavits are perfectly consistent.

<sup>227</sup> *Cook Affidavit*, ¶¶ 78-80.

<sup>228</sup> *Kurucz Reply Witness Statement*, ¶ 8 *et seq.*

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has been operating under the assumption that these lands were considered “remote” for the last ten years. The individual involved, [REDACTED], does not recall the conversation in question. However, if such an opinion was given, it was mistaken. Mr. Cook explained in his second Affidavit that Theodosia Inlet is not, in fact, considered remote by TEAC/FTEAC and that no minimum volume requirement applies to log exports from that area.<sup>229</sup>

202. The Investor notes that, because it believed Theodosia Inlet to be “remote”, it was forced to tow its logs to a non-remote location to be advertised whenever it did not meet the minimum volume requirement. It argues that “[i]f it is true that Theodosia is *not* considered ‘remote’, the blame for the damage this has caused should not fall on Merrill & Ring.”<sup>230</sup> However, as explained by Mr. Cook, the minimum volume requirement imposes no additional burden on the Investor’s business.<sup>231</sup> As a log exporter, the Investor would in any event be required to tow its booms to the Fraser River at its own expense.<sup>232</sup> Bringing logs to a “non-remote” location to be advertised on the Bi-weekly list is but a small step in a much longer journey such logs would take in order to be exported. Moreover, since 2006, logs may be advertised while in transit from a remote location.

203. This helps explain why the Investor never once in *ten years* challenged the remote designation for Theodosia Inlet; it suffered no detriment. Other aspects of the Investor’s behaviour confirm this view. For example, the Investor notes that “remoteness” can

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<sup>229</sup> Cook Supplemental Affidavit, ¶¶ 36-37.

<sup>230</sup> Investor’s Reply, ¶ 366 (emphasis in the original).

<sup>231</sup> Cook Affidavit, ¶ 84.

<sup>232</sup> Cook Supplemental Affidavit, ¶ 40.



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fluctuate over a period of time.<sup>233</sup> If, as the Investor contends, operating from a “remote” location causes inconvenience or additional cost, given such fluctuations, a diligent businessperson would confirm periodically that its lands were still subject to the minimum volume requirement. The Investor did no such thing, suggesting the requirement troubled it very little.

204. In any case, it cannot seriously be argued that a single, unchallenged alleged misapplication of policy in the course of ten years amounts to a violation of the minimum standard of treatment of foreign investors under customary international law.

### 3. The Regime Is Not Wrongfully Discriminatory

205. In its Reply, the Investor makes a series of new allegations related to different types of “discrimination” it allegedly suffers: the Regime “discriminates against log producers in favour of log processors”,<sup>234</sup> it “discriminates against federal and coastal log producers in favour of provincial and interior log producers”,<sup>235</sup> and it also “discriminates against provincial log producers.”<sup>236</sup> The Investor’s position seems to be that every regulatory distinction is a form of discrimination prohibited by Article 1105. This cannot be.

206. In its Counter-Memorial, Canada explained that there is no stand-alone obligation prohibiting “discrimination” under Article 1105(1).<sup>237</sup> NAFTA Chapter Eleven includes a

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<sup>233</sup> *Investor’s Memorial*, ¶ 354(a).

<sup>234</sup> *Investor’s Reply*, ¶ 375.

<sup>235</sup> *Id.*, ¶ 385.

<sup>236</sup> *Id.*, ¶ 392.

<sup>237</sup> *Canada’s Counter-Memorial*, ¶¶ 501-506.

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comprehensive and specific legal regime governing nationality-based discrimination covered by Articles 1102 to 1104, not Article 1105(1). Thus, the *Methanex* Tribunal concluded that “the plain and natural meaning of the text of Article 1105 does not support the contention that the ‘minimum standard of treatment’ precludes governmental differentiations as between nationals and aliens.”<sup>238</sup> The Tribunal’s conclusion is clear: “the text of NAFTA indicates that the States parties explicitly excluded a rule of non-discrimination from Article 1105.”<sup>239</sup> The Investor’s series of allegations of “discrimination” under Article 1105 should therefore be dismissed.

#### 4. The Regime Provides Adequate Protection from “Blockmailing”

207. In its Memorial, the Investor accused Canada of not taking the “appropriate measures to discourage” the practice of “blockmailing” and even went so far as to claim that it “actively encourages and condones” such practice.<sup>240</sup> Canada explained in its Counter-Memorial that this was not the case.

208. At the outset, Canada rejects the use of the expression “blockmailing” by the Investor.<sup>241</sup> The Investor uses the term ambiguously and in such a way as to give a negative connotation to legitimate actions. On the one hand, the Investor uses this term to refer to any offer made on logs that are being advertised on the Bi-Weekly List. This can hardly be considered improper in the context of *Notice 102*. On the other hand, in its

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<sup>238</sup> *Methanex – Award*, Part IV-Chapter C, ¶ 14 (Tab 85).

<sup>239</sup> *Id.*, ¶ 25.

<sup>240</sup> *Investor’s Memorial*, ¶ 356(c); see also *Investor’s Reply* ¶¶ 350, 393.

<sup>241</sup> Canada will nevertheless use the expression “blockmailing” in this submission to facilitate the work of the Tribunal.

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Reply, the Investor seems to be complaining of what it considers non-*bona fide* offers.<sup>242</sup> For instance, Mr. Ringma explains that “domestic log processors are constantly *threatening* to ‘block’ our logs from exports.”<sup>243</sup> According to him, log processors are “threatening” log producers to make offers on advertised logs if they do not supply them with the logs they want.<sup>244</sup> In other words, “blocking” threats are used as a “bargaining chip” in negotiations for the supply of logs.<sup>245</sup> Canada will refer to these alleged actions as “blockmailing.”

209. Mr. Bustard, a market participant who has acted both as a seller and a buyer of logs, explains in his Affidavit that, in his view, the Investor does not accurately describe the situation.<sup>246</sup> Buyers simply contact sellers to express their interest in advertised logs. This gives sellers the opportunity to offer other replacement logs for sale instead. Both sides benefit from knowing what the other wants. These are merely negotiations between companies having different interests. There is no intimidation or wrongdoing.<sup>247</sup>

210. Further, despite the Investor’s efforts to create the impression that wrongdoing is at issue, the Investor has in fact only identified *a single* case of “blockmailing”, concerning ████████ booms.<sup>248</sup> By contrast, in the last 10 years, the Investor has advertised

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<sup>242</sup> *Schadendorf Witness Statement*, ¶ 9; *Investor’s Reply*, ¶394.

<sup>243</sup> *Ringma Witness Statement*, ¶ 8 (emphasis added).

<sup>244</sup> *Id.*

<sup>245</sup> *Kurucz Witness Statement*, ¶ 60.

<sup>246</sup> *Bustard Affidavit*, ¶¶ 16-24.

<sup>247</sup> *Ringma Witness Statement*, ¶ 11.

<sup>248</sup> *Investor’s Memorial*, Footnote 156.

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close to [REDACTED] parcels (or booms) on the Federal Bi-Weekly List.<sup>249</sup> The dearth of evidence on this point is impossible to reconcile with the Investor's accusation that "blockmailing" creates an insecure legal and business environment.<sup>250</sup>

211. It is not sufficient for Mr. Kurucz to vaguely refer to "one occasion" involving "a domestic processor that is known for its aggressive blockmailing and log blocking practices."<sup>251</sup> Given the language tossed about in the Investor's submissions, one would have expected it to support its claim with evidence and to provide the name of the company allegedly involved in this improper behaviour.

212. In any event, as explained in its Counter-Memorial, Canada is not responsible for the actions of private log companies, and it takes all necessary measures to prevent and sanction any wrong actions by private companies in relation to the surplus test.<sup>252</sup> These two points will be re-examined below.

**a) Canada Is Not Responsible for "Blockmailing" by Private Companies**

213. In its Reply, the Investor admits that "Canada does not engage in the practice of blockmail itself."<sup>253</sup> Mr. Ringma, the Investor's own witness, admits that Canada *does not endorse* the practice of "blockmailing."<sup>254</sup> For this reason alone, the Investor's claims

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<sup>249</sup> *Korecky Affidavit*, Exhibit 32; *Korecky Supplemental Affidavit*, ¶¶ 38-39, Exhibit 84.

<sup>250</sup> *Investor's Memorial*, ¶ 355.

<sup>251</sup> *Kurucz Witness Statement*, ¶ 66.

<sup>252</sup> *Korecky Affidavit*, ¶¶ 97, 120.

<sup>253</sup> *Investor's Reply*, ¶ 395.

<sup>254</sup> *Ringma Witness Statement*, ¶ 9.

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stemming from “blockmailing” by private log companies and other forms of “special targeting” by these companies should be dismissed. The Tribunal does not have jurisdiction over such claims as the measures are not attributable to Canada.

214. In its Reply, the Investor submits a novel argument as to why Canada should nevertheless be held responsible for private conduct of industry participants: “were it not for the Log Export Control Regime—a system that Canada cannot deny it is responsible for—blockmail would not be possible at all.”<sup>255</sup> The Investor provides an entertaining illustration: “Canada’s denial is analogous to the claims of a mastermind claiming he is innocent, since he was not the one who actually carried out the crime.”<sup>256</sup> This is a ridiculous analogy. Canada is not the “mastermind” of the “crime” of “blockmailing.”

**b) Canada Takes All Necessary Measures to Prevent and Discipline Any Wrongful Actions by Private Companies**

215. Canada’s policy is to do all it can to prevent any wrongful actions by private companies. DFAIT investigates such actions whenever it is actually raised by log exporters. Canada cannot investigate and address instances of alleged “blockmailing” which are not even reported by the Investor. It is not sufficient simply to say that “blockmailing” “commonly happens in vaguely worded discussions between the buyer and the seller”<sup>257</sup> and that such “deals are ‘under the table’, in the sense that government

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<sup>255</sup> *Investor’s Reply*, ¶ 395.

<sup>256</sup> *Id.*, ¶ 395.

<sup>257</sup> *Kurucz Witness Statement*, ¶ 61.

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does not usually know the specific terms.”<sup>258</sup> Those instances must be reported if Canada is to be expected to do anything about them.

216. Canada’s policy is well-illustrated by the only specific case of “blockmailing” referred to by the Investor in its Memorial. As explained by Ms. Korecky in her first Affidavit,<sup>259</sup> this is a case where FTEAC had initially considered [REDACTED] offers on the Investor’s log to be at fair market value, but where Ms. Korecky subsequently drafted a memorandum to the Minister indicating that he should take into account the element of “blockmailing” involved with these offers and reject them.<sup>260</sup> This example shows that whenever an allegation of “blockmailing” is actually raised by the Investor, it is properly addressed and resolved by DFAIT.<sup>261</sup>

217. In its Reply, the Investor alleges being the victim of “special targeting.”<sup>262</sup> “Targeting” is different from so-called “blockmailing.” The Investor alleges that TEAC/FTEAC “has never adopted any procedures or protocols to address this [targeting] problem.”<sup>263</sup> This is false. In her first Affidavit, Ms. Korecky explained that specific measures have been taken precisely to detect and prevent “targeting” by offering

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<sup>258</sup> *Id.*, ¶ 62.

<sup>259</sup> *Korecky Affidavit*, ¶ 135, Exhibits 49, 50.

<sup>260</sup> *Id.*, Exhibit 50. The summary of the recommendation to the Minister is straightforward: “[t]his note seeks your approval for the proposed export of five (5) booms of logs contrary to the recommendation of FTEAC that the proposed export be denied.”

<sup>261</sup> It should be noted that in the meantime, the offer had been withdrawn. The Minister therefore never had to render any decision in this case.

<sup>262</sup> For instance, the Investor alleges that “Merrill & Ring has been the subject of special targeting on many occasions.” (*Investor’s Reply*, ¶ 349).

<sup>263</sup> *Investor’s Reply*, ¶ 350.

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companies. Thus, whenever a review of all factors demonstrates that an exporting company is being unfairly targeted, the Minister will be advised to disregard a FTEAC recommendation and to declare the logs surplus.<sup>264</sup> Ms. Korecky also provided specific examples of cases in which Canada reprimanded companies involved in such practice against the Investor.<sup>265</sup>

218. In its Reply, the Investor admits that Canada takes disciplinary action against companies involved in targeting.<sup>266</sup> However, it complains that these disciplinary measures are “befogged by secrecy” and that “FTEAC will not even let the victim of an abuse know if, when, or on what basis it might take corrective measures.”<sup>267</sup> Whether corrective measures are made public or not, what matters is that Canada takes action to sanction log processors involved in disruptive behaviour. This puts an end to the behaviour and, in doing so, protects log producers such as Merrill & Ring.

#### 5. The Federal Government Has No Obligation to Grant Standing Exemptions

219. In its Memorial, the Investor complains that *Notice 102* does not provide for “economic” or “utilization” exemptions<sup>268</sup> from the surplus testing procedure, as does Part 10 of the B.C. *Forest Act*.<sup>269</sup> It argued that the differences between federal and provincial

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<sup>264</sup> *Korecky Affidavit*, ¶ 97.

<sup>265</sup> *Id.*, ¶ 97; see also, *Korecky Supplemental Affidavit* ¶ 22.

<sup>266</sup> *Investor’s Reply*, ¶ 361.

<sup>267</sup> *Id.*, ¶ 361.

<sup>268</sup> Otherwise known as “standing” exemptions because they are granted on standing timber.

<sup>269</sup> *Investor’s Memorial*, ¶ 353.

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rules on the matter were “unfair” and “arbitrary”<sup>270</sup> and that they constitute an “abuse of rights.”<sup>271</sup> In its Reply, the Investor added to this, saying that the federal government “refuses to assert its jurisdiction for political reasons” and that it “resiles from the exercise of the authority it rightfully has, deferring instead to the political sensitivities of the B.C. government.”<sup>272</sup> The Investor does not explain in any way how these accusations are in breach of the minimum standard of treatment of aliens under Article 1105.

220. In essence, the Investor is asking the Tribunal to evaluate the legitimacy and appropriateness of federal policy by comparing it to provincial (B.C.) policy. Each of these criticisms assumes or implies that the federal government is under some obligation to adopt rules and procedures that mirror provincial regulations relating to log exports. However, there is no basis for this assumption. The federal government is free to exercise its jurisdiction over log exports in any way it sees fit.

221. The Investor has identified no provision of NAFTA Chapter 11 requiring that the various levels of government in each State adopt matching laws and regulations. Nor could it, as this would contravene the express intentions of the Parties. The NAFTA treats the various levels of government as distinct from each other and expressly forbids comparing measures adopted by one sub-national government to those enacted by another.<sup>273</sup> This is hardly surprising. Each of the NAFTA Parties is a federal state. To allow such comparisons would be to impose a requirement of uniformity and homogeneity that is fundamentally at odds with the purpose of federalism. It would be

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<sup>270</sup> *Id.*, ¶ 353.

<sup>271</sup> *Id.*, ¶ 357.

<sup>272</sup> *Id.*, ¶ 368.

<sup>273</sup> See NAFTA Article 1102(3).



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absurd to conclude that the Parties intended the NAFTA to erode the very basis of their own constitutions in this way.

222. In any event, it is important to note that even applying the standards used by BCMoF in granting economic or utilization exemptions, none of the Investor's lands would probably not qualify for such treatment.<sup>274</sup> The Investor's lands do not suffer from the sort of economic hardship or ecological devastation used to justify standing exemptions under B.C. law.

**D. Conclusion**

223. The Investor has failed to identify any customary legal obligations with respect to treatment of aliens as required by Article 1105. The Investor also failed to demonstrate that any of the measures complained of, either individually or collectively, are “grave enough to shock a sense of judicial propriety and thus give rise to a breach of the minimum standard of treatment” under custom.<sup>275</sup> None of the various trivial allegations raised by the Investor demonstrate “a lack of due process leading to an outcome which offends judicial propriety” or “a complete lack of transparency and candour in an administrative process.”<sup>276</sup> These various (alleged) administrative irregularities are not “wholly arbitrary” or “grossly unfair” to reach the high threshold for breach of Article 1105.<sup>277</sup> The Investor's claim under Article 1105 should therefore be dismissed.

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<sup>274</sup> *Cook Supplemental Affidavit*, ¶¶ 19-23.

<sup>275</sup> *Thunderbird – Award*, ¶ 200 (Tab 136).

<sup>276</sup> *Waste Management II - Award*, ¶ 98 (Tab 157).

<sup>277</sup> *Id.*, ¶ 115.

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## V. THERE IS NO VIOLATION OF NAFTA ARTICLE 1106

### A. Summary of Canada's Position

224. The Investor's Article 1106 claim is not about performance requirements. There are no requirements imposed on the Investor. What the Investor complains of are incidental effects of the Regime.

225. Notwithstanding the Investor's continued effort to fit its claims into NAFTA breaches, Canada does not impose any requirements that fall under Article 1106(1) (a), (c) or (e.) The Investor admits that a breach of Article 1106 requires the Investor to demonstrate that Canada has imposed a requirement that "fits squarely" within the plain terms of Article 1106(1) and the relevant subparagraphs.<sup>278</sup> Canada agrees. However, there is no such requirement here.

- Canada does not require the Investor to export *any* good under Article 1106(1)(a) (even less so a "given level" of goods);
- Canada does not require the Investor to accord *any* preference under Article 1106(1)(c) to domestic goods or services provided in its territory; and
- Canada does not restrict *any* sales by the Investor in Canada under Article 1106(1) (e) (even less so by "relating such sales" to export volumes).

226. The Investor has not proven any breach of Article 1106 and its claim should be rejected.

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<sup>278</sup> *Investor's Reply*, ¶ 433.

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## B. The Regime Does Not Impose Performance Requirements

### 1. Canada Does Not Require the Investor to Export Anything

227. The Investor claims that “the remoteness rule requires it to advertise for export its logs in remote areas in minimum volumes of 2,800m<sup>3</sup> and maximum volume of 15,000m<sup>3</sup>.”<sup>279</sup> The Investor alleges that this violates Article 1106(1)(a) because Merrill & Ring is “compelled” to export a “given level” of goods.<sup>280</sup>

228. In advancing this claim, the Investor completely mischaracterises the volume requirements to advertise on the Federal Bi-Weekly List as a requirement to export a ‘given level’ of logs. There is no such requirement. The Regime does not require Merrill & Ring to export any logs at all. This basic factual inaccuracy is fatal to the Investor’s claim.

229. The Investor ultimately determines the level of exports it wishes to make after it complies with the advertisement requirements of the surplus test procedure. The volume requirements to advertise on the Bi-Weekly List (the so-called “remoteness rule”) does not relate to export volumes. Rather, it relates to the volumes of logs necessary to advertise in remote areas for the purpose of the surplus test.<sup>281</sup> Once it has advertised its logs on the Bi-Weekly List and they are deemed surplus, the Investor is free to apply for an export permit for however many of those surplus logs it wishes to export.<sup>282</sup> Further, even the logs granted an export permit do not have to be exported. As a matter of fact,

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<sup>279</sup> *Investor’s Reply*, ¶ 414.

<sup>280</sup> *Id.*, ¶ 415.

<sup>281</sup> Moreover, even this requirement can be avoided by towing logs to non-remote areas.

<sup>282</sup> *Cook Affidavit*, ¶ 82.

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Merrill & Ring did *not* export almost [REDACTED] of its logs that were granted an export permit.<sup>283</sup> The Regime, therefore, clearly imposes no requirement to export a “given level” of goods.

230. The Regime imposes absolutely no requirement on the Investor to export *any* goods, much less a “given level” of goods.

2. **Canada Does Not Require the Investor to Accord a Preference to Goods Produced in Canada**

231. The Investor argues that “since it is required to cut, sort, and scale its logs in accordance with the specifications laid out in the *Coast Domestic Market End Use Sort Description*, it is required to produce certain types of goods.”<sup>284</sup> The Investor also argues that the requirement to package its logs in accordance with the “remoteness rule” forces it to accord a preference to such goods. Here again the Investor contorts the sorting and advertising requirements that apply to its logs so that they “fit” within the terms of Article 1106(1)(c).

232. Article 1106(1)(c) prohibits a Party from imposing or enforcing a requirement “to purchase, use or accord a preference to goods produced ... in its territory, or to purchase goods ... from persons in its territory.” This subparagraph prohibits requirements to favour a domestic good (i.e. one produced in the territory of Canada) over a foreign good (i.e. one which is not produced in Canada). In other words, it aims to ensure that Investors are not required to use local inputs if they do not wish to.

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<sup>283</sup> *Canada's Counter-Memorial*, ¶ 704.

<sup>284</sup> *Investor's Reply*, ¶ 418.

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233. It goes without saying that the Investor's logs are all goods produced in Canada, and even in the absence of the Regime, Merrill & Ring would still be producing logs in Canada. This is because Merrill & Ring's lands are in Canada and not due to any requirement imposed by Canada. Moreover, to the extent that Merrill & Ring complains that there is a requirement to accord a preference to domestic goods, it is referring to its *own* logs.

234. A measure that may be challenged under 1106(1)(c) must force Merrill & Ring to favour local goods over foreign goods. The Regime imposes no such obligation.

**3. Canada Does Not Require the Investor to Accord a Preference to Services Provided in Canada**

235. Merrill & Ring complains that "if it were not required to cut, sort, and scale its logs in particular ways before being able to export its logs, it would not have to hire the services in Canada of those who perform these tasks."<sup>285</sup> The Investor further argues that it is required to hire the services of those who retrieve logs and to hire extra towing services as a result of the Regime.<sup>286</sup> The Investor contends that this violates Article 1106(1)(c). In other words, the Investor construes certain business *decisions* it takes in light of the existing regulatory framework as a *requirement* imposed by Canada. The Investor's interpretation of Article 1106(1) (c) is overly broad and ignores the purpose of the provision, as well as its express terms.

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<sup>285</sup> *Investor's Reply*, ¶ 421.

<sup>286</sup> *Id.*, ¶ 421.

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236. As Canada has explained, prohibitions on performance requirements are designed to prevent the host Party from distorting investment decisions in its favour.<sup>287</sup> Such requirements are typically imposed at the time of admission or approval of an investment. They are made in connection with an investment and are used as tools to balance trade, foster regional development or increase exports.<sup>288</sup> The cutting, sorting and scaling requirements do not constitute such performance requirements.

237. Article 1106 prohibits a limited number of performance requirements. The fact that “compulsion” is inherent to a “requirement” is not disputed between the parties to this case.<sup>289</sup> Article 1106(1) states that prohibited requirements are imposed “... *in connection with ... the conduct or operation of an investment of an investor ... in its territory*” (emphasis added). Thus, the link between the “requirement” and the “investment” has to be clear and direct. Incidental consequences of a regulatory regime cannot be considered “performance requirements” under Article 1106.

238. This interpretation was confirmed in *S.D. Myers*. The *S.D. Myers* Tribunal rejected the argument that, as a result of an export ban on PCBs, the Investor had to locate its production in Canada and use goods and services in Canada contrary to Article 1106(1)(b) and (c). The Tribunal determined that the export ban did not impose any “requirement” on the investor.<sup>290</sup> The implication is that *even if* the effect of the export ban was to “force” the Investor to have recourse to domestic remediation services in

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<sup>287</sup> See *Canada's Counter-Memorial*, ¶ 696.

<sup>288</sup> See *Canada's Counter-Memorial*, ¶ 694.

<sup>289</sup> *Id.*, ¶ 688; *Investor's Reply*, ¶ 406.

<sup>290</sup> *S.D. Myers - First Partial Award*, ¶¶ 270-277, in particular ¶ 277. In that case, the Investor was challenging a ban adopted by Canada on the export of PCB waste for disposal (Tab 120).

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order to continue its Canadian investment activities, it did not amount to a performance requirement under Article 1106(1) (c). The same reasoning applies here.

239. The fact that Merrill & Ring *may* hire services in Canada to sort, scale and tow its logs in order to comply with the surplus test does not make the regulations a performance requirement under Article 1106(1)(c). The rules do not impose any direct requirements on the investment to hire services in Canada. Rather, this is an incidental effect of the Regime. The sorting and scaling rules exist to promote uniformity and avoid distortions, not create them.

240. The Investor's allegations relating to towing and log retrieval are also incidental to the Regime and do not result from any requirement imposed on the investment. This is clearly demonstrated by the Investors' own pleadings,

While Merrill & Ring must necessarily tow its logs to some extent in Canadian waters, there is nothing natural about the fact that it is *required* to hire the services of towing contractors to a *greater extent than it otherwise would*. In a related way, while it is true that Merrill & Ring is naturally subject to the risk of having its booms break up in Canadian waters, there is nothing natural about being *compelled to assume more risk* than it needs.<sup>291</sup>

241. Furthermore, contrary to what the Investor alleges, the Regime does not “require Merrill & Ring to *hire services* that are provided in its territory full stop.”<sup>292</sup> No such requirement exists. The reality is that Merrill & Ring could choose to cut, sort, and scale its own logs. The Regime does not impose any requirements to “hire services” to perform those tasks. Rather, the Investor made a business decision to do so.

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<sup>291</sup> *Investor's Reply*, ¶ 424 (emphasis added).

<sup>292</sup> *Id.*, ¶ 425 (emphasis added).

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**4. Canada Does Not Require the Investor to Restrict Sales in its Territory in Any Way**

242. The Investor claims that it is required to advertise its remote logs in minimum volumes of 2,800m<sup>3</sup> and maximum volumes of 15,000m<sup>3</sup> and that such volumes are inextricably linked to the volume of Merrill & Ring's exports.<sup>293</sup> The Investor alleges that this violates Article 1106(1)(e).

243. Article 1106(1)(e) prohibits a Party from imposing or enforcing a requirement to "restrict sales of goods or services in its territory that such investment produces or provides by relating such sales in any way to the volume or value of its exports or foreign exchange earnings." The Investor's understanding of Article 1106(1)(e) is flawed: the provision relates to limitations on sales in Canada based on the volume of the Investor's exports. Nothing under the Regime restricts sales in Canada and links them to the Investor's exported volumes of logs. Just as it was determined by the *Pope & Talbot* Tribunal, Article 1106(1)(e) applies only when the requirement restrains domestic sales by linking *domestic and export sales*.<sup>294</sup> The Regime makes no such link.

**C. Conclusion**

244. The Investor has not proved a breach of Article 1106(1), nor could it. Canada does not impose any of the prohibited performance requirements alleged by Merrill & Ring. Specifically:

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<sup>293</sup> *Investor's Reply*, ¶ 426.

<sup>294</sup> *Pope & Talbot - Interim Award*, ¶ 79 (Tab 112).



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- The Regime does not require the Investor to achieve a given level of export;
- The Regime does not require the Investor to accord a preference to goods produced and services provided in Canada; and
- The Regime does not restrict sales of the Investor's goods in Canada by relating such sales to the volume of the Investor's exports.

245. Canada's log export controls simply do not fall within the scope of measures that may be challenged under Article 1106(1). The scope of the obligations under Articles 1106(1), (a), (c) and (e) cannot be broadened in the way suggested by the Investor, as this would amount to creating new performance requirements contrary to the express intention of the Parties. The Tribunal should, therefore, reject Merrill & Ring's claim under Article 1106.

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## VI. THERE IS NO VIOLATION OF NAFTA ARTICLE 1110

### A. Summary of Canada's Position

246. Merrill & Ring's investment, as a whole, has not been expropriated. The Investor does not deny this; nor could it. Canada has not deprived the Investor of its lands, logs or enterprise. Merrill & Ring has never lost control of its business operations. Faced with this reality, the Investor, in its Reply, attempts to convince the Tribunal that it is its "interest" in selling logs at fair market value on international markets that has been taken. Furthermore, it argues that its "interest" is the *only* investment the Tribunal should consider under Article 1110.

247. The Investor takes this position to get around the fact that nothing has been taken: there is no deprivation, let alone a substantial one. The Investor's attempt to narrowly define its investment so as to ensure a finding of expropriation does not find support in international law, renders the substantial deprivation test meaningless and should be rejected. Canada will demonstrate that:

- Merrill & Ring's "interest" in selling logs at fair market value on international markets is not, on its own, an investment under Article 1139 capable of being expropriated
- When considered as a whole, Merrill & Ring's investment has not been expropriated.

248. Since no expropriation has taken place, it is unnecessary to consider whether Canada has met the conditions of Article 1110(1)(a)-(d).

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**B. The Investor’s Alleged Interest in Selling its Logs at Fair Market Value on International Markets Is Not a Stand-Alone Investment Capable of Being Expropriated**

249. Under NAFTA, only investments as defined under Article 1139 benefit from the protection of Section A of Chapter 11, including protection against expropriation without compensation. In its Reply, the Investor argues that Merrill & Ring’s interest in selling its logs for fair value on the international markets should be the *only* investment the Tribunal considers in the course of its deliberations on NAFTA Article 1110.<sup>295</sup> Canada will explain why the Investor’s alleged “interest” does not fall within the definition of investment under Article 1139 (h) and is therefore not capable of being expropriated.

**1. The Investor’s Interpretation of “Interest” Under Article 1139(h) Is at Odds with the Definition of Investment Under NAFTA**

250. Contrary to what the Investor’s arguments suggest, Article 31 of the VCLT does not mandate that tribunals retain the “very first definition” of a word found in the dictionary.<sup>296</sup> This would be literal textual interpretation run amok. Rather, the Tribunal must give terms their ordinary meaning in their context and in light of the Treaty’s object and purpose.

251. The term “interest” in Article 1139(h) must be considered along with the other terms of that sub-paragraph and in the context of the other parts of the Article. In particular, Article 1139(h) covers “interests ... such as under contracts....” Examples

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<sup>295</sup> *Investor’s Reply*, ¶ 464. Canada notes that in its Memorial, the Investor argued that it has a “right” to sell its logs for fair market value and that this constitutes an intangible property right under Article 1139 (g) (*Investor’s Memorial*, ¶ 30). In its Reply, however, it now argues that it has an “interest” and not a “right” to realize fair value for its logs on the International markets (*Investor’s Reply*, ¶ 61).

<sup>296</sup> *Investor’s Reply*, ¶ 48.

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provided include construction and concession contracts. International law has long recognized that some contractual rights, although intangible, constitute property and are capable of being expropriated.<sup>297</sup> Article 1139(h) reflects this recognition by providing that interests such as concession contracts and the like constitute “investments” under NAFTA. Many arbitral decisions concern the expropriation of long-term concession contracts for the exploitation of natural resources.

252. Subparagraphs (i) and (j) of Article 1139 stipulate what is *not* an “investment” under NAFTA. Claims to money under commercial contracts and other commercial arrangements are not “investments.” Nor are “any other claims to money, that do not involve the *kinds of interests* set out in subparagraphs (a) through (h)” (emphasis added). This wording expresses that *all* “interests” covered by the definition of “investment” are of the same “kind.” In other words, an enterprise, an equity share, real estate and “interests ... such as under contracts...” are similar: they are liable to be bought, sold, traded or borrowed against.<sup>298</sup>

253. The Investor argues that, because its alleged “interest” is not specifically excluded from the definition of “investment” (like claims to money), it therefore must be included.<sup>299</sup> This argument is unsustainable. The definition of “investment” in Article 1139 is exhaustive. If the alleged interest is not specifically covered, then it does not

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<sup>297</sup> See, for example, Dolzer, Rudolf and Schreuer, Christoph, *Principles of International Investment Law*, Oxford (2008), at 115-118 (“*Dolzer & Schreuer*”) (Tab 168). The authors comment that “it is understandable that practically all investment treaties state that contracts are covered by the term ‘investment.’” In the footnote they refer to Article 1139 of the NAFTA, amongst others (*Id.*, at 116).

<sup>298</sup> *Canada’s Counter-Memorial*, ¶ 270.

<sup>299</sup> *Investor’s Reply*, ¶ 53.

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constitute an “investment” under NAFTA. This is the only possible interpretation of Article 1139.

254. In the end, what the Investor seeks to characterize as an “interest” under Article 1139(h) is really a claim for damages.<sup>300</sup> Merrill & Ring has sold its logs for “value” for decades. And it has consistently made profits doing just that. Now, it is trying to convince the Tribunal that it has an “interest,” protected by NAFTA, in the *price differential* between the “value” it has been receiving and the “fair value” it would like to get for its logs.<sup>301</sup> A price differential is not an “investment” in any way shape or form – and certainly not under NAFTA Article 1139.

255. While it may be “of importance” to the Investor to make as much money as possible exporting its logs,<sup>302</sup> it does not make that aspiration an “investment” for the purpose of NAFTA.

## 2. Goodwill Does Not Constitute an Investment Under Article 1139

256. The Investor attempts to link its alleged interest to “goodwill” in order to qualify under the definition of investment. This attempt fails for the following three reasons:

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<sup>300</sup> This is clear from the fact that in its Reply, the Investor states that its interest in selling logs for fair value on the international market “includes both the reduced revenues realized the logs, [sic] as well as the increased costs of producing them” (*Investor’s Reply*, ¶ 464). This description highlights that the Investor conflates its definition of investment and its claim for damages.

<sup>301</sup> See, for example, *Investor’s Memorial*, ¶ 11: “Every time Merrill & Ring is forced to sell its logs to B.C. sawmills at artificially suppressed prices, it loses *the difference in value* between that price and the fair market export price it could have received” (emphasis added). See also, *Investor’s Memorial*, ¶ 389.

<sup>302</sup> *Investor’s Reply*, ¶ 48.

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- The Investor confuses the value of an investment with the investment itself;
- The Investor misrepresents awards that do not support its views;
- The Investor does not provide any authority to rebut Canada’s authorities to the effect that goodwill is not a stand-alone investment.

257. The fundamental problem with the Investor’s argument can be summed up in one sentence: “[T]he notion of goodwill is too vague to be regarded as a separate property right apart from the enterprise to which is it attached.”<sup>303</sup> Rather, goodwill is an element of the *value* of an enterprise.<sup>304</sup>

258. The Tribunal in *Methanex* came to the same conclusion, in a passage that the Investor has not quoted fully in its Reply.<sup>305</sup> After rejecting the restrictive notion of property as a “material thing,” the Tribunal concluded that it was difficult to see how goodwill and market share might stand alone.<sup>306</sup> The Tribunal agreed with Professor White that goodwill is merely a factor in valuation.<sup>307</sup> Contrary to what the Investor

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<sup>303</sup> White, Gillian, *Nationalisation of Foreign Property* (Stevens & Sons Limited, 1961) at 49 cited in *Canada’s Counter-Memorial*, ¶ 276 (“White”) (Tab 160).

<sup>304</sup> *White* at 49 (Tab 160).

<sup>305</sup> See *Investor’s Reply*, ¶ 57.

<sup>306</sup> *Methanex - Award*, Part IV-Chapter C, cited in *Canada’s Counter-Memorial*, ¶ 275 (Tab 85).

<sup>307</sup> *Id.*, ¶ 275.

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argues, this Tribunal did not express “the same vision”<sup>308</sup> as the *Pope & Talbot* panel, but rather *rejected* that approach.

259. The Investor implies that the *Oscar Chinn* case does not support Canada’s argument that goodwill is not a stand-alone investment for the purpose of the NAFTA because it is an “old” case. It tries to distinguish that case based on the fact that it refers to the concept of “vested rights,” as opposed to the concept of investment. The question addressed by the PCIJ in *Oscar Chinn* is fundamentally the same as the one facing this Tribunal. The PCIJ considered whether goodwill, on its own, constituted a “vested right,” the deprivation of which required compensation. In this case, the question is whether goodwill alone constitutes an “investment” capable of being expropriated. In both cases, the answer is no. The rationale underlying the decision of the PCIJ still holds today: goodwill is a transient circumstance and has nothing in the nature of a genuine vested right.<sup>309</sup> Notably, the Investor fails to offer *any* international authority stating that goodwill, separate from an enterprise, can constitute an “investment.”

**C. The Tribunal Must Consider Merrill & Ring’s Investment as a Whole**

260. The Investor’s attempt to isolate the alleged “interest in selling logs at fair market value on international markets” should not be allowed to distract from the true nature of Merrill & Ring’s investment in Canada. Merrill & Ring is an enterprise in the business of harvesting timber and selling logs. Merrill & Ring owns lands, timber and logs

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<sup>308</sup> *Investor’s Reply*, ¶ 57.

<sup>309</sup> *The Oscar Chinn Case*, (UK v. Belgium), P.C.I.J. Series A/B, No 63, 12 December 1934, cited in *Canada’s Counter-Memorial*, ¶ 280 (Tab 23). Professor Brownlie in the most recent edition of his treatise states that “[t]his decision is also authority for the view that goodwill is not an item of property separate from an enterprise.” Brownlie, Ian, *Principles of Public International Law*, Seventh Edition, Oxford U. Press, Oxford, (2008) at 532 note 66 (Tab 167).

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amongst other property that it uses in the course of this business. The Tribunal must consider this enterprise as a whole as the investment.

261. The Investor's own submission suggests that the Tribunal should consider its investment as a whole (as opposed to the artificially narrow definition it puts forward in its Reply). While the Investor's Memorial is not always clear or consistent when it refers to its investment, it obviously considered that its investment was composed of more than a single "interest." It defined Merrill & Ring's investments as lands and logs, as well as "the rights to sell its export logs into foreign markets" and "the right to sell for fair market value."<sup>310</sup> However, in different instances, the Investor also refers to Merrill & Ring – the enterprise – as the investment. The following paragraph provides a good example of this (and of the general confusion in terminology):

The Log Export Control Regime is a measure tantamount to expropriation for the following reasons: a) Canada's Log Export Control Regime substitutes government control in the place of *Merrill & Ring's control* over critical parts of its business operations particularly in respect of the conduct and control over *its investments in logs* for export. The administration of the Log Export Control Regime mandates how the *Investment* has to harvest, process, advertise and then sell its principal products. Canada substantially interferes with Merrill & Ring's ordinary and normal property rights by depriving Merrill & Ring through the operation of its laws, policies and administration procedures, of the physical possession and control of *its investments*. Canada takes away *Merrill & Ring's control* to sell these logs at fair market prices. Instead, Canada through FTEAC, takes over this vital operation of Merrill & Ring's business.<sup>311</sup>

262. Merrill & Ring also refers to its investment as a whole in the following passage in which it attempts to distinguish the *Occidental* case,

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<sup>310</sup> *Investor's Memorial*, ¶¶ 27-30.

<sup>311</sup> *Id.*, ¶ 369 (emphasis added). See another example at ¶ 347.



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... Merrill & Ring is not arguing that its interest in realizing fair value for its logs on the international markets is an investment *per se*. Rather, Merrill & Ring is claiming that its interest in realizing fair value for its logs on the international market is *part-and-parcel of a larger investment* an investment that is protected by Article 1139. Merrill & Ring is not claiming that this interest is a stand alone investment on its own; rather, its claim is that this is an inextricable part of a bundle of rights and interests that make up *its investment*.<sup>312</sup>

263. This paragraph of the Investor's Reply contradicts the Investor's position that its interest in realizing a fair value for its logs on the international market is a stand-alone investment capable of being expropriated. Instead, the Investor admits that it is Merrill & Ring's investment as a whole that should be considered.

264. In any case, the Investor provides no authority to support its position that certain elements of an enterprise, such as goodwill or access to the U.S. market, are distinct investments capable of expropriation in their own right. The award in *Pope & Talbot*, which the Investor relies on, does not help the Investor on this count. The *Pope & Talbot* Tribunal did not consider whether access to the U.S. market *alone* had been expropriated.<sup>313</sup> Rather, it considered the investment as a whole and found that no expropriation had taken place. A similar conclusion is warranted in this case. The NAFTA Chapter 11 awards in *Methanex* and *Feldman*, discussed in Canada's Counter-Memorial, also support the view that the investment should be considered as a whole and not artificially parsed for the purpose of an expropriation claim.<sup>314</sup>

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<sup>312</sup> *Investor's Reply*, ¶ 61 (emphasis added).

<sup>313</sup> The *Pope & Talbot* Tribunal so held even after it recognized the access to the U.S. market as a property interest. See *Pope & Talbot - Interim Award*, ¶ 96 (Tab 112). Canada disagreed with the Tribunal's finding that access to the U.S. market constituted a property right.

<sup>314</sup> See *Canada's Counter-Memorial*, ¶¶ 275-276 on *Methanex - Award* (Tab 85) and *Canada's Counter-Memorial*, ¶ 277 on *Feldman - Award* (Tab 49).

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**D. There Has Been No Substantial Deprivation of Merrill & Ring's Investment**

265. Canada and the Investor agree that, to find expropriation, the Tribunal must conclude that Merrill & Ring has been substantially deprived of its investment.<sup>315</sup> For reasons already detailed in its Counter-Memorial, Canada submits that the Investor has not been substantially deprived of its investment. Further, the Investor's approach reduces to irrelevancy the test of "substantial deprivation" required to find a breach of Article 1110.

266. The Investor argues that the Regime is a measure tantamount to expropriation. In support of this, it points to the fact that Merrill & Ring has lost control over critical parts of its business operations, that it loses physical control of the logs under the operation of the Regime, that it loses the "control" to sell the logs at fair market prices, and that its logs suffer substantial physical damage as a result of the operation of the Regime.<sup>316</sup> Canada has demonstrated in its Counter-Memorial that these allegations are groundless.<sup>317</sup> The fact that the Investor's own harvest plan shows Merrill & Ring [REDACTED] demonstrates that no expropriation took place.<sup>318</sup>

267. In its Reply, the Investor changes its expropriation claim. The Investor now argues that Merrill & Ring's interest in selling its logs for fair value on the international

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<sup>315</sup> *Investor's Memorial*, ¶ 308 *et seq.* in particular at ¶ 326; *Canada's Counter-Memorial*, ¶ 730 *et seq.*

<sup>316</sup> See *Investor's Memorial*, ¶ 369.

<sup>317</sup> *Canada's Counter-Memorial*, ¶ 772.

<sup>318</sup> *Ruffle Report*, ¶ 5.1.

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markets should be the *only* investment the Tribunal considers in the course of its deliberations on NAFTA Article 1110.<sup>319</sup> The Investor states:

Once the investment at issue in NAFTA Article 1110 has been so defined, *then the question about the extent of interference with that investment fades away*. Canada has not merely interfered with this investment in some partial or ephemeral way; Canada has completely taken this investment away from Merrill & Ring. This is not just a partial taking it is a complete taking.<sup>320</sup>

This argument makes a mockery of the substantial deprivation test. The reasons cited by the Investor for its finding of a “complete taking” reveal exactly why such arguments should be rejected.

268. The more narrowly an investment is defined, the more likely it is that a substantial deprivation of that investment will be found. By artificially defining the “investment” as the *price differential* between the “value” it receives and the “fair value” it would like to get for its logs, the Investor makes a finding of expropriation inevitable. The Investor’s position leads to the absurd result that there is an expropriation each time the Investor does not realize a sale at a price it considers fair. Only by taking this position can the Investor state that “[t]his is not just a partial taking it is a complete taking.”<sup>321</sup> This approach should be rejected by the Tribunal.

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<sup>319</sup> *Investor’s Reply*, ¶ 464.

<sup>320</sup> *Id.*, ¶ 460 (emphasis added).

<sup>321</sup> *Id.*, ¶ 460.

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**E. The Tribunal Does Not Need to Analyse the Conditions of Article 1110(1)(a)-(d)**

269. In its Memorial, Merrill & Ring argued that the alleged expropriation was discriminatory, arbitrary, not conducted in accordance with due process and Article 1105(1), and was made without compensation.<sup>322</sup> In its Reply, the Investor argues that the failure to pay compensation is determinative, and that as a result “Merrill & Ring is prepared to restrict the inquiry to this single ground.”<sup>323</sup> Canada submits that no compensation was or is required since no expropriation took place.<sup>324</sup> As such, the Tribunal does not need to analyse the conditions of Article 1110(1)(a)-(d).

**F. Conclusion**

270. As Canada has demonstrated, the Investor has not been expropriated. It has not been substantially deprived of its investment. At all times Merrill & Ring has operated its business without government interference or control. The Investor has exported substantial volumes of logs under the Regime and earned substantial profits doing so. Canada has demonstrated why the alleged “interest” in selling logs at fair market value on international markets is not an investment capable of being expropriated under NAFTA Chapter 11. Further, it has demonstrated why the Investor’s attempt to narrowly define its investment in order to ensure a finding of expropriation should be rejected by

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<sup>322</sup> *Investor’s Memorial*, ¶¶ 372-389.

<sup>323</sup> *Investor’s Reply*, ¶ 453(iii).

<sup>324</sup> In its Reply, the Investor states that “Canada, however, would also have the Tribunal examine NAFTA Articles [sic] 1110(1)(a) to (c)” (*Id.*, ¶ 453(iii)). This is a mischaracterization of Canada’s position which it stated clearly in its Counter-Memorial: “In this case there is no basis to reach the question of lawful expropriation and the criteria in Article 1110(1)(a) to (d). There has been no expropriation at all.” (*Canada’s Counter-Memorial*, ¶ 781).

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the Tribunal. For all these reasons, Canada requests that this Tribunal dismiss the Investor's claim under Article 1110 of NAFTA.

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## VII. DAMAGES

### A. Summary of Canada's Position

271. Canada's Counter-Memorial and supporting expert affidavits exposed serious methodological problems, biased assumptions, and unsubstantiated calculations in the Investor's original damages assessment.<sup>325</sup> Rather than attempting to defend or rehabilitate its original damages claim, the Investor admitted Canada's "apparently valid criticisms of the PwC Report and MBG Report,"<sup>326</sup> took the extraordinary measure of withdrawing its original assessment, and filed an entirely new damages claim with its Reply.

272. The Investor's new damages claim consists of the Expert Witness Report of Robert Low (the "*Deloitte Report*") and the Witness Statement of Douglas A. Ruffle (the "*Ruffle Report*"). The new claim advances the theory that the Regime results in lost "export premiums" and asserts that the Investor incurs increased costs attributable to compliance with the Regime.

273. The Investor has forced Canada to expend valuable time and resources responding to a new case on damages at this late stage in the proceedings. Having been granted this second 'kick at the can,' the Investor still fails to adequately demonstrate that it has suffered any loss *as a result* of a breach of NAFTA. Article 1116(1) requires the Investor to demonstrate that it "has incurred loss or damage, *by reason of*, or arising out of" a

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<sup>325</sup> See *Canada's Counter-Memorial* at section VI.A.

<sup>326</sup> *Deloitte Report*, ¶ 1.27.

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breach of NAFTA. As Canada demonstrates below, the Investor's new damages claim remains equally unsubstantiated, based on flawed assumptions and riddled with methodological problems. The Investor's claim falls short of meeting the requirements set out in Article 1116(1).

274. First, while the Investor complains of many different aspects of the Regime, it fails to prove how any *specific* loss flows from a *specific* measure in breach of a NAFTA obligation. Instead, the Investor's new claim grossly oversimplifies. It provides just one measure of loss, regardless of which element of the Regime might be found in breach of NAFTA and regardless of the breach of NAFTA at issue. The Investor should have calculated its damages by establishing what specific loss resulted from each *specific* aspect of the Regime, which can be shown to have violated NAFTA.

275. The Investor's approach is also based on a Utopian "but for" assumption that the Investor operates outside of the Regime, while all other log exporters in British Columbia remain subject to the measures about which the Investor complains. The Investor makes this illogical assumption to avoid the logical consequence of its own theory that the Regime causes lost "export premiums" – specifically, that in the absence of the Regime the Investor would face increased competition from its larger competitors in the export market, resulting in a reduction of any "export premium." While the Investor's Utopian "but for" approach may be convenient, it is an unrealistic premise upon which to base the its damages claim.

276. Second, the Investor claims the Regime results in lost "export premiums." At the Memorial stage of these proceedings, the Investor failed to demonstrate lost "export premiums" on the basis of published prices.<sup>327</sup> The Investor now attempts in its Reply to

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<sup>327</sup> See *Canada's Counter-Memorial*, ¶¶ 835-843.

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establish lost “export premiums” by comparing [REDACTED] on sales subject to the Regime, with what it calls the “[REDACTED]” prices. These “[REDACTED]” prices are [REDACTED] [REDACTED], on sales *not* subject to the Regime.<sup>328</sup> The Investor claims the difference between these prices represents lost “export premiums.” It claims the allegedly lost “export premiums” as part of its alleged loss.

277. The Investor’s analysis fails to establish that the Regime has actually caused any loss of an “export premium.” The Investor’s lost “export premium” analysis suffers from serious methodological flaws, a point illustrated by the fact that many of its alleged “[REDACTED]” prices were actually achieved on sales of B.C. logs that *were* subject to the Regime (not, as represented by the Investor, prices achieved on sales of [REDACTED] that *were not* subject to the Regime). This flaw calls the Investor’s entire analysis into question.

278. The Investor’s approach to *quantifying* the alleged lost “export premiums” is also biased and overstates the alleged damages. As but one example, in quantifying lost “export premiums”, the Investor [REDACTED] on sales subject to the Regime exceeded the “[REDACTED]” prices. Canada’s experts demonstrate that this biased data selection is economically unsound.

279. Third, the Investor asks the Tribunal to accept a claim for damages allegedly attributable to the cost of compliance with the Regime. As with the Investor’s lost “export premium” theory, no serious consideration is given to whether the Regime or the specific aspects of the Regime complained of, actually resulted in the costs that are

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<sup>328</sup> *Investor’s Reply*, ¶¶ 479-481.





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[REDACTED]

1. **Lost Export Premiums**

[REDACTED]

[REDACTED]

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<sup>332</sup> Except with respect to damages claimed under Article 1110, for which the Past Loss Period is November 2003 to December 2006. See *Deloitte Report*, cover letter dated December 14, 2008, at 4.

<sup>333</sup> Except with respect to damages claimed under Article 1110, for which the Future Loss Period is 2007 to 2016. See *Deloitte Report*, cover letter dated December 14, 2008, at 4.

<sup>334</sup> *Deloitte Report*, ¶ 2.15.

<sup>335</sup> *Id.*, ¶ 2.15.

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[REDACTED]

[REDACTED]

[REDACTED]

**2. Costs of Compliance with the Regime**

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

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<sup>336</sup> *Reishus Supplemental Affidavit*, ¶ 46.

<sup>337</sup> *Deloitte Report*, ¶ 3.13.

<sup>338</sup> *Id.*, ¶¶ 3.14-3.16.

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[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

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<sup>339</sup> *Deloitte Report*, ¶¶ 3.17-3.18.

<sup>340</sup> *Id.*, ¶¶ 3.19-3.21.

<sup>341</sup> *Id.*, ¶ 3.22.

<sup>342</sup> *Id.*, ¶ 3.23.

<sup>343</sup> *Id.*, ¶ 3.26.

<sup>344</sup> *Id.*, ¶¶ 3.24-3.25.

<sup>345</sup> [REDACTED] See *Deloitte Report*, ¶ 1.46.

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3. **Future Losses**

290. The Investor's new damages claim makes a speculative attempt at quantifying future loss on the basis of Mr. Low's past loss calculation of the alleged export premium. These damages are also attributed to each of the alleged violations of Articles 1102, 1105, 1106 and 1110 and are claimed for the Future Loss Period of 2009-2016.

4. **The Ruffle Report**

[REDACTED]

[REDACTED]

293. [REDACTED]

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<sup>346</sup> *Ruffle Report*, Appendix I.

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5. **Quantum of Damages in the New Damages Claim**

294. The Investor claims the following in its new damages claim:

- **Articles 1102 or 1105** – Damages in the amount of \$16,804,068, and/or;<sup>347</sup>
- **Article 1106** – Damages in the amount of \$16,756,272 and/or;<sup>348</sup>
- **Article 1110** – Fair Market Value of \$16,228,603 (inclusive of interest calculated to May 31, 2009 the losses would be \$18,682,368.<sup>349</sup>

295. The Investor appears to take the position in its Reply that the amounts claimed *could* be cumulative if the Tribunal were to find a breach of several obligations.<sup>350</sup> The Investor does not explain why this should be the case. As the Investor claims damages for the three categories of loss described above (specifically lost export premiums, costs of compliance, and future losses), under *each* of Articles 1102, 1105, 1106 and 1110, there is *no* basis for treating these amounts as cumulative. To do so would be contrary to basic principles of full reparation

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<sup>347</sup> *Deloitte Report*, ¶¶ 1.38, 1.39, 1.42 and 1.43.

<sup>348</sup> *Id.*, ¶¶ 1.46 and 1.47.

<sup>349</sup> *Id.*, ¶¶ 1.50 and 1.51.

<sup>350</sup> See *Investor's Reply*, ¶ 483, where the Investor links each request for relief under Articles 1102 and 1105, 1106 and 1110 with the words “and/or.” (Note that there is an error in the paragraph numbering of the Investor's Reply as there are two paragraphs 483. The reference in this instance is to the final paragraph of the Investor's Reply, which should, in fact, be paragraph 488).

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[REDACTED]

6. **The Investor Makes a New Claim for Menzies Bay and Squamish Holdings**

[REDACTED]

[REDACTED]

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<sup>351</sup> *Deloitte Report*, ¶ 2.29.

<sup>352</sup> *Ruffle Report*, Tables 1-1, 1-2, 1-3, 5-6, 6-1, 6-3, Figure 6-6 and Appendix II. See also *Deloitte Report*, Note 9 of Schedule 1 at 54; Note 9 of Schedule 3 at 63.

<sup>353</sup> Canada reminds the Tribunal that over 12 months ago, and three months *prior* to the filing of its Memorial, the Investor unsuccessfully tried to add its affiliate, Georgia Basin, as a disputing party to the claim (see Investor’s Motion to Add a Third Party, 12 December 2007). Georgia Basin’s claim stemmed mostly from its logging rights over the Menzies Bay and Squamish holdings, logging rights previously held by the Investor. The Investor’s failed motion demonstrates it was aware that it held logging rights over these holdings, yet it made no mention of its intention to include them in its claim.

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[REDACTED]

[REDACTED]

**C. The Investor Fails to Identify a Proper “But for” Scenario to Assess its Damages**

299. To recover damages, the Investor must submit evidence demonstrating how a *specific* measure, found to breach NAFTA, caused it *specific* loss. The Investor has failed to furnish the evidence necessary to establish how each element of the Regime that it complains of has resulted in the damages claimed. In other words, the Investor fails to identify the proper “but for” scenario in respect of each alleged breach.

300. Further, the “but for” scenario at the heart of the Investor’s damages analysis contemplates the complete removal of Canada’s Log Export Control Regime with respect only to the Investor *alone*. This is an unrealistic foundation upon which to ground the claim.

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354

[REDACTED]

<sup>355</sup> The Menzies Bay and Squamish holdings account for over \$1.55 million of the Investor’s new damages claim. *Deloitte Report*, Schedule 1, note 9 and *Ruffle Report*, Appendix 1.



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301. Canada explains in greater detail below why these fundamental problems with the Investor's approach leave no workable basis on which the Tribunal could assess damages.

1. **The Investor Has Failed to Establish Causation Between its Specific NAFTA Allegations and Specific Damages Claimed**

302. The Investor fails to link specific NAFTA violations to the specific damages that it claims. Its approach is flawed because it advances a general omnibus damages claim in respect of *all* alleged breaches of NAFTA.

303. The following table summarizes the specific allegations of NAFTA breaches that the Investor has made in its Memorial and Reply Briefs.

The Investor's Specific Allegations

| HEAD OF DAMAGE              | SPECIFIC ALLEGATION OF NAFTA VIOLATION  |
|-----------------------------|---|
| Article 1102 <sup>356</sup> | Merrill & Ring is "forced" to observe the requirements of <i>Notice 102</i> while other Log Producers in B.C. and Alberta are not. <sup>357</sup> |
|                             | Merrill & Ring is "forced" to cut, sort, and scale its logs in a particular way while log producers in B.C. Interior and Alberta are not.         |
|                             | Merrill & Ring is "forced" to observe the so-called "remoteness rule" while other log producers on the south Coast are not.                       |
|                             | Merrill & Ring is "forbidden" from receiving standing exemptions while log producers on provincial lands are not.                                 |
|                             | Merrill & Ring is "forbidden" from advertising standing timber, while log producers in the B.C. Interior are not.                                 |

<sup>356</sup> *Investor's Reply*, ¶¶ 243-274.

<sup>357</sup> Merrill & Ring also complains that it is "forced" to sell its logs domestically and that it is forced to sell its logs under "blockmail." These claims necessarily flow from having to observe the requirements of *Notice 102*.

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| HEAD OF DAMAGE              | SPECIFIC ALLEGATION OF NAFTA VIOLATION  |
|-----------------------------|---|
|                             | Merrill & Ring is required to pay a fee-in-lieu to export its provincial logs, while federal log producers are not.                                       |
| Article 1105 <sup>358</sup> | No private landowners have been invited to be a member of FTEAC and that it is never consulted on the selection of new members.                           |
|                             | FTEAC members are in situations of conflicts of interest.   |
|                             | The cancellation of FTEAC meetings.   |
|                             | FTEAC's practice to consider an offer as fair market value whenever it closely matches (+/- 5%) the prevailing domestic market price is too "subjective." |
|                             | Not being able to make any "oral submissions" to FTEAC.   |
|                             | Not knowing the relevant factors to be addressed when asking the Minister to disregard an FTEAC recommendation.   |
|                             | Merrill & Ring complains that the concept of "remote" areas is unclear.   |
| Article 1106 <sup>359</sup> | Merrill & Ring is required to cut and sort timber from their federally regulated lands to "normal market practices."                                      |
|                             | Merrill & Ring is required to scale all timber rafts metrically.  |
|                             | Merrill & Ring is required to follow the "remoteness rule."   |
| Article 1110 <sup>360</sup> | Canada expropriated Merrill & Ring's interest in realizing fair value for its logs on the international market. <sup>361</sup>                            |

304. The Investor's omnibus approach to quantification does not establish a specific connection between any alleged violations and its claimed loss. Establishing this essential connection should have been the first step in the Investor's damages analysis.

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<sup>358</sup> *Investor's Reply*, ¶¶ 18, 348-367.

<sup>359</sup> *Id.*, ¶ 403.

<sup>360</sup> *Investor's Memorial*, ¶ 369.

<sup>361</sup> *Investor's Reply*, ¶ 464.

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The Investor has conveniently decided to skip this exercise altogether. As a result, the Investor has not proven causation as required by Article 1116(2) of NAFTA.

305. For instance, the Investor claims that the Regime does not permit it to advertise standing timber, unlike log producers in the B.C. Interior. It further claims that this is a violation of national treatment under NAFTA Article 1102. But the Investor makes no effort to specifically identify the “but for” scenario resulting from a finding that this aspect of the Regime breaches Article 1102. Nor does it quantify the damages arising from this particular alleged violation. The Investor’s omnibus approach to assessing damages would be of no assistance whatsoever to the Tribunal if it were to find a specific breach of NAFTA Article 1102 on the basis of the Investor’s specific claim regarding the advertising of standing timber.

306. A proper approach to quantifying any damages arising from this specific allegation would require the Investor to provide persuasive evidence of damages arising from the NAFTA breach. For example, the Investor should have provided evidence of a difference in prices it could have obtained by advertising standing timber with prices it did obtain. In practical terms, this would require evidence of sales made at reduced prices as a result of delays caused specifically by and attributable to this particular requirement such as documentary evidence or testimony by customers. The Investor submitted *no* such evidence.

307. Another example of the Investor’s flawed approach is illustrated by its claim that Canada violated Article 1105 because of the imposition of sorting and scaling requirements. Again, the Investor has not attempted to quantify any damages arising from this particular alleged violation. A proper approach to quantification of damages would require the Investor to provide evidence of additional costs, sales made at reduced prices, or lost sales specifically resulting from and attributed to the sorting and scaling requirements. The Investor’s omnibus approach would be of no assistance to the

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Tribunal if it were to find a breach of NAFTA Article 1105 as a result of sorting and scaling requirements.

308. In sum, the Investor's approach has left the Tribunal with no way of being able to quantify the alleged damages arising from each alleged breach of NAFTA. As the Investor has failed to link *specific* loss to a *specific* breach it has failed to prove causation. The Tribunal should not accept the Investor's general omnibus damages claim as being a workable approach to establishing that all alleged NAFTA violations actually caused the alleged loss. As a result, the Investor's claim must fail.

## 2. The Investor Advances a Utopian “But for” Scenario to Support its New Damages Claim

309. The Investor also continues to imagine a Utopian “but for” world as the basis of its damages claim. In its “but for” world, the Investor operates outside of the Regime, while every other owner of private land continues to comply with the Regime.<sup>362</sup> Mr. Low has adopted the same “but for” world that was advocated in the deeply flawed and now retracted MBG and PwC Reports.

310. The Investor advances such an unrealistic scenario to avoid the logical consequences of its theory that log export controls result in lost “export premiums.” A more realistic “but for” scenario would be that log export controls are removed for all private federal landowners in B.C. In this scenario, the Investor would have to face competition in the export market from other large federal private land owners in British

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<sup>362</sup> Specifically, Mr. Low states: “[o]ur analysis is based on Canada and B.C. maintaining the Procedures currently in place and that Merrill & Ring should receive monetary compensation for the losses it has and will continue to suffer as a result of the Procedures.” See *Deloitte Report*, ¶ 1.32.

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Columbia.<sup>363</sup> The consequence of the Investor's theory (that the Regime causes an export premium) would be that the increased competition in the export market would significantly reduce any “export premium.” This is what the Investor seeks to avoid.

311. In sum, the Investor's Utopian “but for” approach simply does not provide the Tribunal with a reasonable framework to assess the Investor's claim for damages. This element of the Investor's approach further warrants a rejection of its damages claim.

**D. The Investor's New Damages Claim Does Not Provide a Reliable Measure of Alleged Loss**

312. In the foregoing section, Canada has demonstrated how fundamental flaws with the Investor's approach to damages render its new damages claim unworkable. This problem with the Investor's approach is compounded by the flaws in the Investor's: (1) lost “export premiums” theory; (2) claim for the costs of compliance allegedly attributable to the Regime; and (3) future loss claim. Canada addresses these flaws below.

**1. The Investor's Claim for Lost “Export Premiums” Is Fatally Flawed**

313. The Investor claims that the Regime results in “export premiums” for exported logs relative to B.C. domestic prices, and that the lost premiums are representative of its damages. The Investor's lost “export premiums” theory must be rejected for the following reasons. First, the Investor provides no evidence demonstrating a causal link between any element of the Regime and the alleged lost “export premiums,” or that the alleged premiums are an appropriate benchmark for an assessment of its damages.

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<sup>363</sup> In particular, the largest private federal landowners on the B.C. Coast, Island Timberlands and Timberwest.

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Second, Mr. Low’s calculation of the lost “export premium” is unsubstantiated and deeply flawed. Therefore, it cannot be regarded as a reliable benchmark for an assessment of the Investor’s alleged damages. Third, Mr. Low’s calculation of damages arising from the lost “export premium” is based on the exaggerated and overly optimistic revised harvest plan in the *Ruffle Report*.

**a) The Investor Has Not Established a Causal Link Between the Regime and Alleged Lost “Export Premiums”**

[REDACTED]

[REDACTED]

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<sup>364</sup> Specifically, the *Deloitte Report* states “[REDACTED]” and that [REDACTED]” See *Deloitte Report*, ¶ 2.11.

<sup>365</sup> *Deloitte Report*, ¶ 2.14.

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[REDACTED]

[REDACTED]

[REDACTED]

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<sup>366</sup> *Deloitte Report*, ¶ 3.4(a) and (b).

<sup>367</sup> *Id.*, ¶ 2.14.

<sup>368</sup> *Id.*, ¶ 2.19(a).

<sup>369</sup> *Id.*, ¶ 2.19(b) and (c).

<sup>370</sup> *Id.*, ¶ 2.19(d).

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<sup>371</sup> *Deloitte Report*, ¶ 2.19(e) and (f).  
<sup>372</sup> *Id.*, ¶ 2.19(g).  
<sup>373</sup> *Korecky Supplemental Affidavit*, Exhibit 84.  
<sup>374</sup> *Reishus Supplemental Affidavit*, ¶ 57.



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<sup>375</sup> *Deloitte Report*, ¶ 5.3.

<sup>376</sup> *Reishus Supplemental Affidavit*, ¶ 111.

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<sup>377</sup> *Reishus Supplemental Affidavit*, ¶ 56.

<sup>378</sup> *Reishus Affidavit*, ¶ 91.

<sup>379</sup> *Id.*, ¶¶ 92-93.

<sup>380</sup> *Id.*, ¶ 94.

<sup>381</sup> *Jendro Supplementary Affidavit*, ¶ 4.1.5.

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<sup>382</sup> *Jendro Supplemental Affidavit*, ¶ 3.4.2-3.4.4. [REDACTED]

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<sup>383</sup> *Deloitte Report*, ¶ 3.4(b).

[REDACTED]

<sup>385</sup> *Deloitte Report*, ¶ 3.4(b) (emphasis added).

<sup>386</sup> *Jendro Supplemental Affidavit*, ¶ 3.4.2.

<sup>387</sup> *Id.*, ¶ 2.1.9.

<sup>388</sup> *Id.*, ¶ 3.4.4, Appendix C.

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<sup>389</sup> *Jendro Supplemental Affidavit*, ¶ 3.3.13(6).

<sup>390</sup> *Id.*, ¶ 3.4.5.

<sup>391</sup> *Id.*, ¶ 3.4.12.

<sup>392</sup> *Reishus Supplemental Affidavit*, ¶ 100.

<sup>393</sup> *Jendro Supplemental Affidavit*, ¶ 3.4.6.

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<sup>394</sup> *Reishus Supplemental Affidavit*, ¶ 79.

<sup>395</sup> *Jendro Supplemental Affidavit*, ¶ 3.4.11.

<sup>396</sup> *Id.*, ¶ 3.4.13.

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<sup>397</sup> *Jendro Supplemental Affidavit*, ¶ 2.1.5.

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<sup>398</sup> *Reishus Supplemental Affidavit*, ¶ 65.

<sup>399</sup> *Jendro Supplemental Affidavit*, ¶ 3.5.19, Figure 3.5-3.

<sup>400</sup> *Id.*, ¶ 2.1.14.



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<sup>401</sup> *Jendro Supplemental Affidavit*, ¶ 3.3.14(7).

<sup>402</sup> *Id.*, ¶ 3.3.15(8).

<sup>403</sup> *Id.*, ¶ 3.3.9(2). [REDACTED]

<sup>404</sup> *Id.*, ¶ 3.3.10(3). [REDACTED]

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<sup>405</sup> *Reishus Supplemental Affidavit*, ¶ 50 (emphasis in original).

<sup>406</sup> *Ruffle Report*, ¶ 3.1.

<sup>407</sup> *Jendro Supplemental Affidavit*, ¶ 7.1.4.

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<sup>408</sup> *Reishus Supplemental Affidavit*, ¶ 147.

<sup>409</sup> *Ruffle Report*, ¶¶ 4.1- 4.6.8.

<sup>410</sup> *Jendro Supplemental Affidavit*, ¶¶ 7.2.7-7.2.10.

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<sup>411</sup> *Jendro Supplemental Affidavit*, ¶ 2.5.4.

<sup>412</sup> *Deloitte Report*, ¶¶ 3.11-3.26, 4.33-4.48.

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<sup>413</sup> *Deloitte Report*, ¶ 4.33.

<sup>414</sup> *Id.*, Schedule 1.

<sup>415</sup> *Id.*, ¶ 1.46.

<sup>416</sup> *Id.*, Schedule 3.

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<sup>417</sup> *Deloitte Report*, ¶ 3.13.

<sup>418</sup> *Bowie Supplemental Report*, ¶¶ 153-155, 157.

<sup>419</sup> “Bucking” refers to the process of cutting the logs into prescribed length according to the preference of customers in order to maximize values.

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<sup>420</sup> *Deloitte Report*, ¶ 3.22.

<sup>421</sup> *Bowie Supplemental Report*, ¶¶ 193-194.

<sup>422</sup> *Id.*, ¶ 193.

<sup>423</sup> *Deloitte Report*, ¶ 3.14-3.16.

<sup>424</sup> *Bowie Supplemental Report*, ¶ 165.

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<sup>425</sup> *Bowie Supplemental Report*, ¶¶ 167, 248, 251.

<sup>426</sup> *Id.*, ¶¶ 168-169, 249-251.



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<sup>427</sup> *Deloitte Report*, ¶¶ 4.38-4.39.

<sup>428</sup> *Bowie Supplemental Report*, ¶ 162.

<sup>429</sup> *Id.*, ¶ 168.

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<sup>430</sup> *Deloitte Report*, ¶¶ 3.17-3.18, 4.40-4.41.

<sup>431</sup> *Bowie Supplemental Report*, ¶ 181.

<sup>432</sup> *Id.*, ¶¶ 183, 256-257.

<sup>433</sup> *Korecky Affidavit*, ¶ 161.

<sup>434</sup> *Bowie Supplemental Report*, ¶¶ 145, 256.

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<sup>435</sup> *Deloitte Report*, ¶ 3.23.

<sup>436</sup> *Bowie Supplemental Report*, ¶¶ 202-205, 274-275.

<sup>437</sup> *Deloitte Report*, ¶ 4.55.

<sup>438</sup> *Bowie Supplemental Report*, ¶ 85.

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**c) Summary Regarding the Investor's Claims for Cost of Compliance**

359. The Investor's claims for the costs of compliance with the Regime are without merit. The Investor has utterly failed to establish that any of the costs are attributable to the Regime.<sup>439</sup> Its approach to quantification of the alleged costs is rife with methodological errors, calling into question the reasonableness of any of the costs that have been claimed. Given the weaknesses inherent in this element of the Investor's claim, it should be dismissed by the Tribunal.

**3. The Investor's Future Loss Claim Should Be Rejected**

360. The Investor claims damages for future losses assuming that it will continue to be subject to the Regime. Below Canada demonstrates that the Investor's future loss claim is speculative and, as such, falls short of the applicable legal standard. At any rate, since the Investor's claim for future loss is based upon Mr. Ruffle's flawed harvest plan and Mr. Low's flawed lost "export premium" calculations, it is entirely unreliable.

**a) The Investor's Future Loss Claim Is Speculative**

361. Compensation for future loss is not granted as a matter of course in international arbitration due to the often speculative nature of such claims. Damages for future loss are awarded only if the Investor establishes that projected losses have a sufficient degree of certainty. The official commentary of the ILC on its Articles on State Responsibility provides,

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<sup>439</sup> With the exception of costs related to the provincial fees-in-lieu of domestic manufacture.

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In cases where lost future profits have been awarded, it has been where an anticipated income stream has attained sufficient attributes to be considered legally protected interests of sufficient certainty to be compensable.<sup>440</sup>

362. This is a long established principle in international arbitration. In the *Rudloff* case, the US-Venezuela Mixed Claims Commission held that: “[d]amages to be recoverable must be shown with a reasonable degree of certainty, and cannot be recovered for an uncertain loss”<sup>441</sup>. The Iran-US Claims Tribunal echoed this view in the *Amoco* Award holding that “one of the best settled rules on the law on international responsibility of States is that no reparation for speculative or uncertain damages can be awarded.”<sup>442</sup>

363. Recently, the Tribunal in *LG&E* reiterated that: “Tribunals have been reluctant to provide compensation for claims with inherently speculative elements.”<sup>443</sup>

364. The Investor’s future loss claim is speculative for a number of reasons. As a general matter, future market prices, demand and export volumes cannot be predicted with any sufficient certainty.

[REDACTED]

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<sup>440</sup> Responsibility of States for Internationally Wrongful Act 2001, *Report of the International Law Commission*, Fifty-Third Session (23 April-1 June and 2 July-10 August 2001), Supp. No. 10 (A/56/10), United Nations, New York 2001 (“*ILC Commentary*”) (Tab 171).

<sup>441</sup> *Rudloff Case (Merits)*, United States-Venezuela Mixed Claims Commission, (1903-5) IX UNRIAA 255, 258 (Tab 174).

<sup>442</sup> *Amoco International Finance v. Iran*, Award of 14 July 1987, 15 Iran-US CTR 189, ¶ 238 (Tab 166).

<sup>443</sup> *LG&E Energy Corp. et al. v. Argentina* (ICSID No. ARB/02/1) Award 25 July 2007, (“*LG&E – Award*”) ¶ 51 (Tab 70).

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[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

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<sup>444</sup> *Deloitte Report*, ¶ 4.50.

<sup>445</sup> *Id.*, ¶ 4.49.

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[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

368. The Investor’s speculative view of the future is simply without foundation and cannot serve as the basis of a future damages claim.

**b) The Investor’s Future Loss Claim Is Fatally Dependent on the Flawed Revised Harvest Plan and “Export Premium” Theory**

369. Canada has demonstrated that the Investor’s analysis of alleged lost “export premiums” and projected future harvest volumes are both fundamentally flawed. As they

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<sup>446</sup> *Reishus Supplemental Affidavit*, ¶¶ 161-166.

<sup>447</sup> *Id.*, ¶ 170.

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are the basis upon which the Investor makes its future loss claim, it too must be viewed as fundamentally flawed and unreliable.

#### E. Conclusion

370. The Investor was granted a second chance to prove it suffered loss as a result of NAFTA violations stemming from the Regime. But like its first effort, the Investor's second attempt is without merit.

371. The Investor's new damages claim presents the Tribunal with a problematic approach to quantifying damages – it makes no effort to link *specific* loss to a *specific allegation* of a breach of NAFTA. Furthermore, the new damages claim is also founded on an entirely implausible scenario in which *only* the Investor is not subject to the Regime. Finally, the Investor's approach to quantification of damages is unworkable.

372. These overarching problems are compounded by the Investor's inability to establish a causal connection between the Regime and both the alleged lost "export premiums" (in the past and in the future) and between the Regime and the various costs of compliance claimed by the Investor. The methodological errors in the Investor's calculations expose the claim as unreliable, unrealistic and deserving of complete dismissal by the Tribunal. In short, the Investor has failed to establish that it "has incurred loss or damage, by reason of, or arising out of" a breach of NAFTA by Canada as required by Article 1116(1) of NAFTA.



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## VIII. RELIEF REQUESTED

### A. Interest

373. Canada discussed the law applicable to awards of interest in its Counter-Memorial.<sup>448</sup> Interest should not be awarded unless necessary to provide full reparation of a breach. The Investor has failed to prove any loss that could give rise to an award of interest. Furthermore, the Investor presented no legal argument as to why it should be entitled to interest. In particular, the Investor has not established the appropriate accrual date, interest rate or whether interest should be calculated on a simple or compound basis. As a result, Canada asks that the Tribunal deny the Investor's claim for interest.

### B. Costs

374. Canada re-iterates the principles set out in its Counter-Memorial regarding the costs of these proceedings. Canada also requests that the Investor be ordered to pay the costs of this arbitration and to indemnify Canada for its legal costs.<sup>449</sup>

375. The Investor's conduct in this case warrants an award of costs in favour of Canada. For example, the Investor's withdrawal of the PwC and MBG Reports and filing of an entirely new damages claim at the Reply stage (without any advance notice to the Tribunal and Canada) have resulted in the following unnecessary and unreasonable costs to Canada: (1) costs incurred (needlessly) in the preparation of the Reishus and Jendro Affidavits, the Bowie Report and Canada's submissions on damages at the Counter-Memorial stage; (2) costs incurred (needlessly) consulting with experts on document

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<sup>448</sup> *Canada's Counter-Memorial*, ¶¶ 870-892.

<sup>449</sup> *Id.*, ¶¶ 893-897.

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production relating to the now retracted PwC and MBG Reports; (3) costs incurred consulting with experts on document production relating to the *Deloitte* and *Ruffle Reports*; and, (4) costs incurred in the preparation of the *Reishus* and *Jendro Supplemental Affidavits*, *Bowie Supplemental Report*, and Canada's submissions on damages in its Rejoinder to address the issues raised in the Investor's new damages claim.

376. Moreover, the Investor's motion to add its affiliate, Georgia Basin Holdings L.P., as a disputing party in this arbitration should be a further factor to be taken into consideration on the issue of costs. The Investor was entirely unsuccessful on this motion. In refusing the motion, the Tribunal ruled that the companies' claims were not sufficiently alike and that permitting the motion would prejudice Canada by permitting the evasion of the procedural rules of the NAFTA and allowing a new claim by way of an amendment.<sup>450</sup>

377. Canada respectfully requests an opportunity to submit a more detailed submission to the Tribunal so that it can fully address these and all other relevant considerations regarding the issue of costs in this matter.

**C. Order Requested**

378. For the foregoing reasons, Canada respectfully requests that this Tribunal render an award:

- i. Dismissing the claims of Merrill & Ring in their entirety;

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<sup>450</sup> *Merrill & Ring Forestry v. Canada*, Decision on a Motion to Add a New Party, January 31, 2008.

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- ii. Ordering that Merrill & Ring bear the costs of the arbitration in full and indemnify Canada for its costs of legal representation.

March 27, 2009

*Respectfully submitted  
on behalf of Canada,*

(Original signed by Sylvie Tabet)

Sylvie Tabet  
Lori Di Pierdomenico  
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### Glossary of Terms

| TERM                              | DEFINITION   |
|-----------------------------------|--|
| <b>Aboriginal land</b>            | Land falling within the exclusive authority of the federal Department of Indian and Northern Affairs.  |
| <b>Boom of logs</b>               | An assemblage of logs floating on a body of water and contained within a perimeter of floating, chained logs. Designed for storage or for towing through protected waters. <i>Also referred to as “raft of logs.”</i>                                |
| <b>B.C. Coast</b>                 | Area of British Columbia west of the Coast and Cascade Mountains, including any islands off the coast (e.g. Vancouver Island).   |
| <b>B.C. Interior</b>              | Area of British Columbia east of the Coast and Cascade Mountains.  |
| <b>Blanket standing exemption</b> | Exemption from the B.C. local use and manufacturing requirement granted to “standing” (i.e. uncut) timber in a given geographic area. <i>See also: individual standing exemption; utilization exemption; economic exemption.</i>                     |
| <b>Bucking</b>                    | Process of cutting a felled tree into logs of size and trimming off unwanted portions according to customer preferences in order to maximize value.  |
| <b>Crown land</b>                 | For the purpose of these submissions, land owned by the provincial government.   |
| <b>Economic exemption</b>         | Exemption from the B.C. local use and manufacturing requirement granted either to standing timber or logs when they cannot be economically harvested at domestic prices. <i>See also: blanket standing exemption; individual standing exemption.</i> |
| <b>Federal land</b>               | Private land in British Columbia acquired by Crown grant prior to March 12, 1906.  |

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| <b>Fee-in-lieu of manufacture</b>     | Fee imposed on all logs subject to the provincial regime authorized for removal and exported from British Columbia.   |
| <b>Harvested surplus applications</b> | Applications to advertise “harvested” (i.e. cut) timber on the Bi-Weekly list.  |
| <b>Individual standing exemption</b>  | Exemption from the B.C. local use and manufacturing requirement granted to an individual land owner for “standing” (i.e. uncut) timber. <i>See also: blanket standing exemption; utilization exemption; economic exemption.</i>           |
| <b>Provincial land</b>                | Private land in British Columbia granted after March 12, 1906, and Crown land.  |
| <b>Provincial regime</b>              | Part 10 of the <i>B.C. Forest Act</i> and related measures pertaining to the local use and manufacture requirement for timber harvested in British Columbia.  |
| <b>Raft of logs</b>                   | An assemblage of logs floating on a body of water and contained within a perimeter of floating, chained logs. Designed for storage or for towing to another location through protected waters. <i>Also referred to as “boom of logs.”</i> |
| <b>Regime</b>                         | The Federal Log Export Control Regime, comprised of the Export and Import Permits Act (EIPA) and <i>Notice 102</i> and associated procedures.   |
| <b>Scaling</b>                        | Measuring logs in order to determine and record their species, dimensions, volume and quality.  |
| <b>Sorting</b>                        | Separating and classifying logs according to species, size, and quality.  |
| <b>Sort</b>                           | A user-specified category of sizes and quality characteristics for logs within a species group used for the marketing of logs.  |

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|                                      |  |
|--------------------------------------|--|
| <b>Standing surplus applications</b> | Applications to advertise “standing” (i.e. uncut) timber on the Bi-Weekly list.  |
| <b>Utilization exemption</b>         | Exemption from the B.C. local use and manufacturing requirement granted either to standing timber or logs when they would otherwise go to waste. <i>See also: blanket standing exemption; individual standing exemption.</i> |