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CERTIFICATE

The Loewen Group, Inc. and Raymond L. Loewen
v.

United States of America
(ICSID Case No. ARB(AF)/98/3)

I hereby certify that the attached is a true copy of the Decision of the Arbitral Tribunal on Hearing of Respondent's Objection to Competence and Jurisdiction, dated January 5, 2001.

Antonio R. Parra
Acting Secretary-General

Washington, D.C., January 9, 2001

The Loewen Group, Inc. and Raymond L. Loewen

v

United States of America

(ICSID Case No. ARB(AF)/98/3)

Decision on hearing of Respondent's objection to competence and jurisdiction

I. INTRODUCTION

1. This dispute arises out of litigation brought against the first Claimant, the Loewen Group, Inc ('TLGI') and Loewen Group International, Inc ('LGII'), its principal United States subsidiary, in Mississippi State Court by Jeremiah O'Keefe Sr., his son and various companies owned by the O'Keefe family (collectively called 'O'Keefe'). The litigation arose out of a commercial dispute between O'Keefe and the Loewen companies which are competitors in the funeral home and funeral insurance business in Mississippi. The dispute concerned three contracts between O'Keefe and the Loewen companies said to be valued by O'Keefe at $980,000 and an exchange of two O'Keefe funeral homes said to be worth $2.5 million for a Loewen insurance company worth $4 million approximately.

2. The Mississippi jury awarded O'Keefe $500 million damages, including $75 million damages for emotional distress and $400 million punitive damages. The verdict was the outcome of a seven-week trial in which, according to the Claimants, the trial judge repeatedly allowed O'Keefe's attorneys to make extensive irrelevant and highly prejudicial references (I) to the Claimants' foreign nationality (which was contrasted to O'Keefe's Mississippi roots); (ii) race-based distinctions between O'Keefe and the Loewen companies; and (iii) class-based distinctions between the Loewen companies (which were portrayed as large wealthy corporations) and O'Keefe (who was portrayed as running family-owned businesses). Further, according to the Claimants, after permitting those references, the trial judge refused to give an instruction to the jury stating clearly that nationality-based, racial and class-based discrimination was impermissible.

3. The Loewen companies sought to appeal the $500 million verdict and judgment but were confronted with the application of an appellate bond requirement. Mississippi law requires an appeal bond for 125% of the

judgment, but allows the bond to be reduced or dispensed with for 'good cause'.

4. Despite the Claimants' claim that there was good cause to reduce the appeal bond, the Mississippi Supreme Court refused to reduce the appeal bond at all and required the Loewen companies to post a $625 million bond within seven days in order to pursue its appeal without facing immediate execution of the judgment. According to the Claimants, that decision effectively foreclosed the Loewen companies' appeal rights.

5. The Claimants allege that the Loewen companies were then forced to settle the case 'under extreme duress'. Other alternatives to settlement were said to be catastrophic and/or unavailable. On January 29, 1996, with execution against their Mississippi assets scheduled to start the next day, the Loewen companies entered into a settlement with O'Keefe under which they agreed to pay $175 million.

6. In this claim the Claimants seek compensation for damage inflicted upon TLGI and LGII and for damage to the second Claimant's interests as a direct result of alleged violations of Chapter Eleven of the North American Free Trade Agreement ('NAFTA') committed primarily by the State of Mississippi in the course of the litigation.

II. THE PARTIES

7. The first Claimant TLGI is a Canadian corporation which carries on business in Canada and the United States. The second Claimant is Raymond Loewen, a Canadian citizen who was the founder of TLGI and its principal shareholder and chief executive officer.

8. Raymond Loewen submits his claim as 'the investor of a party' on behalf of TLGI under NAFTA, Article 1117.

9. In these proceedings, until June 1, 1999 the Claimants were represented and from that date the first Claimant has been represented by:

Mr Christopher F. Dugan	Jones, Day, Reavis & Pogue
Mr James A. Wilderotter	Jones, Day, Reavis & Pogue
Mr Gregory A. Castanias	Jones, Day, Reavis & Pogue

From June 21, 1999 the second Claimant has been represented by:

Mr John H. Lewis, Jr.	Montgomery, McCracken, Walker & Rhoads

10. The Respondent is the Government of the United States of America. It has been represented by:

Mr Kenneth L. Doroshow	U.S. Department of Justice
Mr Mark A. Clodfelter	U.S. Department of State
Mr Barton Legum	U.S. Department of State

11. The Government of Canada on September 7, 2000 and the Government of Mexico on September 7, 2000 gave written notice of their intention to attend the hearing on competence and jurisdiction.

12. Canada has been represented by:
Mr Fulvio Fracassi, Department of Foreign Affairs and International Trade, Ottawa, Canada

13. Mexico has been represented by:
Mr Hugo Perezcano Díaz, Secretaría de Commercio y Fomento Industrial (SECOFI), Mexico City, Mexico

III. PROCEDURAL HISTORY

14. On July 29, 1998 the Claimants delivered to the Respondent a Notice of Intent to Submit a Claim to Arbitration in accordance with NAFTA, Article 1119. On October 30, 1999 the Claimants delivered to the Respondent a written consent and waiver in compliance with NAFTA, Article 1121(2)(a) and (b).

15. On July 29, 1998, and pursuant to NAFTA, Article 1120, the Claimants filed their Notice of Claim with the International Centre for Settlement of Investment Disputes ('ICSID') and requested the Secretary-General of ICSID to approve and register its application and to permit access to the ICSID Additional Facility.

16. On November 19, 1998, the Secretary-General of ICSID informed the parties that the requirements of Article 4(2) of the ICSID Additional Facility Rules had been fulfilled and that the Claimants' access to the Additional Facility was approved. The Secretary-General of ICSID issued a Certificate of Registration of the Notice of Claim on the same day.

17. On March 17, 1999 the Tribunal was constituted. The Secretary-General of ICSID informed the parties that the Tribunal was 'deemed to have been constituted and the proceedings to have begun' on March 17, 1999, and that Ms Margrete Stevens, ICSID, would serve as Secretary of the Tribunal. All subsequent written communications between the Tribunal and the parties were made through the ICSID Secretariat.

18. On April 6, 1999, the Respondent filed an objection that the dispute is not within the competence of the Tribunal. The Respondent requested that the objection be dealt with by the Tribunal as a preliminary question and that the parties be given an opportunity to brief the issue in accordance with a separate schedule pursuant to Article 38 of the Additional Facility Rules.

19. The first session of the Tribunal was held, with the parties' agreement, in Washington D.C. on May 18, 1999. In accordance with Article 21 of the ICSID Arbitration (Additional Facility) Rules ('the Rules'), the Tribunal determined, with the agreement of the parties, that the place of arbitration would be Washington D.C.

20. The President noted the parties' agreement that the quorum for sittings of the Tribunal would be constituted by all three of its members. It was also noted that the Tribunal could take decisions by correspondence among its members, or by any other appropriate means of communication, provided that all members were consulted. Decisions of the Tribunal would be taken by the majority of its members.

21. The Tribunal made the following orders:

(1) The Claimants to file their memorial by Monday, July 19, 1999.

(2) Respondent to file its memorial on competence and jurisdiction, if any, stating the grounds of its objection, by Wednesday, August 18, 1999.

(3) Following receipt of the Respondent's memorial on competence and jurisdiction, if any, the Tribunal will rule whether the objection to jurisdiction and competence will be determined as a preliminary matter or joined to the merits of the dispute. The Tribunal reserves the right to call for a written response from the Claimants before giving its decision on the question whether competence and jurisdiction will be determined as a preliminary matter or otherwise.

(4) The Respondent to file its counter-memorial on the merits within 60 days after either the Respondent's not filing a memorial on competence and jurisdiction within the time limited or the Tribunal's determination that the objection to jurisdiction and competence shall be joined to the merits.

(5) Having regard to the statement made by the Claimants' counsel the Respondent shall be entitled to reasonable discovery within the time limit for the filing of its counter-memorial but that entitlement shall be exercised only for the purpose of the Respondent formulating its memorial on jurisdiction and competence and its counter-memorial.

22. On July 6, 1999 the Tribunal confirmed that, by subsequent agreement of the parties,

(1) the Claimants were to file their memorial by Monday, October 18, 1999; and

(2) the Respondent was to file its memorial on jurisdiction and competence, if any, by Friday, December 18, 1999.

23. Each Claimant through its attorneys has filed its own memorial, written submission and final submission on competence and jurisdiction, and has made its own submissions.

24. On May 26, 1999, the Respondent requested that all filings in this matter, not excluding the minutes of proceedings, be treated as open and available to the public. The Claimants agreed that the minutes and other filings should be publicly available but only after the matter is concluded.

25. On September 28, 1999, the Tribunal delivered its Decision on the Respondent's request for a ruling on disclosure. By its Decision the Tribunal noted that Article 44(2) of the ICSID Additional Facility Arbitration Rules provides that the minutes kept of all hearings pursuant to Article 44(1) 'shall not be published without the consent of the parties'. The Tribunal pointed out that this prohibition is primarily directed to the Tribunal but was understood in the *Metalclad* Arbitration (ICSID Case ARB(AF)/97/1) Decision as being directed to the parties as well. The Tribunal went on to deny the Respondent's request to the extent that it sought to bring about a situation in which the Tribunal or the Secretariat makes available to the public all filings in this case.

26. In its Decision the Tribunal rejected the Claimants' submission that each party is under a general obligation of confidentiality in relation to the proceedings. The Tribunal stated that in an arbitration under NAFTA, it is not to be supposed that, in the absence of express provision, the Convention or the Rules and Regulations impose a general obligation on the parties, the effect of which would be to preclude a Government (or the other party) from discussing the case in public, thereby depriving the public of knowledge and information concerning government and public affairs. The Decision concluded by repeating the comment made by the *Metalclad* Tribunal, namely that it would be of advantage to the orderly unfolding of the arbitral process if during the proceedings the parties were to limit public discussion to what is considered necessary.

27. On November 1, 1999, the Respondent requested a further extension of time until February 18, 2000, within which to file its memorial on competence and jurisdiction. The request, which was opposed by the Claimants, was granted by the Tribunal on December 9, 1999. At the same time the Tribunal dealt with an application by the Respondent for further and better discovery. While rejecting the Respondent's submission that there had been a waiver by the Claimants of attorney-client privilege, the Tribunal ordered that the Respondent was entitled to discovery of the attorney-client communications of the Claimants or either of them relating directly to the issue of duress.

28. On February 14, 2000, the first Claimant sought clarification of the Tribunal's Decision of September 28, 1999, relating to confidentiality. The request followed the release by the Respondent on January 10, 2000 of materials relating to the arbitration, including 'the minutes of the May 18, 1999 hearing before the Tribunal as well as the audio recording of that hearing'. The Respondent interpreted the Decision as merely limiting the right of the Tribunal or the Secretariat to release information, not the right of the parties themselves to release information. On the other hand, the first Claimant interpreted the Decision as restricting the right of the parties to disclose minutes and related material. By its Decision on June 2, 2000 the Tribunal affirmed the correctness of the first Claimant's interpretation of the Decision on September 28, 1999, stating that the Convention and the Rules prohibit publication by the Tribunal and the parties of the minutes and a full record of the hearing and any order made by the Tribunal. However, the Decision of

June 2, 2000 stated that neither it nor the earlier Decision was intended to affect or qualify, or could affect or qualify, any statute-imposed obligation of disclosure by which any party to the arbitration might be bound.

29. By its Decision of June 2, 2000, the Tribunal also dealt with an application by the Respondent for further and better discovery, in particular relating to documents and information reflecting the advice and conclusions of the Claimants and their advisers during the Mississippi proceedings concerning alternatives to settlement of the Mississippi litigation. The Tribunal ordered the Claimants to produce all information in the possession of the Claimants, their counsel or others who acted on their behalf that relates directly to the question whether Loewen had alternatives to entering into the Mississippi settlement. The Tribunal stated that information ordered to be produced should include commitments from lenders for financing the Loewen Group's ongoing operations in anticipation of the possible reorganization filing and draft petitions for the purpose of seeking possible relief from the Mississippi Supreme Court's bonding decision in the US federal courts and the Supreme Court. The documents were to be produced within twenty-one (21) days of June 2, 2000.

IV. THE NATURE OF THE CLAIMANTS' CLAIM

30. The Claimants' case is that

(i) the trial court, by admitting extensive anti-Canadian and pro-American testimony and prejudicial counsel comment, violated Article 1102 of NAFTA which bars discrimination against foreign investors and their investments;

(ii) the discrimination tainted the inexplicably large verdict;

(iii) the trial court, by permitting extensive nationality-based, racial and class-based testimony and counsel comments, violated Article 1105 of NAFTA which imposes a minimum standard of treatment for investments of foreign investors;

(iv) the excessive verdict and judgment (even apart from the discrimination) violated Article 1105;

(v) the Mississippi courts' arbitrary application of the bonding requirement violated Article 1105; and

(vi) the discriminatory conduct, the excessive verdict, the denial of the Loewen companies' right to appeal and the coerced settlement violated Article 1110 of NAFTA, which bars the uncompensated appropriation of investments of foreign investors.

31. The Claimants allege that the Respondent is liable for Mississippi's NAFTA breaches under Article 105, which requires that the Parties to NAFTA shall ensure that all necessary measures are taken to give effect to the provisions of the Agreement, including their observance by State and provincial governments. The Claimants also allege that, by tolerating the misconduct which occurred during the O'Keefe litigation, the Respondent directly breached Article 1105, which imposes affirmative duties on the Respondent to provide 'full protection and security' to investments of foreign investors, including 'full protection and security' against third party misconduct.

V. THE RESPONDENT'S OBJECTION TO COMPETENCE AND JURISDICTION

32. By its Memorial on Competence and Jurisdiction, the Respondent objected to the competence and jurisdiction of this Tribunal on the following grounds:

(i) the claim is not arbitrable because the judgments of domestic courts in purely private disputes are not 'measures adopted or maintained by a Party' within the scope of NAFTA Chapter II;

(ii) the Mississippi court judgments complained of are not 'measures adopted or maintained by a Party' and cannot give rise to a breach of Chapter Eleven as a matter of law because they were not final acts of the United States judicial system;

(iii) a private agreement to settle a litigation matter out of court is not a government 'measure' within the scope of NAFTA Chapter II;

(iv) the Mississippi trial court's alleged failure to protect against the alien-based, racial and class-based references cannot be a 'measure' because Loewen never objected to such references during the trial; and

(v) Raymond Loewen's Article 1117 claims should be dismissed because he does not 'own or control' the enterprise at issue.

33. Each of the Claimants filed submissions in answer to the Respondent's objections contesting each of the grounds of objection advanced by the Respondent. The Respondent filed its final submissions in reply. The Claimants then filed submissions in response.

34. The hearing on the Respondent's objection to competence and jurisdiction took place in Washington D.C. on September 20, 21 and 22, 2000.

35. After the conclusion of the oral hearing, pursuant to an order made by the Tribunal, the Government of Mexico filed, on October 16, 2000, submissions concerning certain matters of interpretation of NAFTA which addressed the effect of Article 1121, the meaning of the word 'measure', the rights of an investor to advance a claim under Article 1117 and the decisions in *Azinian v United Mexican States* Case No. ARB(AF)/97/2; 14 ICSID Review-FILJ 538 and *Metalclad v United Mexican States* Case No. ARB(AF) 97/1 which were referred to in oral argument by the disputing parties.

36. The disputing parties responded to Mexico's submission by filing written submissions pursuant to the order made by the Tribunal at the conclusion of the oral hearing on September 22, 2000. It will be convenient to refer to Mexico's submissions when we consider the Respondent's grounds of objection.

37. In determining the Respondent's objection, it is proper to look at the Claimants' notice of claim for it is by the Notice of Claim itself and the request for arbitration that the Claimants submit their claim to arbitration under Articles 1116 and 1117 of NAFTA. It has not been suggested that there is in this case any material difference between the nature of the claim formulated in the Notice of Claim and that formulated in the Memorials filed by the Claimants.

38. No distinction has been drawn in the submissions of the disputing parties between the concepts of competence and jurisdiction. The ICSID Arbitration (Additional Facility) Rules make specific provision for objections to 'competence' (Article 46) but make no such provision for objections to 'jurisdiction'. Article 46 has been applied on the footing that it extends to objections which go to jurisdiction as well as objections going to the constitution and composition of the Tribunal.

VI. THE RESPONDENT'S FIRST GROUND OF OBJECTION: WHETHER JUDICIAL ACTS IN LITIGATION BETWEEN PRIVATE PARTIES ARE 'MEASURES' REGULATED BY NAFTA?

39. Article 1101(1) of NAFTA provides:

'This Chapter [Eleven] applies to measures adopted or maintained by a party' relating to:

(a) investors of another Party;

(b) investments of investors of another Party in the territory of the Party; ...'

40. Article 201 defines 'measure' as including 'any law, regulation, procedure, requirement or practice'. The breadth of this inclusive definition, notably the references to 'law, procedure, requirement or practice', is inconsistent with the notion that judicial action is an exclusion from the generality of the expression 'measures'. 'Law' comprehends judge-made as well as statute-based rules. 'Procedure' is apt to include judicial as well as legislative procedure. 'Requirement' is capable of covering a court order which requires a party to do an act or to pay a sum of money, while 'practice' is capable of denoting the practice of courts as well as the practice of other bodies.

41. Article 1019(1), which requires each Party to promptly publish any law, regulation, precedential judicial decision, administrative ruling of general application and any procedure ... regarding government procurement' differs from the definition of 'measure' in Article 201, which contains no explicit reference to judicial decisions. While Article 1019(1) is directed only to the imposition of an obligation to publish rules of general application, it does not follow that this obligation should be regarded as co-extensive with the inclusive definition of 'measure' or as confining what the definition comprehends. Although Article 1019 clearly indicates that a precedential judicial decision is not only a 'measure' but also a measure 'adopted or maintained by a Party', the Article is consistent with the Respondent's submission that 'measures' does not extend to every judicial action.

42. Other NAFTA provisions indicate that judicial action is not beyond the reach of the word 'measures'. Article 1716, in requiring a NAFTA Party to provide 'that its judicial authorities shall have the authority to order prompt and effective provisional measures' to prevent infringement of intellectual property rights, recognises that judicial orders may constitute 'measures'. Article 1715 requires a Party to provide specified 'civil judicial procedures' for the enforcement of intellectual property rights. These 'procedures' extend to the making of a variety of judicial orders, including final judgments (Article 1715(2)). Article 1701(1) is concerned to ensure that 'measures to enforce

intellectual property rights do not themselves become barriers to legitimate trade'. Plainly 'measures' there includes the judicial procedures in Article 1715 i.e. judicial orders. See also Article 1715(2)(f) (where the reference to 'measures ... taken' must be understood as referring to judicial acts, including injunctions and other enforcement procedures).

43. The Respondent concedes that when a government entity is involved in a domestic court proceeding, it may be that, in appropriate circumstances, a resulting court judgment constitutes a 'measure adopted or maintained by a Party'. This concession is at odds with the argument that the failure to mention 'judicial order' or 'judgment' in Article 201 signifies an intention to confine 'measures' to legislative and executive actions. In general, where the meaning of 'measures' is so confined, the restricted meaning arises from an express limitation or an implied limitation arising from the context. No such limitation is to be found in Article 201.

44. Nor can 'measures' be confined to provisional or interim judicial acts as distinct from final judicial acts. Such a distinction finds support neither in Article 1701 nor Chapter 10 of NAFTA (which applies to 'measures adopted or maintained by a Party relating to procurement'). The reference in Article 1019(1) to 'precedential judicial decision' which is one instance of a measure 'adopted or maintained by a Party', is to a final decision as well as a provisional decision. See also Annex 1010.1B paras 2 and 3.

45. The approach which this Tribunal takes to the interpretation of 'measures' accords with the interpretation given to the expression in international law where it has been understood to include judicial acts. In *Regina v Pierre Bouchereau*, Case 30 77 [1977] ECR 1999, the European Court of Justice rejected the argument that 'measure' excludes actions of the judiciary, holding that the word embraces 'any action which affects the rights of persons' coming within the application of the relevant treaty provision (at 11). In the *Fisheries Jurisdiction Case (Spain v Canada)*, No. 96 (ICJ 4 December 1998), the International Court of Justice stated that 'in its ordinary sense the word ['measure'] is wide enough to cover any act, step or proceeding, and imposes no particular limit on their material content or on the aim pursued thereby' (at 66). See also *Oil Fields of Texas Inc v NIOC*, 12 Iran-US Cr Trib Rep 308 (1986) at 318-319 (where the judicial acts in question were held to be expropriations within the expression 'expropriations

or other measures affecting property rights', thus amounting to 'measures affecting property rights').

46. The significance for this case of the interpretation of 'measures' in the context of international law is that Article 102(2) of NAFTA requires the Parties to interpret and apply its provisions 'in the light of its objectives set out in paragraph 1 and in accordance with applicable rules of international law'. Further, an interpretation of 'measures' which extends to judicial acts conforms to the objectives of NAFTA as set out in Article 102(1), more particularly objectives (b), (c) and (e), namely to

> '(b) promote conditions of fair competition in the free trade area;
>
> (c) increase substantially investment opportunities in the territories of the Parties;
>
> ...
>
> (e) create effective procedures for the implementation and application of this Agreement, for its joint administration and for the resolution of disputes'.

47. Such an interpretation of the word 'measures' accords with the general principle of State responsibility. The principle applies to the acts of judicial as well as legislative and administrative organs. (See draft Article 4 on State Responsibility adopted by the International Law Commission and later provisionally adopted by the United Nations General Assembly Drafting Committee on its second reading, Geneva, May 1–June 9, July 10-August 18, 2000, A/CN.4/L.600, August 21, 2000.) In *Azinian v United Mexican States* Case No. ARB(AF)/97/2, 14 ICSID Review-FILJ 538, the Tribunal, in rejecting the claim that there were violations of NAFTA, quoted (at 567) with approval the comments made by the former President of the International Court of Justice who, after acknowledging the reluctance in some arbitral awards of the last century to admit that the State is responsible for judicial actions, stated:

> '... in the present century State responsibility for judicial acts came to be recognized. Although independent of Government, the judiciary is not independent of the State: the judgment given by a judicial authority emanates from an organ of the State in just the same way as a law promulgated by the legislature or a decision taken by the executive.'
>
> (Eduardo Jimenez de Aréchaga, 'International Law in the Past Third of a Century', 159-1 Recueil des Cours (General Course in Public International Law, The Hague, 1978).

The former President went on to say that State responsibility for acts of judicial authorities may result from three types of judicial decision, the first of which is a decision of a municipal court clearly incompatible with a rule of international law. The second type is what is known traditionally as a denial of justice. The Claimants assert that the NAFTA violations of which they complain fall within these categories of judicial decision.

48. The *Azinian* Tribunal pointed out (at 568) that State responsibility for judicial decisions does not entitle a claimant to a review of national court decisions as though the international jurisdiction seised has plenary appellate jurisdiction. This is neither true generally nor for NAFTA. As the Tribunal said,

> 'What must be shown is that the court decision itself constitutes a violation of the treaty' (at 568).

49. The views expressed by the *Azinian* Tribunal were not necessary for the decision in that case because it involved no challenge to the decisions of the Mexican courts. Subject to our later consideration of the rule of exhaustion of local remedies and the rule of judicial finality, the views are nonetheless persuasive and support our view that 'measures' in Chapter Eleven, according to its true interpretation, does not exclude judicial acts.

50. A Tribunal established pursuant to NAFTA Chapter Eleven, Section B, must decide the issues in accordance with the provisions of NAFTA and applicable rules of international law (Article 1131(1)). Further, as already noted, Article 102(2) provides that the Agreement must be interpreted in the light of its stated objectives and in accordance with applicable rules of international law. These objectives include the promotion of conditions of fair competition in the free trade area, the increase of investment opportunities and the creation of effective procedures for the resolution of disputes (Article 102(1)(b), (c) and (e)).

51. Guided by these objectives and principles, we do not accept the Respondent's submission that NAFTA is to be understood in accordance with the principle that treaties are to be interpreted in deference to the sovereignty of states. In *AMCO Asia Corp v Republic of Indonesia* 1 ICSID Reports 377 (1983) the Tribunal rejected the suggested principle (at 394, 397). Whatever the status of this suggested principle may have been in earlier times, the

Vienna Convention on the Law of Treaties is the primary guide to the interpretation of the provisions of NAFTA (*Ethyl Corporation v Canada*, Award on Jurisdiction, June 24, 1998, at 55-56, 38 ILM 708 (where a NAFTA Tribunal expressly rejected the argument that Section B of Chapter 11 is to be construed strictly). See also *Pope & Talbot v Canada*, Interim Award, June 26, 2000 (where a NAFTA Tribunal adopted a broad interpretation of the expression 'investment' in Article 1110). NAFTA is to be interpreted in good faith in accordance with the ordinary meaning to be given to its terms in their context and in the light of its object and purpose (Vienna Convention, Article 31(1)). The context includes the preamble and annexes (Vienna Convention, Article 31(2)).

52. We agree with the Respondent that not every judicial act on the part of the courts of a Party constitutes a measure 'adopted or maintained by a Party'. Mexico submits that, in order to constitute a 'measure', the judicial action under consideration must have a general application. Thus a judicial affirmation of a general principle might well constitute a measure, whereas a specific order requiring a defendant to pay a sum of money would not. The definition of 'measure' in Article 201 (which includes 'requirement') is by no means consistent with this argument.

53. The question then arises whether the words 'measures adopted or maintained by a Party' should be understood, as the Respondent argues, to exclude judicial acts being the judgments of domestic courts in purely private matters. The purpose of Chapter Eleven, 'Section B – Settlement of Disputes between a Party and an Investor of Another Party' is to establish 'a mechanism for the settlement of investment disputes that assures both equal treatment among investors of the Parties in accordance with the principle of international reciprocity and due process before an arbitral tribunal'. The text, context and purpose of Chapter Eleven combine to support a liberal rather than a restricted interpretation of the words 'measures adopted or maintained by a Party', that is, an interpretation which provides protection and security for the foreign investor and its investment: see *Ethyl Corporation v Canada*, Award on Jurisdiction, June 24, 1998, 38 ILM 708, (where the NAFTA Tribunal concluded that the object and purpose of Chapter Eleven is to 'create effective procedures ... for the resolution of disputes' and to 'increase substantially investment opportunities' (at 83)).

54. Neither in the text or context of NAFTA nor in international law is there to be found support for the Respondent's submission that measures adopted or maintained by a Party', in its application to judicial acts, excludes the judgments of domestic courts in purely private disputes. Neither the definition of 'measure' in Article 201 nor the provisions of Chapters 10 and 17 relating to 'measures' and 'procedures' contain any indication that, in its application to judicial acts, the existence of a measure depends upon the identity of the litigants or the characterisation of the dispute as public or private. An adequate mechanism for the settlement of disputes as contemplated by Chapter Eleven must extend to disputes, whether public or private, so long as the State Party is responsible for the judicial act which constitutes the 'measure' complained of, and that act constitutes a breach of a NAFTA obligation, as for example a discriminatory precedential judicial decision. The principle that a State is responsible for the decisions of its municipal courts (or at least its highest court) supports the wider interpretation of the expression 'measure adopted or maintained by a Party' rather than the restricted interpretation advanced by the Respondent.

55. Generally speaking, litigation between private parties is less likely to generate a 'measure adopted or maintained by a Party' but, in some circumstances, private litigation may do so. In this respect, we do not regard the discussion of private litigation in *Retail, Wholesale and Department Store Union, Local 580 v Dolphin Delivery Ltd* [1986] 2 SCR 572, upon which the Respondent relies, as influential in the present context. The discussion relates to s. 32(1) of the Canadian Charter of Rights and Freedoms which applies Charter provisions to the legislative, executive and administrative branches (but not the judicial branch) of government.

56. As the Claimants submit, the Mississippi trial court's judgment ordering Loewen to pay O'Keefe $500 million and the Mississippi Supreme Court requirement that Loewen post a $625 million bond were 'requirements' within the meaning of the definition of 'measure' in Article 201, subject to consideration of Article 1121, the principle of finality of judicial acts and the rule of exhaustion of local remedies.

57. The Respondent argues that the words 'adopted or maintained' in Article 1101 are indicative of an intent to limit Chapter 11 to those actions that involve ratification by government. This limitation, so the Respondent submits, accords with the 'act of state' doctrine. That doctrine is a doctrine of

municipal rather than international law. See *W.S. Kirkpatrick & Co Inc v Environmental Tectonics Corporation International* 493 US 400 (1990) at 404 (where the Court acknowledged that it had 'once viewed the doctrine as an expression of international law' but had more recently described it 'as a consequence of domestic separation of powers, reflecting the strong sense of the Judicial Branch that its engagement in the task of passing on the validity of foreign acts of state may hinder the conduct of foreign affairs (*Banco Nacional de Cuba v Sabbatino* 376 US 398, 423 (1964))'. No authority and no materials have been placed before us which justify the conclusion that the act of State doctrine has been adopted by sufficient countries to be considered as a rule of international law pursuant to Article 38 of the Statute of the International Court of Justice. In any event, the act of State doctrine is now expressed in terms of 'acts of a governmental character done by a foreign state within its own territory and applicable there' (Restatement (Third) of Foreign Relations Laws of the United States §443(1)), without differentiating between 'public' and 'private' litigation.

58. Whatever the effect of the act of State doctrine may be, Article 1105, in requiring a Party to provide 'full protection and security' to investments of investors, must extend to the protection of foreign investors from private parties when they act through the judicial organs of the State.

59. Further, the award of punitive damages would satisfy the public element of the Respondent's public/private dichotomy. It is generally accepted that punitive damages awards are intended to serve the public interest (D.B. Dobbs, Dobbs Law of Remedies §3.11(1) at 457 (2d ed 1993).

60. We reject therefore the Respondent's objection that the Mississippi Court judgments are not 'measures adopted or maintained by a Party' because they resolved a dispute between private parties.

VII. THE RESPONDENT'S SECOND GROUND OF OBJECTION: THE MISSISSIPPI COURT JUDGMENTS ARE NOT 'MEASURES ADOPTED OR MAINTAINED BY A PARTY' AND CANNOT GIVE RISE TO A BREACH OF CHAPTER 11 BECAUSE THEY WERE NOT FINAL ACTS OF THE UNITED STATES JUDICIAL SYSTEM

61. The Respondent argues that the expression 'measures adopted or maintained by a Party' must be understood in the light of the principle of customary international law that, when a claim of injury is based upon judicial

action in a particular case, State responsibility only arises when there is final action by the State's judicial system as a whole. This proposition is based on the notion that judicial action is a single action from beginning to end so that the State has not spoken until all appeals have been exhausted. In other words, the State is not responsible for the errors of its courts when the decision has not been appealed to the court of last resort. The Respondent distinguishes this substantive requirement of customary international law for a final non-appealable judicial action, when an international claim is brought to challenge judicial action, from international law's procedural requirement of exhaustion of local remedies ('the local remedies rule').

62. The Respondent submits that there is nothing to show that in Chapter Eleven the Parties intended to derogate from this substantive rule of international law when judicial action is the basis of the claim for violation of NAFTA. To the contrary, the Respondent argues that the terms of Article 1101, 'adopted or maintained by a Party', incorporate the substantive rule of international law and require finality of action. Only those judicial decisions that have been accepted or upheld by the judicial system as a whole, after all available appeals have been exhausted, so the argument runs, can be said to possess that degree of finality that justifies the description 'adopted or maintained'.

63. The Claimants' response to this argument is that Article 1121(1)(b) of NAFTA requires an arbitral claimant to waive its local remedies, not exhaust them. This Article authorizes the filing of a Chapter 11 claim only if

> 'the investor and the enterprise waive their right to indicate or continue before any administrative tribunal or court under the law of any Party, or other dispute settlement procedures, any proceedings with respect to the measure of the disputing Party that is alleged to be a breach referred to in Article 1116 ...'.

The Claimants submit, first, that 'the Article eliminates the necessity to exhaust local remedies provided by the host country's administrative or judicial courts'. (B. Sepulveda Amor, *International Law and International Sovereignty: The NAFTA and the Claims of Mexican Jurisdiction*, 19 Houston Journal of International Law 565 at 574 (1997)). The Claimants submit, secondly, that the so-called substantive principle of finality is no different from the local remedies rule and that international tribunals have reviewed the

decisions of inferior municipal courts where the exhaustion requirement has been waived or is otherwise inapplicable.

64. The Respondent argues that Article 1121(2)(b) is not a waiver provision and that it does not waive the local remedies rule or for that matter the rule of judicial finality. The Respondent acknowledges, however, that the Article relaxes the local remedies rule to a partial but limited extent, without defining or otherwise indicating what that extent is or may be.

65. Observations of the NAFTA Tribunals in both *Metalclad Corporation v United Mexican States* ICSID Case No. ARB/AF/97/1 (footnote 4) and in the *Azinian Case*, to which we have referred, support the Claimants' case to the extent that it is based on Article 1121(2)(b). But Mexico, in its written submissions to this Tribunal, points out that the *Metalclad* Tribunal which, in the relevant passage, purported to state Mexico's position in that case, did not do so accurately. Mexico also points out that, in the *Azinian Case*, as there was no complaint of any violation of NAFTA based on a judicial act, the Tribunal's observations were not necessary for its decision. Other cases relied upon by the Claimants include *G.W. McNear Inc v United Mexican States*, Docket No. 211. Opinions of the Commissioners 68 at 71, 72 (1928) and *The Texas Company Claim*, Decision 32-B, American-Mexican Cl Rep 142 (1948), but in these cases the relevant treaty waived exhaustion.

66. There is support for the view that no distinction should be drawn between the principle of finality and the local remedies rule. Indeed, Edwin M. Borchard, The Diplomatic Protection of Citizens Abroad 198 (1915), upon which the Respondent relies, stated:

> 'It is a fundamental principle that the acts of inferior judges or courts do not render the state internationally liable when the claimant has failed to exhaust his local means of redress by judicial appeal or otherwise, for only the highest court to which a case is appealable may be considered an authority involving the responsibility of the state'.

In the *Finnish Ships Arbitration* 3 RIAA 1497 (1937) it was pointed out that exhaustion of local remedies meant that there must be a final decision of a court which is the highest in a hierarchy of courts to which the claimant can resort in the host State. Borchard is not the only commentator who regards the principle of finality and the local remedies rule as different sides of the same coin (see C.F. Amerasinghe, Local Remedies in National Law 181 (1990)). And in the *Interhandel Case* (1959) ICJ 6, the claim was dismissed

expressly on the ground that Switzerland 'has not exhausted the local remedies available to it' (at 11, 19, 26-27). Although the case was taken by Interhandel to the United States Supreme Court, the Supreme Court remanded the case to the District Court and proceedings were still pending in that court.

67. While the content of the two rules is similar, if not the same, the rules were thought to serve different purposes. The local remedies rule (described as 'procedural') was designed to ensure that the State where violation of international law occurred should have the opportunity to address it by its own means, within the framework of its own domestic legal system (*Interhandel Case* (1959) ICJ Reports 6 at 27). Most, if not all legal systems, have a self-correcting capacity. In other words, the claimant was bound to take steps to ensure that the self-correcting mechanism of the State's judicial system is fully engaged as a condition precedent to recognition of the State's responsibility for breach of its international obligation. See the Report of the International Law Commission to the United Nations General Assembly, Yearbook of the International Law Commission, 1975, Vol. II, 62. Now, compliance with the local remedies rule is seen as a condition precedent to invoking the responsibility of a State for breach of an international obligation. (See Article 45 of the draft articles on State responsibility, provisionally adopted by the Drafting Committee of the United Nations General Assembly on second reading, based on the draft previously adopted by the International Law Commission (A/CN.A/L.600, August 21, 2000)).

68. On the other hand, the rule of judicial finality (often described as 'substantive') was thought to be directed to the responsibility of the State for judicial acts. As the statement by Borchard, already quoted, makes clear, it was considered that the State was not responsible for the acts of lower courts.

69. Although it has been said that the responsibility of the State for a breach of international law constituted by an alleged judicial action arises only when there is final action by the State's judicial system considered as a whole, it is now recognised that the judiciary is an organ of the State and that judicial action which violates a rule of international law is attributable to the State (A.V. Freeman, *The International Responsibility of States for Denial of Justice*, 31-33 (1970)). The rule of judicial finality was influenced by the principles of separation, independence of the judiciary and respect for the finality of judicial decisions. However, the judiciary, though independent of

Government, is not independent of the State and the judgment of a court proceeds from an organ of the State as does a decision of the executive.

70. The modern view is that conduct of an organ of the State shall be considered as an act of the State under international law, whether the organ be legislative, executive or judicial, whatever position it holds in the organisation of the State. That, in effect, is the principle expressed in draft Article 4 on State Responsibility, provisionally adopted by the Drafting Committee of the United Nations General Assembly, based on the draft previously adopted by the International Law Commission (A/CN.A/L.600, August 21, 2000). Although the draft has not been finally approved, it is a highly persuasive statement of the law on State Responsibility as it presently stands. Draft Article 4 accords with the view expressed by Eduardo Jimenez de Arechaga, the former President of the International Court ('International Law in the Past Third of a Century', 159-1 Recueil des Cours, (General Course in Public International Law, The Hague, 1978).[1]

71. Viewed in this light, the rule of judicial finality is no different from the local remedies rule. Its purpose is to ensure that the State where the violation occurred should have an opportunity to redress it by its own means, within the framework of its own domestic legal system.

72. Just as it was said that the function of the local remedies rule was to establish whether the point had been reached at which the home State may raise the issue on the international level (G. Schwarzenberger, *International Law*, 604, (1957)), now it is the function of the rule to establish that State responsibility for a breach of an international obligation may be invoked.

73. We accept that an important principle of international law should not be held to have been tacitly dispensed with by an international agreement, in the absence of words making clear an intention to do so (*Elettronica Sicula SpA (Elsi) (United States v Italy)* (1989) ICJ 15 at 42). Such an intention may, however, be exhibited by express provisions which are at variance with the continued operation of the relevant principle of international law.

[1] Cited in *Azinian v United Mexican States* Case No. ARB/(AF)/97/2, 14 ICSID Review-FILJ at 567.

74. Having reached this point in our consideration of the arguments, we have concluded that this ground of objection should be dealt with at the hearing on the merits. Our reasons for reaching this conclusion relate partly to the arguments based on Article 1121(2)(b) and Chapter Eleven and partly to other arguments advanced by the Claimants in response to the Respondent's objection. We have already mentioned the lack of specificity in the Respondent's acknowledgment that the Article partially relaxes the local remedies rule. Consideration might be given by the Respondent to the possibility of presenting an argument that Article 1121(2)(b) does no more than curtail or restrict rights that a claimant would otherwise have but for the existence of Article 1121(2)(b). The remarks of the International Court of Justice in *Headquarters Agreement* (Advisory Opinion) ICJ Reports 12 at 29, 42-43, a decision not cited in argument, may have a bearing on the operation of Article 1121(2)(b) and also on the Claimants' submission that an agreement to arbitrate dispenses with any obligation to have recourse to municipal courts. Another argument of the Claimants, namely that the local remedies rule has no application to denial of justice cases, is one that can conveniently be dealt with at the hearing on the merits where the argument can be considered in the context of the particular allegations by the Claimants of denial of justice on which findings can then be made. Similarly put over is consideration of the Respondent's submissions that the Loewen companies failed to pursue various local remedies which, according the Respondent, were open to them and would, if successful, have resulted in an effective remedy under municipal law. The hearing of this ground of objection should therefore stand over to the hearing on the merits.

VIII. THE RESPONDENT'S THIRD GROUND OF OBJECTION: THAT A PRIVATE AGREEMENT TO SETTLE A MATTER OUT OF COURT IS NOT A GOVERNMENT 'MEASURE' WITHIN THE SCOPE OF NAFTA CHAPTER ELEVEN

75. This ground of objection was not strongly pressed. In this case much turns on the circumstances in which the Mississippi proceedings came to be settled and that is a matter which must be dealt with at a hearing on the merits.

IX. THE RESPONDENT'S FOURTH GROUND OF OBJECTION: <u>THAT THE MISSISSIPPI TRIAL COURT'S ALLEGED FAILURE TO PROTECT AGAINST THE ALIEN-BASED, RACIAL AND CLASS-BASED REFERENCES CANNOT BE A 'MEASURE' BECAUSE LOEWEN NEVER OBJECTED TO SUCH REFERENCES DURING THE TRIAL</u>

76. This ground of objection does not, in our view, go to competence or jurisdiction. If the Respondent's case on this point is made out, it could result in a dismissal of the claim. It is an issue which appropriately and conveniently should be heard and determined at a hearing on the merits.

<u>X. THE FIFTH GROUND OF OBJECTION:</u> <u>RAYMOND LOEWEN'S ARTICLE 1117 CLAIM SHOULD BE DISMISSED BECAUSE HE DOES NOT OWN OR CONTROL THE ENTERPRISE AT ISSUE</u>

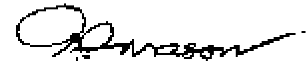
The objection on this ground, if upheld, would not be dispositive of the second Claimant's entire claim which is partly based on Article 1116. Further, it is far from clear that the objection goes to jurisdiction and, in any event, it is an objection which can be dealt with at the hearing on the merits. For this reason we do not consider it appropriate to decide this question on an objection to competence and jurisdiction.

<u>ORDERS</u>

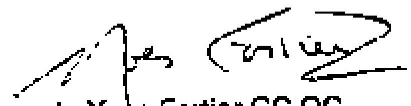
In the result we make the following orders:

1. Dismiss the Respondent's objection to competence and jurisdiction so far as it relates to the first ground of objection.
2. Adjourn the further hearing of the Respondent's other grounds of objection to competence and jurisdiction and join that further hearing to the hearing on the merits.
3. The Respondent to file its counter-memorial on the merits within 60 days of the date of this Decision.
4. The Claimants to file their replies within 60 days of the time limited for the filing of the Respondent's counter-memorial on the merits.

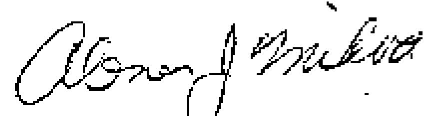
5. The Respondent to file its rejoinder within 60 days of the time limited for the filing of the Claimants' replies.
6. Fix October 15, 2001 as the date of the hearing on the merits.



Sir Anthony Mason, President



L. Yves Fortier CC QC



Judge Abner J. Mikva

DATED the fifth day of January 2001.