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

BETWEEN:

MOBIL INVESTMENTS CANADA INC. AND MURPHY OIL CORPORATION

Claimant/Investor

AND:

GOVERNMENT OF CANADA

Respondent/Party

GOVERNMENT OF CANADA

REPLY TO SECOND ARTICLE 1128 SUBMISSIONS

7 FEBRUARY 2011

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I. INTRODUCTION

1. The second NAFTA Article 1128 submissions of the United States of America and the United Mexican States confirm that the Guidelines for Research and Development Expenditures ("Guidelines") are reserved from Article 1106 because they are subordinate to a measure listed in Annex I. First, the United States confirms that Article 3 of Annex I contains "rules of priority" between the elements of a reservation. Those rules confirm that the reservation for the Accord Implementation Acts is not restricted in the manner asserted by the Claimants.

2. Second, Mexico and the United States confirm that a NAFTA tribunal must examine domestic law when deciding if a measure is subordinate to a measure listed in Annex I. Thus, the submissions confirm that the Tribunal should defer to the decisions of the Canadian courts that the Guidelines are authorized by, and consistent with, the Accord Implementation Acts.

3. Finally, Mexico and the United States confirm that a measure can be subordinate to a measure listed in Annex I, even if it imposes additional or more onerous burdens. Consequently, even if the Guidelines impose such burdens, which they do not, they are still reserved.

II. THE NAFTA PARTIES AGREE THAT ANNEX I(3) CONTAINS RULES FOR INTERPRETING RESERVATIONS

4. The United States confirms that Article 3 of Annex I contains "rules of interpretation for construing reservations," which include "rules of priority for considering the different elements."[1] Consequently, the Claimants' assertion that Article 3(c) of Annex I is "irrelevant" to the scope of the reservation for the Accord Implementation Acts[2] has no foundation.

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[1] Second Submission of the United States of America, 21 January 2011, ¶ 8.

[2] Claimants' Reply to Canada's Post Hearing Submission, 31 January 2011, ¶ 5.

5. The "rules of priority for considering different elements" in Article 3 include the rule in Article 3(c) that, for an "unqualified" reservation, the Measures element "prevails over all other elements" unless there is a relevant discrepancy between those elements.[3] Thus, the Claimants' assertion that the reservations in Annex I of the NAFTA are confined to authority expressly identified in the Description element is baseless. Indeed, when the NAFTA parties intended for the Description to prevail over the other elements, they stated that explicitly. In Article 3 of Annex II and Annex VI, the rule of priority is that the Description element prevails.[4] This is not the rule of priority for Annex I reservations.

6. The reservation for the Federal Accord Implementation Act is "unqualified"[5] and contains no discrepancy between the elements.[6] Thus, the "rule of priority" in Article 3(c) of Annex I is that the Measures element "prevails over all other elements," including the Description element. Consequently, the Claimants' argument that the reservation for the Federal Accord Implementation Act is confined to the authority expressly identified in that Description is inconsistent with the second Article 1128 submission of the United States.

7. Regardless, the Claimants' argument is irrelevant because the Guidelines are still reserved, even under the Claimants' interpretation. First, the Description of the Federal Accord Act expressly identifies the obligation to expend on research and development ("R&D") and education and training ("E&T"). The authority to issue guidelines concerning this obligation, expressly provided in section 151.1(1), is covered by this

[3] Annex I, ¶ 3(c) states that the Measures element shall prevail unless there is a "discrepancy between the Measures element and the other elements considered in their totality [that] is so substantial and material that it would be unreasonable to conclude that the Measures element should prevail."

[4] Annex II, ¶ 3 ("In the interpretation of a reservation, all elements of the reservation shall be considered. The Description element shall prevail over all other elements."); Annex VI, ¶ 3 ("In the interpretation of a commitment, all elements of the commitment shall be considered. The Description element shall prevail over all other elements.").

[5] Canada's Post Hearing Submission, 3 December 2010, ¶¶ 9-10; Canada's Reply to Claimants' Post Hearing Brief, 31 January 2011, ¶¶ 20 - 23.

[6] Neither party in this dispute has suggested that there is a discrepancy that prevents the Measures element from prevailing (see Canada Post Hearing Submission, 3 December 2010, ¶ 11).

Description.[7] Second, even if the Guidelines do not fall into the reservation for the Federal Accord Implementation Act, they do fall into the reservation for the Provincial Accord Implementation Act, which has no Description element.[8]

III. THE NAFTA PARTIES AGREE THAT DOMESTIC LAW MUST BE APPLIED WHEN DECIDING IF AN ALLEGED SUBORDINATE MEASURE IS CONSISTENT WITH A LISTED MEASURE

8. The reservation for a measure listed in Annex I of the NAFTA includes "any subordinate measure adopted or maintained under the authority of and consistent with the [listed] measure."[9] When deciding whether a domestic measure is subordinate to another domestic measure listed in Annex I, the Tribunal is directed by the "law of the NAFTA" to apply domestic law, as previously explained by Canada.[10]

9. Mexico agrees:

> [I]n order to determine whether a subordinate measure fulfils the requirements set out in paragraph 2(f)(ii) of Annex I, it would be necessary to carry on an assessment of the subordinate measure under the national law governing the measure listed in Annex I.[11]

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[7] Canada's Reply to Claimants' Post Hearing Brief, 31 January 2011, ¶ 28.

[8] Canada's Post Hearing Submission, 3 December 2010, ¶¶ 16 - 22. The Claimants suggest that the reservation for provincial measures existing at the time the NAFTA entered into force is a "discreditable and aberrant episode" that should be ignored (Claimants' Reply to Canada's Post Hearing Submission, 31 January 2011, ¶ 10). The Claimants provide no basis for this suggestion, nor explain how it is consistent with the express agreement of the three NAFTA Parties (see Canada's Post Hearing Submission, 3 December 2010, fn. 13). The Claimants also argue that Canada is barred from relying on the provincial reservation because, the Claimants assert, Canada raised the reservation for the first time at the hearing. This is not correct – Canada noted in its Counter Memorial that the Guidelines are reserved under the provincial reservation (see Counter Memorial, ¶ 223 and fn. 348). Even if Canada did only raise the reservation for the first time at the hearing – which it did not - this is only because the Claimants did not challenge that the Guidelines were subordinate to the federal Act until immediately before that hearing (see Claimants' Submission on the US and Mexico's NAFTA Article 1128 Submissions, 1 September 2010, ¶¶ 34-43).

[9] Article 2(f)(ii), Annex I.

[10] Canada's Reply to Claimants' Post Hearing Brief, 31 January 2011, ¶¶ 36-37; Canada's Post Hearing Submission, 3 December 2010, ¶ 26 ("Whether a domestic measure is adopted under the authority of and consistent with another domestic measure can only be determined under domestic law.").

[11] Submission of the United Mexican States Responding to Questions Raised by the Tribunal, 21 January 2011, ¶ 3.

10. While the United States stated that a tribunal must apply the "law of the NAFTA" to determine whether a domestic measure is "consistent with" another domestic measure listed in Annex I,[12] it stated that a tribunal must also apply domestic law:

> Because a measure is taken by a Party under its national law, the Tribunal must look to the national law context under which the subordinate measure in question was adopted or maintained to determine whether it is in fact authorized under and consistent with the relevant measure.[13]

11. Thus, all three NAFTA parties agree that the Tribunal "must" examine domestic law when deciding if an alleged subordinate measure is "consistent with" a measure listed in Annex I. This agreement is both a "subsequent agreement" and "subsequent practice" for the purposes of Article 31(3) of the Vienna Convention on the Law of Treaties.[14] Such agreement and practice "shall be taken into account"[15] by the Tribunal and is presumptively conclusive since "it constitutes objective evidence of the understanding of the parties as to the meaning of the treaty."[16]

12. Consistent with the interpretation agreed by the three NAFTA parties, the Tribunal should apply domestic law to determine whether the Guidelines are subordinate to the Accord Implementation Acts.[17] Thus, it should apply the decisions of the Canadian courts that the Guidelines are authorized by, and consistent with, those Acts.[18]

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[12] Second Submission of the United States of America, 21 January 2011, ¶ 9.

[13] Id., ¶ 6.

[14] **CA-9**, Vienna Convention on the Law of Treaties, 23 May 1969, art. 31(3). See Canada's Response to 1128 Submissions, 1 September 2010, ¶¶ 7, 9, 12; Hearing Transcript, pp. 1227:15 – 1228:13.

[15] **CA-9**, Vienna Convention on the Law of Treaties, art. 31(3)(a)-(b).

[16] **RA-158**, Yearbook of the International Law Commission, pp. 221-222, ¶ 15, quoted in Canada's Response to Article 1128 Submissions, 1 September 2010, ¶ 11. See also Hearing Transcript, pp. 1229:20 – 1230:4.

[17] Canada's Reply to Claimants' Post Hearing Brief, 31 January 2011, ¶¶ 33-37.

[18] Id., ¶¶ 38-53.

IV. THE NAFTA PARTIES AGREE THAT AN ALLEGED SUBORDINATE MEASURE CAN BE CONSISTENT WITH A LISTED MEASURE EVEN IF IT IMPOSES ADDITIONAL OR MORE ONEROUS BURDENS

13. Canada previously confirmed that "[a] measure can be 'consistent with' a measure listed in Annex I of the NAFTA even if it imposes additional and/or more onerous burdens on a legal or natural person who is subject to that measure."[19] Mexico and the United States agree. Mexico stated that "[a] subordinate measure can be 'consistent with the [listed] measure' if it imposes additional and/or more onerous burdens."[20] The United States effectively agreed, noting that "the phrase 'additional and/or more onerous burdens,' is not found in the NAFTA." The United States went on to state the factors on which it believes a tribunal can rely to decide if an alleged subordinate measure is consistent with a listed measure.[21] None of those factors are the burdens, more onerous or not, imposed on the investor.

14. Thus, the three NAFTA Parties agree that a measure can be "consistent with" a measure listed in Annex I of the NAFTA even if it imposes additional and/or more onerous burdens. This is both a subsequent agreement and subsequent practice the Tribunal should apply under Article 31(3) of the Vienna Convention. Consequently, even if the Guidelines impose additional or more onerous burdens on the Claimants – which they do not – they are still subordinate to the Accord Implementation Acts and fall into the reservations for those measures.

V. THE CLAIMANTS DRAW TOO MUCH FROM THE SECOND ARTICLE 1128 SUBMISSION OF THE UNITED STATES

15. As noted above, in addition to agreeing with Mexico and Canada that the Tribunal "must" apply domestic law to determine if a measure is subordinate for the purposes of

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[19] Canada's Post Hearing Submission, 3 December 2010, ¶ 33.

[20] Submission of the United Mexican States Responding to Questions Raised by the Tribunal, 21 January 2011, ¶ 5.

[21] Second Submission of the United States of America, 21 January 2011, ¶ 10.

Article 2(f)(ii) of NAFTA Annex I, the United States also stated that the Tribunal must apply the "law of the NAFTA." It stated that:

> For the NAFTA, considerations in relevant cases would include the context of the reservation the Parties negotiated, including the NAFTA obligation from which the listed measure is reserved and the degree of the reserved measure's and subordinate measure's non-conformity with that obligation, in light of the other elements of the reservation that would be relevant.[22]

16. In their response to Canada's Post Hearing Submission, the Claimants draw from this paragraph the conclusion that "a future subordinate measure cannot be consistent with a reserved measure for the purposes of Annex I if it decreases the conformity of that measure with the Treaty."[23] The Claimants draw too much.

17. While the United States believes that conformity with the obligation may be important in "relevant cases,"[24] it does not mention the circumstances in which it will be important. Thus, the submission is consistent with an interpretation that the conformity with a substantive obligation is only relevant where the reservation is being phased out, is qualified, or where there is a material discrepancy between the elements.[25] The parties agree that none of these circumstances is present in this case.[26]

18. The Claimants' interpretation of the United States' submission eliminates the distinction between Article 2(f)(ii) of Annex I and Article 1108(1)(c). The latter Article prevents an amendment to a listed measure which "decrease[s] the conformity of the measure ... with" Article 1106. Under the Claimants' interpretation of the United States' submission, this same test would apply to determine if a measure is "consistent with" a listed measure, for the purposes of Article 2(f)(ii) of Annex I. Yet, there is nothing in the

[22] Second Submission of the United States of America, 21 January 2011, ¶ 9.

[23] Claimants' Reply to Canada's Post Hearing Submission, 31 January 2011, ¶ 17.

[24] Second Submission of the United States of America, 21 January 2011, ¶ 9.

[25] See Annex I, ¶ 3(a)-(c).

[26] Canada's Post Hearing Submission, 3 December 2010, ¶ 11; Claimants' Redacted Post-Hearing Brief, 7 January 2011, ¶ 15 ("There is no liberalization commitment in the Accord Act reservation.").

United States' submission which supports the conflation of these two Articles with entirely separate texts and purposes.[27]

19. Even if the Claimants' interpretation of the United States' submission was accepted, the Guidelines are still reserved. Article 1106(1)(c) of the NAFTA prohibits requirements "to purchase, use or accord a preference to goods produced or services provided in its territory, or to purchase goods or services from persons in its territory." The Claimants have failed to prove that the Guidelines decrease the conformity of the Accord Implementation Acts with Article 1106(1)(c) because they have failed to prove that the Guidelines increase any requirement in the benefits regime to purchase, use or accord a preference to domestic goods or services. The Claimants continue to challenge administrative features of the Guidelines which have nothing to do with the purchase, use or accordance of a preference to local goods or services.[28] The Claimants also challenge the requirement to expend a certain percentage of revenues on R&D and E&T. However, this requirement is consistent with the Claimants' obligation under the Accord Acts and benefits decisions to expend on R&D and E&T and report those expenditure to the Board.[29]

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Respectfully submitted
on behalf of Canada,

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[27] See Canada's Post Hearing Submission, 3 December 2010, ¶¶ 33-47.

[28] See further Rejoinder, ¶ 120.

[29] See further Rejoinder, ¶ 119.