EXPROPRIATING EXPROPRIATION LAW: 
THE IMPLICATIONS OF THE METALCLAD DECISION 
ON CANADIAN EXPROPRIATION LAW AND 
ENVIRONMENTAL LAND-USE REGULATION

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THE NORTH AMERICAN FREE TRADE Agreement (NAFTA) Chapter 11 Metalclad case was groundbreaking. It was the first and remains the only finding of an Article 1110 expropriation violation. It was also the first judicial review of any Chapter 11 award. Yet, as important as these developments may be, their significance pales in comparison to the far-reaching budgetary and sovereignty implications of the decision itself. The tribunal gave an expansive interpretation of the types of regulatory measures that could be considered expropriation. Due to the concomitant duty to compensate affected foreign state party investors, the decision threatens to place prohibitive costs on rational environmental management. The central argument of this paper is that while a literal reading of Article 1110 can support the tribunal's interpretation, such an interpretation undermines the underlying purpose of the treaty text - which is to harmonise economic rights. By contrast, the tribunal's reading gives foreign investors much greater proprietary rights than domestic investors, thereby distorting economic competition. The purpose of this paper is to analyse the Metalclad case from a Canadian legal perspective and to assess the public policy implications.

INTRODUCTION

THE METALCLAD ARBITRAL TRIBUNAL decision1 was the first finding of a NAFTA2 Chapter 11 violation of the Article 1110 expropriation protection provision. It was also the first judicial review of any

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1 Metalclad Corporation and The United Mexican States (2000), Case No. ARB(AF)/97/1, (International Centre for the Settlement of Investment Disputes (Additional Facility)) [Metalclad].
Chapter 11 award. Yet, as ground breaking as these two developments may have been for the institutional evolution of the investor-state dispute mechanism (ISDM), their significance pales in comparison to the far-reaching budgetary and sovereignty implications of the decision itself. The tribunal gave an expansive interpretation of the types of governmental measures that could be deemed to be expropriation; thus carrying with them a concomitant duty to compensate affected investors. The tribunal held that expropriation under Article 1110 included:

Not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.

In effect, the tribunal adopted an interpretation of the Article 1110 expropriation protection that would impose an obligation to pay compensation whenever a state party enacts a measure that merely incidentally interferes with investor interests - even economic benefits that are nothing more than anticipated.

On this basis, the tribunal concluded that since the creation of a nature preserve in a rural Mexican province made the future operation of a planned hazardous waste facility impossible, its American investors needed to be compensated. In response to this finding, the lead Mexican counsel before the tribunal expressed his dismay that the decision may very well indicate that whenever "an ecological decree affects the property rights of foreign investors, even if it's lawful under our domestic law, then it should be regarded as a compensable taking." In the judicial review of

3 United Mexican States v. Metalclad Corp. (2001), 89 B.C.L.R. (3d) 359 [hereinafter "Award Review"]. Subsequently, awards have been considered for judicial review in Canada (Attorney General) v. S.D. Myers Inc. [2005] 3 F.C.R. 368 (QL) and The United Mexican States v. Marvin Roy Feldman Karpa, [2003] O.J. No. 5070 (Ont. S.C.J.) (QL). In both cases the courts determined that the tribunal decisions were within the arbitration mandate and thus, there were no grounds for judicial review. See also J.C. Thomas, "A Reply to Professor Brower" (2002) 40 Colum. J. Transnat'l L. 433 at 434.

4 Metalclad, supra note 1 at para. 103.

5 Ibid. at para. 112.

the arbitration decision, Justice Tysoe of the British Columbia Supreme Court also expressed concern regarding the "extremely broad definition" of expropriation.\(^7\) In addition to the conventional notion of expropriation as a taking of property, Tysoe J. observed: \(^8\)

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\text{[T]he Tribunal held that expropriation under the NAFTA includes covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property. This definition is sufficiently broad to include a legitimate rezoning of property by a municipality or other zoning authority.}
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Given this primacy afforded private investment-backed expectations over public policy considerations, the *Metalclad* tribunal expropriation definition could place prohibitive costs on any future environmental regulation. Indeed, the expropriation protection within Chapter 11 had long been a source of great trepidation among NAFTA critics.\(^9\) Until the *Metalclad* decision, the possible extent of the constraints placed upon the environmental regulation of land use had been purely speculative. However, as Tysoe J. noted, henceforth, municipal zoning authorities may need to consider the possibility of compensating foreign landowners for regulatory measures that deprive them of nothing more than expected economic benefits.

Within Canadian zoning law, this is a novel prospect. According to British common law tradition, as articulated in *France Fenwick and Co. Ltd. v. The King*, "A mere negative prohibition, though it involves interference with an owner's enjoyment of property, does not, ...merely because it is obeyed, carry with it at common law any right to compensation. A subject cannot at common law claim compensation merely because he

\(^7\) Award Review, *supra* note 3 at para. 99.

\(^8\) Ibid.

obeys a lawful order of the State."\textsuperscript{10} With respect to municipal zoning authority, the Supreme Court of Canada held in \textit{Hartel Holdings} that if regulatory land use restrictions are implemented pursuant a legitimate and valid planning purpose, the resulting detriment to landowners must be endured in the service of the greater public interest.\textsuperscript{11} For most property owners, this law remains unchanged. Article 1110 expropriation protection only extends to foreign investors from other NAFTA state parties. Yet, if the \textit{Metalclad} decision is indeed a harbinger of future Article 1110 interpretation, then the particular economic interests of American and Mexican investors have been elevated by NAFTA above the common law, and compensation will be required if a zoning authority decides to interfere with their enjoyment of property rights. In other words, if they are to obey the lawful regulatory order of the state, then compensation is due if the regulation diminishes the economic value of their investment. Considering the massive amount of American foreign investment in the Canadian economy, this could place prohibitive costs on any future municipal environmental land-use regulatory measures.\textsuperscript{12}

While municipal zoning authorities, as creatures of provincial statutes, are not directly accountable to international law,\textsuperscript{13} local governments, as one commentator noted, "are of necessity required to be sensitive to the policy objectives of the two senior levels ... [due to] the fundamental mismatch between local governments' revenues and their responsibilities, which implies a measure of financial dependence. With financial


\textsuperscript{11} \textit{Hartel Holdings Co. v. Calgary (City)}, [1984] 1 S.C.R. 337 [\textit{Hartel}].

\textsuperscript{12} In 2001, the United States accounted for $215 billion or 66.9% of foreign direct investment in Canada. The major recipient sectors for foreign direct investment flows into Canada were energy, metallic minerals, machinery and transportation equipment, followed by finance and insurance, food, beverage and tobacco, chemicals and electronics. "Opening Doors to the World Canada's International Market Access Priorities 2003," online: International Trade Canada <http://www.dfait-maeci.gc.ca/tna-nac/2003/3-en.asp>.

dependence goes policy dependence." If a municipality does attempt to regulate in a sector dominated by foreign investment from NAFTA-state-nationals, the federal government, which would be responsible for the payment of any resulting Chapter 11 award, has a number of powerful constitutional and political means by which it could force the offending municipality to absorb the financial penalty. Concerned by the prospect of the federal government passing the costs of future Chapter 11 awards from the national level to the local authority responsible, the Federation of Canadian Municipalities has called on the federal government to "guarantee that it will never penalize municipalities for actions that are valid under domestic law but violate NAFTA." To assess the possible impact the Metalclad decision may have on the capacity of municipal authorities to regulate land use, first this paper will set out the legal regime of Chapter 11 arbitration; second, it will briefly outline the economic and historical rationale for Chapter 11 expropriation protection; third, the initial treatment of Article 1110 by previous arbitration tribunals will be discussed, followed by a detailed account of the Metalclad award decision and subsequent judicial review; fourth, assuming that the Metalclad decision is the current state of Article 1110 law, the paper will discuss in-situ conservation pursuant to the United Nations

Convention on Biological Diversity\textsuperscript{18} to highlight some potential difficulties Article 1110 may now create for land use regulation; fifth, the implications for Canadian expropriation law will be discussed; sixth, recent developments concerning current thinking about Article 1110 will be identified; and finally, the prospects for future Article 1110 reform will be assessed.

THE CHAPTER 11 ARCHITECTURE

According to Daniel Price, one of the United States (U.S.) drafters and negotiators of NAFTA, Chapter 11 has three objectives: first, "to establish a secure investment environment through the elaboration of clear rules of fair treatment of foreign investments and investors;" second, "to remove barriers to investment by eliminating or liberalizing existing restrictions;" and third, "to provide an effective means for the resolution of disputes between an investor and the host government."\textsuperscript{19} Part A of Chapter 11 provides the substantive obligations, while Part B establishes the ISDM by which foreign state party investors seek remedies against host governments for violations of the substantive obligations.

In Section A,\textsuperscript{20} Article 1101 restricts the scope and coverage of the ISDM to investment as defined by Section C. "Investment" is broadly defined as:

- an enterprise;
- an equity security of an enterprise;
- a debt security of an enterprise;
- a loan to an enterprise; or
- a share in income or profits of the enterprise.

Claims to money that arise solely from commercial contracts or trade financing are expressly excluded from the definition. Nonetheless, due to the breadth of the language, both the replacement value of property and the reasonable expectations of profit seem to be protected.\textsuperscript{21}


\textsuperscript{20} NAFTA, supra note 2.

\textsuperscript{21} Banks, supra note 9 at 508.
The substantive obligations that state parties owe foreign investors, often referred to as "disciplines," require host state-parties to afford foreign investment, National Treatment (Art. 1102),22 Most-Favoured-Nation Treatment (Art. 1103),23 a guarantee of at least a Minimum Standard of Treatment as defined by international law (Art. 1105),24 protection from Performance Requirements (Art. 1106),25 and protection from Expropriation (Art. 1110). Since the primary topic of this paper is expropriation, the provision defining this "discipline" is reproduced in full:

**Article 1110: Expropriation and Compensation**

1. No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ("expropriation"), except:

a) for a public purpose;
b) on a nondiscriminatory basis;
c) in accordance with due process of law and Article 1105(1); and
d) on payment of compensation in accordance with paragraphs 2 through 6.

Paragraphs 2 through 6 require compensation for violations of Article 1110 to be "paid without delay" at the "fair market value" of the investment.

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22 Article 1102 (1): Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.

23 Article 1103 (1): Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to investors of any other Party or of a non-Party with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.

24 Article 1105 (1): Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.

25 Article 1106 (1): No Party may impose or enforce any of the [listed] requirements, or enforce any commitment or undertaking, in connection with the establishment, acquisition, expansion, management, conduct or operation of an investment of an investor of a Party or of a non-Party in its territory.
On first reading, Article 1110 appears to set three different thresholds for application:

1. directly nationalize or expropriate
2. indirectly nationalize or expropriate
3. measures tantamount to nationalization or expropriation

However, ISDM tribunals have to date considered "indirect" and "tantamount" to be functionally equivalent.26 According to Daniel Price, the inclusion of the phrase "tantamount to nationalization or expropriation" was intended to ensure that "a measure that diminishes the value of an investment, [but] does not necessarily transfer ownership to a third party, [may still be scrutinized] under the rubric of expropriation."27 The purpose was to address the problem of "creeping" or "disguised" expropriation through strict regulations, which effectively deprive an investor of the use and benefit of property without any direct physical occupation or transfer of title.28 Yet, since "tantamount" means "equivalent," this language has been regarded as redundant. As one tribunal commented, "Something that is equivalent to something else cannot logically encompass more."29 Thus, current debate over Article 1110 concerns the nature of indirect regulatory expropriation (creeping or otherwise) that results in a deprivation of the enjoyment of property rights.30

The legal determination of the definition of indirect expropriation is complicated by the fact that the language of Article 1110 is ambiguous. A plain reading of the text could lead to one of two very different conclu-

26 Mann & von Moltke, supra note 9 at 38.
29 Pope & Talbot Inc. v. Canada, Interim Award by Arbitral Tribunal (26 June 2000), online: Appleton & Associates <http://www.appletonlaw.com/4b3P&T.htm > at para. 104 [Pope & Talbot]. The Tribunal notes that the words "equivalente" and "équivalent" are used in the equally authoritative Spanish and French texts of the treaty, respectively.
30 Ibid. at para. 102.
sions. Firstly, in subsection (1), there appears to be a complete prohibition of both direct and indirect expropriation, except if it is for a "public purpose," on a "non-discriminatory basis," in "accordance with due process of law," and accompanied with the "payment of compensation." Consequently, unlike the other provisions of Chapter 11, liability under Article 1110 is not triggered by unlawful conduct. Expropriations that are conducted for a legitimate public purpose, are non-discriminatory, and carried out in accordance with due process of law will still require investors to be compensated. That being the case, the conditional exceptions to the prohibition against expropriation seem to be superfluous. Read literally, all expropriation, lawful or otherwise, requires compensation. Therefore, the listed exceptions serve no function since both lawful and unlawful expropriations require compensation.

Conversely, one could also read the provision such that the condition "and on payment of compensation" would have a disjunctive meaning, indicating the list is a set of joint and several conditions, rather than a purely conjunctive set of requisites. Logically, the list of exception conditions (a), (b), (c), and (d), could refer to a set of (a) or (b) or (c) or (d), or any two, or three, or all four. Thus, a state could claim the right to expropriate without a concomitant duty to compensate if the measure were for a public purpose, or occurred on a nondiscriminatory basis, or occurred in accordance with due process of law, or occurred on payment of compensation. Such an interpretation, however, would offer little investor protection.

Since a literal reading of Article 1110 leads to either a very permissive or a very restrictive standard, neither interpretation would seem to reflect the intention of the drafters. Thus, to understand the provision properly, one must go beyond the text and interpret the provision with regard to the purpose and intent of the state-parties. Indeed, Daniel Price has stated that the language in Article 1110 was not "intended to go beyond the classical international law formulation." From the American point of view, according to the authoritative American Law Institute, Third Restatement of the Law on the Foreign Relations of the United States, the preferred U.S. standard of international expropriation law is as follows:

A state is responsible under international law for injury resulting from: (1) a taking by the state of the property of a national of another state that
(a) is not for a public purpose, or
(b) is discriminatory, or
(c) is not accompanied by provision for just compensation.

31 Price, supra note 27 at 111.
In the accompanying commentary regarding this formulation, the American Law Institute maintains, "A state is not responsible for loss of property or for other economic disadvantage resulting from bona fide general taxation, regulation, forfeiture for crime, or other action of the kind that is commonly accepted as within the police power of states, if it is not discriminatory."\textsuperscript{32}

The Metalclad tribunal, however, ignored the preferred U.S. standard regarding international expropriation law and opted for a strictly textual reading to arrive at a conjunctive interpretation of Article 1110; thus, rendering any contextual or purposeful consideration of public interest inconsequential.\textsuperscript{33} According to the tribunal, regardless of the policy rationale, regulatory interference with the private property rights of foreign investors necessitates compensation. In other words, the tribunal assumed the NAFTA state parties had contracted out of customary international law and instituted a much higher standard of property protection. As will be argued below, the standard goes well beyond the protection offered in the domestic law of any NAFTA state party.

Yet, even assuming pursuant to Article 1110 that public policy considerations should not be taken into account in the determination of whether compensation is due, there are other provisions that specifically allow for the consideration of environmental measures. For example, the NAFTA preamble states that parties undertake to implement the accord "in a manner consistent with environmental protection and conservation."\textsuperscript{34} Moreover, Article 104 provides that in relation to other environmental and

\textsuperscript{32} American Law Institute, \textit{Restatement of the Law Third, the Foreign Relations of the United States} (USA: American Law Institute Publishers 1987) 1 Section 712, Comment (g), cited in \textit{Marvin Roy Feldman Karpa (CEMSA) v. United Mexican States Case No. ARB(AF)/99/1} (2002) at para. 104 [hereinafter "Feldman"]. The American notion of "police power" refers to the common law regulatory authority of the state to restrict uses of property iminical to public health, safety, or welfare without incurring a duty to compensate the offending owners. This principle will be discussed in detail below.

\textsuperscript{33} \textit{Ibid.} at para. 111.

\textsuperscript{34} Note: there is an environmental side agreement that established the Commission on Environmental Cooperation (CEC) based in Montreal, but its primary purpose is to ensure state parties enforce their own laws. It does not impose any other obligations. \textit{North American Agreement on Environmental Cooperation}, Sept. 8, 9, 12, & 14, 1993, Can.-Mex.-U.S., 32 I.L.M. 1480; Also pursuant Article 2101, NAFTA incorporates the GATT Article XX, which provides \textit{inter alia}, "nothing in [the treaty] shall be construed to prevent that adoption or enforcement by [the parties] of measures...(b) necessary to protect human, animal or plant life or health; ...[g] relating to the conservation of living and non-living exhaustible natural resources ...This is all subject to the requirement "that such measures are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination
conservation agreements, as identified in the agreement text or listed in Annex 104.1, "such obligations shall prevail to the extent of the inconsistency, provided that where a Party has a choice among equally effective and reasonably available means of complying with such obligations, the Party chooses the alternative that is the least inconsistent with the other provisions of this Agreement." Nevertheless, for this provision to have any effect, the extent and nature of the claimed conflicting environmental obligation must be broadly construed. To date, however, ISDM tribunals have declined to do so and have instead focused on the obligation to take regulatory measures that are least inconsistent with the promotion of trade and investment.

Nonetheless, while seeking to foster trade and investment, pursuant to Article 1114, Chapter 11 appears to allow some derogation from strict economic discipline for the purposes of environmental protection. Article 1114 (1) states:

Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns.

On closer inspection, if this provision is read literally, it is devoid of substance. While Article 1114 indicates that nothing in Chapter 11 "shall be construed to prevent a Party" from adopting any measure necessary "to ensure that investment activity ...is undertaken in a manner sensitive to environmental concerns," any such measure needs to be "otherwise consistent with this Chapter." In other words, if Chapter 11 allows it, then you may proceed, but any environmental measure that will interfere

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35 The listed agreements are as follows: (a) the Convention on the International Trade in Endangered Species of Wild Fauna and Flora, done at Washington, March 3, 1973, as amended June 22, 1979; (b) the Montreal Protocol on Substances that Deplete the Ozone Layer, done at Montreal, September 16, 1987, as amended June 29, 1990; (c) the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal, done at Basel, March 22, 1989, on its entry into force for Canada, Mexico, and the United States.
with investment will not be allowed. Of course, since any environmental measure worth taking will restrict proprietary freedom (otherwise there would be no need to regulate the activity) the provision, if read literally, appears to be meaningless.

The entire aim of environmental regulation is to restrict the harmful actions of private actors pursuing their own particular economic benefit. Consequently, the "Environmental Measures" protection codified within Article 1114 seems to be perversely designed to ensure that Chapter 11 obligations are not hindered by environmental regulation. Alternatively, Article 1114(1) could simply be viewed as another example of poor drafting. Indeed, it is unlikely that the intent of the parties is to insulate the treaty from all future environmental measures, since they expressly demand all past environmental regulation be strictly honoured. Following Article 1114(1), subsection (2) states, "[t]he Parties recognize that it is inappropriate to encourage investment by relaxing domestic health, safety or environmental measures." Therefore, read literally, the provision seems both to disallow the enactment of new environmental measures and simultaneously to ban any relaxation of established environmental standards. A literal interpretation of Article 1114 would thus indicate that it was the intent of the parties to freeze environmental regulation indefinitely. Since this is an absurd proposition, it would seem that the phrase "any measure otherwise consistent" should be interpreted within the context of the Preamble and Article 104, to afford the flexibility necessary to allow state parties to meet ever-evolving environmental challenges.

INVESTOR REMEDIES

THE ENFORCEMENT OF "DISCIPLINE" under Chapter 11 is provided by Section B, which establishes the ISDM and allows aggrieved investors of one state party to submit claims directly against another state party. Claims meeting a number of procedural requirements are submitted to binding arbitration under one of three mechanisms:

(1) the International Center for the Settlement of Investment Disputes Convention (ICSID);37

36 Prof. H. Mann has referred to this as the "smoke and mirrors" derogation, Private Conversation (October 2001). C.f. J. Martin Wagner, "International Investment, Expropriation and Environmental Protection" (1999) 29 Golden Gate U.L. Rev. 465 provides a good overview of the relationship between foreign investment and environmental regulation.

Presently, the United States is a party to the ICSID Convention, but Canada and Mexico are not. The ICSID Convention is only available if both states involved (directly or indirectly as home of the investor) are signatories, while the ICSID Additional Facility only requires one state to be a party to the ICSID Convention. Consequently, only UNCITRAL and the ICSID Additional Facility are currently operative for the purposes of Chapter 11 arbitration. As a prerequisite for the initiation of the ISDM, a complainant investor must waive the right to pursue monetary damages before any other administrative tribunal or court of law regarding the matter at issue. Claims are then decided by arbitral tribunals composed of three members - one chosen by each of the two parties in dispute, and the third presiding member is selected by agreement of the disputing parties. Any resulting arbitral award is treated as the legal equivalent of a final judgment from a court of law in any state party.

THE ECONOMIC & HISTORICAL RATIONALE FOR CHAPTER 11

According to liberal economic theory, a primary justification for an international legal standard requiring compensation for expropriation is to force governments to internalise the real costs

41 NAFTA, supra note 2 at art. 1121.
of regulation, thereby deterring inefficient over-regulation. In theory, a general duty to compensate foreign investors should serve to facilitate the efficient flow of international capital to maximize investment for the supply of socially desirable goods and services. Yet, the standard law-and-economics model also assumes that rational economic actors in a market environment will produce the socially optimal quantity of a particular good or service only if the actor is forced to bear the full costs of its economic activities through regulatory measures.

The example of a hazardous waste dump is a useful illustration of the proper balance regulation must strike. A landfill site has the potential to pollute the surrounding groundwater. Consequently, the operation of the facility could undermine the quality of life of neighbouring citizens and the health of the environment for future generations. Quality of life has value. Operating a hazardous waste dump without proper environmental protection safeguards will diminish the quality of life for neighbouring citizens and future generations if contamination of the surrounding area is allowed to occur. Thus, the wider social benefit and individual profits gained from storing hazardous waste at low cost and in an ecologically irresponsible manner would be partially achieved at the expense of those who receive no economic benefit, but have been forced to pay the ecological costs due to a deterioration in their quality of life. In order to ensure that a rational cost-benefit assessment of a social good is fully understood, the real social costs of economic activity need to be shifted onto those who generate them. Thus, cost internalisation by cost generators is essential for maintaining the efficiency of a free market.

Yet, just as rational regulation shifts costs to promote the maximisation of socially desirable goods and services, the irrational imposition of regulation will act as a disincentive for the offering of socially desirable goods and services. In particular, regulation and expropriation used for political ends will tend to distort the proper functioning of the market. Rather than fostering the socially optimal quantity of a particular good or service, a politicised market will foster the optimal quantity of a particular good or service for a privileged class of economic rent seekers. Since the outsider status of foreign investors reduces the political "costs" of taking foreign-owned property or placing it at a competitive disadvantage in comparison with domestic actors, it is feared that foreign-owned property

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43 Been & Beauvais, supra note 28 at 88.
44 Coase, supra note 42 at 9.
is vulnerable to political interference.\textsuperscript{45}

This concern is particularly acute regarding Mexico, since it has sweeping powers under Article 27 of its Constitution to redistribute private wealth for public policy purposes.\textsuperscript{46} This constitutional provision has its origins in the 1910 Revolution and the Constitution of 1917, which provided for the nationalisation of mining resources and the restoration of communal lands. In doing so, a framework was established for a strong interventionist state that has the power to maintain tight control over the economy.\textsuperscript{47} As a result, Article 27 granted the state the authority to place strict limits on the foreign ownership of land and natural resources. Furthermore, the Constitution provided that all foreign investment be subject to the domestic law of the Mexican state.\textsuperscript{48} This constitutional requirement that foreign nationals settle their disputes according to Mexican law was a response to the nineteenth century imperial practice of extending diplomatic protection to subjects abroad to protect the security of foreign ventures. In opposition to this practice, the so-called Calvo doctrine, named after the late-nineteenth-century Argentine jurist Carlos Calvo who first articulated it, maintained that since sovereign states are equal and independent, all nations should enjoy absolute freedom from foreign interference. Thus, while foreign nationals were afforded the full protection of the law, they were not entitled to any special rights or privileges. As with citizens, foreign nationals must seek redress for grievances before domestic courts.\textsuperscript{49}

After the largely uncompensated Mexican nationalisation of American and British oil industry assets in 1938, the legal redress offered by the Calvo doctrine seemed cold comfort for foreign investors.\textsuperscript{50} While equal before the law, the lawmakers did not treat them equitably. In protest, U.S. Secretary of State, Cordell Hull, demanded the Mexican government extend "prompt, adequate and effective compensation" to American inves-

\textsuperscript{46} Article 27: The Nation shall at all times have the right to impose on private property rights the limitations dictated by the public interest, as well as to regulate, for the collective good, the use of natural resources susceptible to appropriation, to ensure a more equitable distribution of public wealth, to conserve them, to achieve the well-balanced development of the country and the improvement of the living conditions of the rural and urban population.
\textsuperscript{48} Ibid.
\textsuperscript{49} Wiltse, supra note 19 at 1154.
\textsuperscript{50} G. Starner, "Taking a Constitutional Look: NAFTA Chapter 11 as an Extension Of Member States’ Constitutional Protection of Property" (2002) Law & Pol’y Int’l Bus. at 405 [hereinafter "Starner"].
tors. While Secretary of State Hull was ultimately unsuccessful in convincing the Mexican government to amend its ways, his position would become the foundation for the American preferred standard regarding the international law on expropriation.\textsuperscript{51} As mentioned above, the Third Restatement of the Law on the Foreign Relations of the United States maintains, "A state is responsible under international law for injury resulting from: (1) a taking by the state of the property of a national of another state that (a) is not for a public purpose, or (b) is discriminatory, or (c) is not accompanied by provision for just compensation."\textsuperscript{52}

In opposition to this standard, and in defence of state sovereignty over national resources, the Calvo doctrine gained widespread acceptance in the developing world. Thus, a bilateral dispute between Mexico and the United States became generalised as two competing legal visions of a just international economic order.\textsuperscript{53} During the Cold War, the Soviet bloc struck a diplomatic alliance with developing countries in opposition of liberal economics and thereafter, the Calvo doctrine of sovereign legal autonomy over domestic economic relations became a weapon of international politics.\textsuperscript{54} Using the numerical dominance in the United Nations General Assembly, the Soviet bloc and developing countries cooperated to pass a number of resolutions affirming the right to expropriate foreign-owned property provided "appropriate compensation" was extended "in accordance with the rules in force in the State taking such measures in the exercise of its sovereignty."\textsuperscript{55} Compensation was thus contingent upon domestic legislation and standards of appropriateness. As a countermeasure, the United States initiated a Bilateral Investment Treaty (BIT) programme, which committed treaty partners to investor protection based on the preferred American expropriation standard in return for freer access to the American market.\textsuperscript{56} Over time, these BIT agreements would serve as models for bilateral relationships between other nations as

\textsuperscript{51} Been & Beauvais, \textit{supra} note 28 at 47.
\textsuperscript{52} Feldman, \textit{supra} note 32 at para. 104.
\textsuperscript{53} Been & Beauvais, \textit{supra} note 28 at 48.
\textsuperscript{54} Beauvais, \textit{supra} note 45 at 252.
\textsuperscript{56} A. Guzman "Why LDCs Sign Treaties that Hurt Them: Explaining the Popularity of Bilateral Investment Treaties" (1998) 38 Va. J. Int'l L. 639 at 645 [hereinafter "Guzman"].
well. Currently, there are over 1,500 bilateral investment treaties in effect around the world.\textsuperscript{57}

In the negotiations leading to the signing of NAFTA, it was apparent that before entering into a free trade pact with the United States and Canada, Mexico needed to exempt its prospective trade partners from Article 27 of its Constitution and the Calvo clause if it wished to realise greater foreign investment. This is the purpose of Chapter 11. As Daniel Price has explained, Chapter 11 was designed to remove investment disputes from "the political realm and put them more into the realm of commercial arbitration."\textsuperscript{58} In effect, Mexico promised to internalise the costs of the regulation and expropriation of American and Canadian foreign investment, thereby creating a more hospitable investment climate. Thus, the government moved to immunise the nationals of its prospective NAFTA partners from Article 27 of the Mexican Constitution. To eliminate the possibility of a constitutional challenge, the Mexican Chamber of Deputies passed a decree declaring that the submission of disputes to international mechanisms "is not, in any manner, an invocation of diplomatic protection by a foreign government."\textsuperscript{59}

In creating a more hospitable investment climate in Mexico through the Chapter 11 ISDM, Canada and the United States have likewise effectively undermined the ability of their own legal systems to exert jurisdiction over investment disputes that involve foreign nationals of NAFTA state parties. By design, due to the ability of the ISDM to take property issues out of the domestic judiciary's reach, Chapter 11 effectively exerts supra-constitutional authority over the judiciary of state parties.\textsuperscript{60} As one commentator has observed: \textsuperscript{61}

Chapter 11 alters the traditional, hierarchical relationship between foreign investors and host states in two ways. First, it prohibits certain exercises of sovereignty at the expense of foreign investors. Second, it creates a mechanism for resolving investment disputes that places foreign investors and their host states on a more equal footing. Because investors do not have to rely on the mercy of their


\textsuperscript{58} Price, \textit{supra} note 27 at 112.

\textsuperscript{59} Schneiderman (2000), \textit{supra} note 47 at 766.

\textsuperscript{60} \textit{Ibid.} at 763.

\textsuperscript{61} Brower, \textit{supra} note 40 at 73.
host states or their home states for protection, Chapter 11 redistributes bargaining power in a manner more reminiscent of relationships between commercial actors.

Yet, due to the potentially broad scope of the types of governmental regulation that could be captured by the wording of Article 1110, the property rights foreign investors enjoy under the ISDM could potentially go well beyond that offered by either Canadian or American jurisprudence.

In Canada, since there is no constitutional protection of property rights, the ISDM carries with it the possibility of disrupting the marketplace by creating two classes of investment. Under Canadian law, the scope of expropriation claims is very limited, primarily restricted by the ambit of expropriation legislation. Whether the state owes compensation for property rights is, therefore, essentially a question of statutory interpretation. Valid legislation or governmental action has near unfettered authority to restrict private property rights for the common good. If the legislature expressly denies compensation, then as the court bluntly observed in Florence Mining Co. v. Cobalt Lake Mining Co., "The prohibition, 'Thou shalt not steal,' has no legal force upon the sovereign body." However, while the power to take property is sweeping, it is rarely wielded in an unrestrained manner. Since Canada is a democracy, governments must eventually answer to the electorate for their actions. Moreover, property rights are not without judicial protection. Within the British common

62 See A & L Investments Ltd. v. Ontario (Minister of Housing) (1997) 62 L.C.R. 241 (Ont. C.A.) at para. 29 concerning the lack of constitutional protection afforded proprietary rights. It should be noted that the Canadian Bill of Rights, S.C. 1960, c. 44, Pt. I, reprinted R.S.C. 1985, App. III offers some quasi-constitutional protection for proprietary rights pursuant to s.1 (a) which states, "It is hereby recognized and declared that in Canada there have existed and shall continue to exist without discrimination by reason of race, national origin, colour, religion or sex, the following human rights and fundamental freedoms, namely, (a) the right of the individual to life, liberty, security of the person and enjoyment of property, and the right not to be deprived thereof except by due process of law; ..." However, the Supreme Court in Authorson (Litigation Guardian of) v. Canada (Attorney General) (2003), 227 D.L.R. (4th) 385 at paras. 51-52, "The Bill of Rights does not protect against the expropriation of property by the passage of unambiguous legislation. ...The Bill of Rights protects only rights that existed at the time of its passage, in 1960. At that time it was undisputed, as it continues to be today, that Parliament had the right to expropriate property if it made its intention clear."  
63 Hartel, supra note 11.  
law tradition, property rights can only be infringed or taken away with unequivocal legislation. In addition, unless the right to compensation is expressly precluded by legislation, courts will assume there is an obligation to pay compensation for any confiscated property.65 These basic principles of statutory interpretation date back to at least 1215 when the Magna Carta declared, "No Freeman shall ... be disseised ... [but] by lawful Judgment of his peers, or by the law of the land."66

In the De Keyser's Royal Hotel decision, the House of Lords reaffirmed this principle noting, "Since Magna Carta, the estate of a subject in lands or buildings has been protected against the prerogative of the Crown."67 This restraint on executive authority over property rights is basic rule of law. Simply put, only the democratically accountable members of the legislature have the constitutional authority to extinguish common law proprietary interests. If property is expropriated, then compensation shall usually be required because, as the court stated in De Keyser's Royal Hotel, "The recognized rule for the construction of statutes is that, unless the words of the statute clearly so demand, a statute is not to be construed so as to take away the property of a subject without compensation."68 Yet, with respect to land-use regulation where the intent of the legislature is clear, governmental action has near unfettered authority to restrict private property rights for the good of the community, leaving the individual titleholder with nothing in return. Compensation is not presumed, since no citizen need be compensated for simply obeying the law.69

By contrast, property rights in the United States are constitutionally protected under the so-called "takings" clause of the Fifth Amendment. According to American takings jurisprudence, individuals should not bear

66 Magna Carta, 17 John.
67 De Keyser's Royal Hotel, [1920] A.C. 508 at 542, 569 [emphasis added].
68 Ibid. at 542.
public burdens. Consequently, where property is taken for public use, just compensation is constitutionally mandated. However, this is subject to the common law "police power exception," whereby uses of property inimical to public health, safety, or welfare may be barred without incurring a duty to compensate offending landowners. Therefore, while the jurisprudence on regulatory takings in the United States tends to be much more protective of private land interests, due to the police power exception, this difference should not be overstated.

Indeed, until 1922, the takings clause had been understood to prohibit only the physical seizure of property. That year, the U.S. Supreme Court in Pennsylvania Coal Co. v. Mahon held that "while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking." Since then, the Supreme Court of the United States has had great trouble defining the proper limits of regulatory control. In principle, it is a balancing of rights and obligations such that the state is barred from forcing individuals to bear public burdens that, in all fairness and justice, should be borne by the public as a whole. Consequently, in U.S. constitutional law, the deprivation of property through regulation for public purposes is sufficient to bring a case within the constitutional protection against "taking" for "public use." Although some regulation is necessary for the general good, a regulation "goes too far" if it effectively "takes" property rights for purposes outside of the so-called "police power exception."

In 1978, the court in Pennsylvania Central Transportation Co. v. New York City identified three factors that must be considered:

1. the economic impact of the regulation
2. the degree to which the regulation has interfered with

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73 Pennsylvania Coal, supra note 70.
74 Porterfield, supra note 72.
75 Pennsylvania Coal, supra note 70; Armstrong, supra note 70; Eastern Enterprises v. Apfel, supra note 70.
the owner's reasonable expectations concerning the property
3. the character of the regulatory action

Under this test, a state or local government may exercise, in most instances, its police powers to regulate property without compensating the owner, even if the regulation causes the property to lose most of its value. Nonetheless, after nearly two centuries of takings jurisprudence, American expropriation law remains very much unsettled. Currently, whether or not a state regulator has gone too far is a fact-based consideration that defies strict rules of general application. As one American judge has lamented, "Even the wisest lawyers would have to acknowledge great uncertainty about the scope of this Court's takings jurisprudence." 

Consequently, given the complexity of takings law, no attempt was made in NAFTA to address directly the problem of regulatory expropriation. The issue was deliberately left for ISDM tribunals to consider. As Daniel Price has explained, the negotiators could not find "a bright line that would distinguish between legitimate, bona fide and nondiscriminatory regulation, on the one hand, and an expropriatory act requiring compensation, on the other hand." Therefore, the drafters abandoned the attempt. Daniel Price observed, "If the United States Supreme Court and arbitral tribunals could not do it in over 200 years, it was unlikely that the negotiators were going to do it in a matter of weeks with one line in a treaty." In the 1986 Canada-U.S. Free Trade Agreement, this was not an issue since both parties had complete faith in the security of property within each other's jurisdictions. The trials, tribulations, and complexities of takings law could be left in confidence to each other's judiciary. However, this confidence did not extend to Mexico. In order to assuage investor trepidation and foster greater investment in Mexico, mandatory arbitration under the ISDM was instituted, and because it was a tripartite agreement, all parties became subject to its binding authority.

Since the law governing Chapter 11 left out any reference to the police power exception to the protection of property rights, the protection offered by Article 1110 is potentially sweeping. While at customary international law a state is not responsible for private economic disadvantage resulting from bona fide regulation within its police power authority, a plain

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77 Lucas, supra note 70 at 1019. Justice Scalia stated that in some cases a landowner who suffered a 95 percent loss in property value due to regulatory control "will get nothing."


80 Ibid. at 6.

81 NAFTA, supra note 2.

82 Feldman, supra note 32 at 105.
reading of the Article 1110 text could indicate that NAFTA state-parties have contracted out of this customary norm. Indeed, it was on this basis the *Metalclad* tribunal ruled that, in the consideration of Article 1110, it did not need to consider the motivation or intent behind the regulatory action. As such, the *Metalclad* tribunal interpretation of Article 1110, if subsequently followed by other tribunals, would effectively immunise foreign investors from the police power exception, granting them supra-constitutional protection for even expected economic benefit, while absolving them of public burdens. In effect, foreign investors have rights without responsibilities. Since this has been the only Article 1110 claim to be successfully argued to date, it sets an unnerving precedent. Although under Article 1136(1) "[a]n award made by a Tribunal shall have no binding force except between the disputing parties and in respect of the particular case," Chapter 11 interpretation is governed by rules of international law, and past arbitral decisions, while not binding, will inform the analysis of future tribunals. This is a disturbing prospect.

Under the *Metalclad* tribunal interpretation of Article 1110, the well-established international law principle of polluter pays, first enunciated by the OECD in 1972, has been transformed into pay the polluter. According to the customary polluter pays principle, the community "owns" the environment as a public commons, and users must pay for any damage to the commons. By contrast, if the community is obligated to pay a polluter to modify its behaviour, the implicit message is that the polluter owns the environment and can use it with impunity. Thus, foreign investors could use the ISDM to enforce ultimata-free investment of regulatory burdens or provide compensation for lost market potential. Indeed, there are indications that this has already occurred. One early commentator on the political effect of Chapter 11 noted that American tobacco producers threatened to use the ISDM to challenge a move by the Canadian parliament to require plain generic packaging on cigarettes. In another instance, the Canadian government, concerned about the possible adverse health effects of the gasoline additive methylcyclopentadienyl

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83 *Metalclad*, supra note 1 at para. 111.
84 Mann, *supra* note 9 at 391; Starner, *supra* note 50 at 418.
85 D. Gantz, "Reconciling Environmental Protection and Investor Rights under Chapter 11 of NAFTA" (2001) 31 Environmental Law Reporter, 10646 [hereinafter "Gantz"].
86 Mann & von Moltke, *supra* note 9 at 46.
87 This threat proved to be unnecessary due to the *RJR-MacDonald Inc. v. Canada* [1995] 127 D.L.R. (4th) 1 decision, which held that any such move would violate the freedom of expression guaranteed by the *Charter of Rights and Freedoms*. See Schneiderman (1996), *supra* note 9.
manganese tricarbonyl (MMT), banned its importation. However, after an American producer initiated ISDM proceedings claiming *inter alia* Article 1110 expropriation,\(^8\) the ban was rescinded and a US$19.3 million settlement was reached. As one observer has warned,\(^9\)

It is increasingly apparent that the private rights of foreign investors are being used not as a defensive protection against government abuse because an investor is a foreign-owned company, but as a strategic offensive threat to be wielded against government decision-makers rendering or considering decisions adverse to the interests of a company involved. The cases demonstrate the lobbying capacity attached to Chapter 11, a capacity never envisaged when the NAFTA negotiations took place.

Such a development would skew the cost-benefit analysis of market risk assessment in favour of foreign capital, thus placing domestic investment at a competitive disadvantage. Returning to the example of a hazardous waste site, if both an American firm and a Canadian firm were to acquire land to develop separate and competing facilities, only the Canadian firm would be subject to subsequent costs of any regulation that diminished the reasonably-to-be-expected economic benefit of property.\(^9\) So ironically, Chapter 11 provides an economic incentive for domestic actors in highly regulated sectors to incorporate abroad in order to invest at home. Thus, it appears investment protections designed to ensure a fair playing field for foreign investment might have actually been skewed significantly in favour of foreign investment, placing domestic actors at a competitive disadvantage.

It is perhaps for this reason that the new federal *Species at Risk Act* (SARA) contains an unprecedented compensation provision for adverse economic impact suffered as a result of regulatory restrictions on the use and development of land.\(^1\) Section 64 creates ministerial regulatory discretion to "provide fair and reasonable compensation to any person


\(^{9}\) Mann, *supra* note 9 at 405.

\(^{1}\) *Species at Risk Act*, S.C. 2002, c. 29 [*"SARA"*]C.f., online: Environment Canada <http://www.speciesatrisk.gc.ca/default_e.cfm> and Government of Canada <http://www.sararegistry.gc.ca/default_e.cfm>; The purpose of this statute is to prevent the extinction and extirpation of endangered or threatened species by (1) requiring stewardship programs and government-approved wildlife recovery measures to ensure the continued diversity of species located or residing on
for losses suffered as a result of any extraordinary impact” due to critical habitat protection regulation. As one observer has noted, "The purpose of this provision is to compensate landowners for the private burdens of providing a 'public' good and to avoid a situation where landowners have economic incentives to destroy wildlife habitat on their land rather than face costly habitat protection orders.”92 However, the observer further comments that this provision introduces "a novel principle into our [Canadian] legal system, borrowed from American 'regulatory takings' jurisprudence, that taxpayers ought to compensate individual property owners when the decisions of democratically elected governments have the effect of reducing the market value of their property yet fall short of expropriating or 'sterilizing' the property altogether.”93

With respect to domestic and non-NAFTA state-party nations, such compensation is discretionary, but for Mexican and American investors, Article 1110 enforces a mandatory system of compensation.94 Given the large degree of American investment within the Canadian economy protected by Article 1110, compensating American firms for lost investment-backed expectations would be extremely expensive. Pursuant to SARA, Canadian investors would no doubt demand equal consideration, further compounding the costs. To prevent such a development, a "regulatory chill” may result, inhibiting governments and agencies from taking steps they believe necessary to protect the environment.95 This problem, of course, extends to all the NAFTA partners. In order to understand the significance of the Metalclad decision for all NAFTA state-parties, two previous arbitral tribunal considerations of Article 1110 need to be discussed

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94 SARA, supra note 91. Since the SARA, pursuant to s.11, seeks to foster voluntary stewardship agreements with the private sector, it remains to be seen how aggressively federal regulators will attempt to prohibit economic activity that endangers critical habitat.
95 Mann, supra note 9 at 406.
before analysing the *Metalclad* decision itself.

**POPE & TALBOT**

In 1996, THE UNITED STATES AND Canada entered into a softwood lumber export agreement that set quota on the quantity of softwood exported to the U.S. free of import duties. The quota was then allocated to the provinces to be divided among individual producers. One of these companies, Pope & Talbot Inc., a wholly owned subsidiary of a U.S. corporation, complained that it did not receive a fair share of the quota.\(^{96}\) Consequently, Pope & Talbot initiated ISDM proceedings, claiming, *inter alia*, a right to Article 1110 compensation. Based upon the prohibition against any "measure tantamount to expropriation," the statement of claim attempted to define expropriation broadly as any "act by which governmental authority is used to deny some benefit of property to an investor," including "government action that harms or delays the effective enjoyment of an investment."\(^ {97}\) It sought US$ 80 million in damages and legal costs. The tribunal rejected the Article 1110 claim, although it later found the company had been denied fair and equitable treatment in violation of Article 1105. This was due to a lack of good faith in the consultation process initiated to address its complaint after the NAFTA challenge had been launched.\(^ {98}\) With respect to Article 1110, the tribunal accepted that "access to the U.S. market" is a property interest subject to Article 1110 protection,\(^ {99}\) but determined that the allegedly unfair quota allocation did not actually constitute an interference substantial enough to be considered an expropriation under customary international law.\(^ {100}\) This conclusion was largely based upon the *Third Restatement of the Law on the Foreign Relations of the United States*, which restricts the obligation to compensate for expropriation to situations where an action "is confiscatory, or ...prevents, unreasonably interferes with, or unduly delays, effective enjoyment of an alien's property."\(^ {101}\) Based on these criteria, the tribunal rejected Canada's contention that regulatory measures were not the proper subject of Article 1110 compensation. The tribunal held:

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\(^{96}\) *Pope & Talbot*, supra note 29.

\(^{97}\) V. Been, "NAFTA's Investment Protections and the Division Of Authority For Land Use and Environmental Controls" (2002) 32 Environmental Law Reporter 11001 [hereinafter "Been"].

\(^{98}\) *Pope & Talbot*, supra note 29.


\(^{100}\) *Ibid*. at para. 94.

\(^{101}\) *Ibid*. at para. 102.
Regulations can indeed be exercised in a way that would constitute creeping expropriation...Indeed, much creeping expropriation could be conducted by regulation, and a blanket exception for regulatory measures would create a gaping loophole in international protections against expropriation.\textsuperscript{102}

Following the \textit{Third Restatement of the Law on the Foreign Relations of the United States}, the tribunal relied on Comment (g) to Section 712 on expropriation to advance the notion that Article 1110 protection is engaged once regulation deprives the investor of "effective control over the enterprise" or makes it "impossible for the firm to operate at a profit."\textsuperscript{103} Observing that Pope & Talbot retained control over its business and continued to export substantial quantities of softwood at a profit,\textsuperscript{104} the tribunal thus concluded that any disadvantage suffered under the quota allocation regime could not constitute expropriation.\textsuperscript{105}

**S.D. MYERS INC.**

In 1998, S.D. MYERS INC., AN AMERICAN firm engaged in the disposal of PCBs (polychlorinated biphenyls), brought a US$ 20 million claim against Canada. In 1995, S.D. Myers established a Canadian subsidiary with intent to export Canadian PCBs to the U.S. for disposal.\textsuperscript{106} Canada, however, as a state party to the \textit{Basel Convention},\textsuperscript{107} which prohibits state parties from engaging in the international trade of hazardous waste, had adopted a policy of destroying PCBs within its borders. Beginning in 1990, the export of PCB waste was banned. Nevertheless, there was an exemption for exports to the United States due to the presence of PCB waste owned by American governmental agencies operating in Canada. S.D. Myers attempted to use this exemption to enter the Canadian PCB remediation market.\textsuperscript{108} Although American law prohibited the private

\textsuperscript{102} \textit{Ibid.} at para. 99.
\textsuperscript{103} \textit{Ibid.} at para. 102 note 81.
\textsuperscript{104} \textit{Ibid.} at paras. 100-101.
\textsuperscript{105} \textit{Ibid.} at para. 102.
importation of PCBs, in 1995, the U.S. Environmental Protection Agency (EPA) granted a special import permit to S.D. Myers. Canada reacted to this action by instituting a complete ban on all PCB exports. In 1997, however, Canada reconsidered and opened the border for S.D. Myers, but it only remained open for five months because an American court action successfully challenged the legality of the EPA import licence.\textsuperscript{109}

Based on the \textit{Pope & Talbot} decision, S.D. Myers claimed that the denial of access to the Canadian market between 1995 and 1997 was a protected property right under Article 1110 and as such, the Canadian government needed to compensate the company for lost economic opportunities. The claim was advanced despite the fact Article 104 of NAFTA expressly provides obligations undertaken in the \textit{Basel Convention} "shall prevail" over NAFTA obligations. However, Article 104 is only effective "on its entry into force for Canada, Mexico and the United States." Thus, since the United States had signed but not ratified the \textit{Basel Convention}, Article 104 was not applicable to the dispute. Nonetheless, the tribunal commented:\textsuperscript{110}

Even if the Basel Convention were to have been ratified by the NAFTA Parties, it should not be presumed that Canada would have been able to use it to justify the breach of a specific NAFTA provision because \textit{...where a party has a choice among equally effective and reasonably available alternatives for complying ...}with a Basel Convention obligation, it is obliged to choose the alternative that is \textit{...least inconsistent} \textit{...}with the NAFTA. If one such alternative were to involve no inconsistency with the Basel Convention, clearly this should be followed. [\textit{emphasis in the original}]

Article 104 dictates that given a choice between two equally effective environmental protection measures, parties should take the "least inconsistent" for the promotion of trade and investment. In its assessment of this balance, the tribunal concluded:\textsuperscript{111}

Parties have the right to establish high levels of environmental protection. They are not obliged to compromise their standards merely to satisfy the political or economic interests of others states; Parties should avoid creating distortions to trade; environmental protection and economic development can and should be mutually supportive.

\textsuperscript{109} \textit{Sierra Club v. EPA}, 118 F. 3d 1324 (9th Cir. 1997).
\textsuperscript{110} \textit{S.D. Myers}, Nov. 13, \textit{supra} note 106 at para. 215.
\textsuperscript{111} \textit{Ibid.} at para. 220.
The tribunal then explained that international law does not generally treat regulations as expropriation, and accordingly, "regulatory conduct by public authorities is unlikely to be the subject of legitimate complaint under Article 1110 ...although the Tribunal does not rule out that possibility." Generally, the tribunal observed, "[e]xpropriations tend to involve the deprivation of ownership rights," while regulations are a "lesser interference." This distinction, the tribunal explained, "screens out most potential cases of complaints concerning economic intervention by a state and reduces the risk that governments will be subject to claims as they go about their business of managing public affairs."

In a separate opinion, one of the arbitrators further commented that while "[t]here may be some cases where a measure that is presented as a regulation must, in law and justice, be treated as a nationalization or expropriation for the purposes of Article 1110 ...the vast run of cases, regulatory conduct by public authorities is not remotely the subject of legitimate complaints under Article 1110." Since the closure of the border was temporary and no property or benefit was transferred directly to others, the tribunal held that no expropriation had occurred. Yet, culpatory evidence was presented showing that the Canadian government was motivated more by economic protectionism than environmentalism. As a result, while the tribunal recognised the legitimate public policy reasons to support the exportation ban, it found that Canadian policy was actually "shaped to a very great extent by the desire and intent to protect and promote the market share of enterprises that would carry out the destruction of PCBs in Canada and that were owned by Canadian nationals." S.D. Myers, therefore, succeeded based on a national treatment violation and was awarded CAN$ 6,050,000 in damages, as well as $850,000 for legal costs.

A troubling aspect of this decision is the fact that while the tribunal scrutinised the policy basis for governmental action, the tribunal did not question whether the reasonable-to-be-expected economic interest was in fact reasonable. Given the obvious legal barrier presented by the Basel

112 Ibid. at para. 281.
113 Ibid. at para. 282.
114 Ibid.
116 S.D. Myers, Nov. 13, supra note 106 at paras. 287-288.
117 Ibid. at para. 162.
118 An attempt to obtain judicial review of this award was unsuccessful. See Canada (Attorney General) v. S.D. Myers, Inc. [2005] F.C.J. No. 29.
119 Been, supra note 97.
Convention and the precarious legality of the EPA permit, the venture was inherently risky.\textsuperscript{120} If judged by the standards of American takings law, it is unlikely S.D. Myers would have succeeded. Regarding heavily regulated economic sectors, American courts have determined that it is unreasonable for investors to expect compensation for losses suffered due to alterations in the regulatory regime.\textsuperscript{121} Nonetheless, such a change in the regulation of a highly regulated industry was the very basis for the successful S.D. Myers complaint and would be for Metalclad as well.

The recent defeat of the US$ one billion claim brought by Methanex against the United States alleging, \textit{inter alia}, that the Californian phase-out of the gasoline additive MTBE (methyl tertiary butyl ether) is a measure tantamount to expropriation provides hope for regulators. Although factually similar to the Canadian attempt to ban MMT, the Americans decided to defend their right to regulate and won.\textsuperscript{122} With respect to highly regulated economic activity, the Tribunal commented that where a firm enters into "a political economy in which it was widely known, if not notorious, that governmental environmental and health protection institutions" are "operating under the vigilant eyes," then strict regulation should be expected.\textsuperscript{123}

Returning to the S.D. Myers decision, it is interesting to note that the environmental protection provisions contained within Article 1114 played no part in the award decision. In the separate and concurring opinion, a tribunal member recognised that the language of the article is extremely

\textsuperscript{120} Been & Beauvais, \textit{supra} note 28 at 71.
\textsuperscript{121} T. Lilley, "Keeping NAFTA 'Green' for Investors and the Environment" (2002) 75 S. Cal. L. Rev. 727 at 752-3 [hereinafter "Lilley"] states, "In a highly regulated industry...courts consider that the investor is on notice that regulations may at any time be changed or extended. To expect otherwise would be unreasonable. Even in an industry that is not yet highly regulated, if the use imposes a high magnitude of externalities on the neighbors, regulation should be expected at some time." \textit{Good v. United States}, 189 F. 3d 1355, 1363 (Fed. Cir. 1999) held: "In light of the growing consciousness of and sensitivity toward environmental issues, Appellant must also have been aware that standards could change to his detrimen, and that regulatory approval could become harder to get." \textit{Mitchell Arms, Inc. v. United States}, 26 Cl. Ct. 1, 5 (1992) held "government as we know it would soon cease to exist if such exclusively governmental functions as the control over foreign commerce could not be accomplished without the payment of compensation to those business interests that have chosen to operate within this highly regulated area."

\textsuperscript{122} Methanex Corporation v. United States, Final Award, (Aug. 9, 2005) online: Nafta Claims <http://naftaclaims.com/Disputes/USA/Methanex/Methanex_Final_Award.pdf>.

\textsuperscript{123} \textit{Ibid.} at Part IV, Chapt. D at para. 9.
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problematic, but refused to dismiss Article 1114 as "empty rhetoric." Instead, the tribunal member defended Article 1114 "as acknowledging and reminding interpreters of Chapter 11 (Investment) that the parties take both the environment and open trade very seriously and that means should be found to reconcile these two objectives and, if possible, to make them mutually supportive." Within the context of expropriation, the separate opinion noted:

International law ...requires a tribunal to look at the context of a provision. The immediate context of Chapter 1110 [sic] is the text of NAFTA itself, which exhibits in various places including Article 1114 and elsewhere, a concern that governments remain reasonably free to continue to take measures that are in the public interest.

As such, the tribunal member argued, "Looking at Article 1110 in context, it is not possible to see it as a generous invitation for tribunals to impose liability on governments that are engaged in the ordinary course of protecting health, safety, the environment and other public welfare concerns." This contextual understanding of state-party obligations, however, would be notably absent in the Metalclad decision.

METALCLAD AWARD DECISION

The METALCLAD dispute has its origins in the 1990 decision by the federal government of Mexico to authorise Confinamiento Tecnico de Residuos Industriales, S.A. de C.V. (COTERIN) to construct and operate a hazardous waste transfer station in Guadalcazar, San Luis Potosi (SLP). Soon after, it became apparent that COTERIN, rather than storing and transferring the waste as authorised, was disposing it untreated onsite. Approximately 20,000 tons were illegally dumped. Once news of this environmental contamination broke, the local community was set into a rage. Numerous federal investigations and inquiries followed. In September 1991, after eleven months of illegal dumping, the

124 Separate Opinion, supra note 115 at para. 118.
125 Ibid.
126 Ibid. at para. 214.
127 Ibid.
COTERIN operation was closed and the entrance was sealed.\footnote{128}{C. Tollefson, "Metalclad v. United Mexican States Revisited: Judicial Oversight of NAFTA’s Chapter Eleven Investor-State Claim Process" (2002) 11 Minn. J. Global Trade 183 at 188-89 [hereinafter "Tollefson"].}

In 1991, and again in 1992, the municipality turned down COTERIN’s applications to convert the closed transfer station into a hazardous waste landfill. Despite these refusals, COTERIN persisted. In 1993, it received an environmental impact authorisation from the Federal Secretariat for Environmental and Natural Resources (SEMARNAP) to proceed with its hazardous landfill development plans, despite the company’s dubious commitment to environmental responsibility and municipal resistance. Simply put, Mexico needed the facility. The country produces approximately ten million tons of hazardous waste per year, but can process only about ten to twenty percent of it. As a result, the illegal dumping of waste is more the rule than the exception.\footnote{129}{Lilley, supra note 121 at 734.}

To assuage governmental concerns about its reliability, COTERIN sought a partnership with Metalclad Corp., one of the largest and most experienced hazardous waste disposal companies in the United States.\footnote{130}{Ibid.}

While COTERIN was in the process of securing state and federal permits, it was also negotiating with Metalclad.\footnote{131}{Tollefson, supra note 128 at 188-89.} Three months after the issuance of the federal construction permit on April 23, 1993, Metalclad entered into a 6-month option agreement to purchase the COTERIN site. The agreement to purchase was conditional upon receiving all the proper permits. Once satisfied these had been provided, Metalclad finalised the purchase and began construction. Shortly after the purchase, the governor of SLP embarked on a public campaign to prevent the operation of the landfill.\footnote{132}{Metalclad, supra note 1 at para. 37.}

On October 26, 1994, the municipal government of Guadalcazar ordered the cessation of all building activities due to the absence of a municipal construction permit.\footnote{133}{Ibid. at para. 28-40.} The federal government claimed it could not intervene. Handcuffed by a stop work order and infuriated by the lack of support from Mexican officials, Metalclad sought redress by means of a US$ 90 million Chapter 11 claim.

In its submission to the ISDM tribunal, Metalclad asserted federal officials had repeatedly assured the firm that it had all the authority necessary to construct and operate the landfill, since the municipality lacked any basis for denying the construction permit. Metalclad claimed federal officials had told them that a municipal construction permit would be advis-
able so as "to facilitate an amicable relationship with the Municipality." Yet, despite local popular opposition and a municipal stop work order, Metalclad resumed construction on November 15, 1994. In Mexico's submissions, they denied federal officials had advised Metalclad that a municipal permit was unnecessary, and argued that Metalclad knew or should have known that the permit was indeed required. Moreover, it was pointed out that Metalclad's actual knowledge of the requirement was implicitly suggested by the fact that Metalclad still pursued a construction permit despite continuing to develop the landfill site in direct contravention of the municipal order.

The characterisation of the nature of the legal consultations between the Mexican federal authorities, Metalclad, and the municipality would become the critical issue within the tribunal decision. Rejecting Mexico's contention that Metalclad was the author of its own misfortune, the tribunal held that the representations of federal officials did indeed occur and that due to the "absence of a clear rule as to the requirement or not of a municipal construction permit, as well as the absence of any established practice or procedure as to the manner of handling applications for a municipal construction permit, amounts to a failure on the part of Mexico to ensure the transparency required by NAFTA."

Although transparency is not a Chapter 11 discipline, the tribunal transplanted the principle from Article 102(1) as an "underlying objective of NAFTA" necessary for implementing the treaty goal of increasing cross-border investment opportunities and ensuring the successful completion of investment initiatives. Article 102(1) states that the "objectives" of NAFTA include the promotion of "national treatment, most-favoured-nation treatment and transparency" so as to, *inter alia*, eliminate trade barriers, promote fair competition and increase investment opportunities. Article 102(2) states that Parties shall interpret and apply the provisions of NAFTA "in the light of its objectives set out in paragraph 1 and in accordance with applicable rules of international law." Based on this language, the tribunal interpreted the Article 1105(1) guarantee as a Minimum Standard of Treatment under international law in terms of Articles 26 and 27 of the *Vienna Convention of the Law of Treaties* - which when read together indicate that domestic legal regimes cannot be relied upon

138 Article 1105 (1) "Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security."
139 *Vienna Convention, supra* note 15.
to excuse the failure to honour international obligations. Consequently, following the customary doctrine of *pacta sunt servanda*, the tribunal found the lack of clarity over the necessity of a municipal permit was not in accordance with the fair and equitable treatment guarantee under Article 1105(1), since it violated NAFTA's treaty objectives outlined under Article 102(1).

As a result, the tribunal ruled that the "authorities of the central government of any Party" have a positive duty to properly inform prospective investors of legal obligations and correct any misunderstandings, if and when they become apparent. In effect, under the legal rubric of Article 102(1) transparency, state parties have a positive obligation to act as legal counsel to investors, and if that advice is faulty, the state is liable. Otherwise, investors will be lost in a foreign landscape without a reliable map.

As evidence of the unacceptably opaque legal environment Metalclad was attempting to operate within, the tribunal noted that immediately following the conclusion of a five-year operational agreement (hereinafter the "*Convenio*") between Metalclad and the federal Secretariat of the Environment (SEMARNAP), the municipality denied Metalclad’s construction permit application, without consultation or explanation. Mexico argued that the town council had simply determined that the ecological and health risks outweighed the benefits for the communities surrounding the site. Yet, due to the lack of regard given to the *Convenio* by the municipality and that Metalclad had not received notice of the town council meeting that decided this issue, the tribunal held the actions of the town council were both unreasonable and *ultra vires* its authority.

Firstly, the tribunal was satisfied the *Convenio* ensured the project

140 *Metalclad*, *supra* note 1 at para. 100.
141 An international law doctrine dictates that a treaty must be kept and interpreted in a manner that maintains the integrity of the original intent and objectives behind the accord.
142 *Metalclad*, *supra* note 1 at para. 78.
143 *Ibid.* at para. 48. The November 25, 1995 "*Convenio*" established an audit schedule to check the project’s compliance with the laws and regulations; to check the project's plans for prevention of and attention to emergencies; and to study the project's existing conditions, control proceedings, maintenance, operation, personnel training and mechanisms to respond to environmental emergencies. It also required Metalclad to contribute two new pesos per ton of waste toward social works in Guadalcazar, free medical advice for the inhabitants of Guadalcazar, and give preference to the inhabitants of Guadalcazar for technical training.
would be consistent with responsible environmental and health standards. Consequently, any suggestion that the municipality was insulated from Chapter 11 liability based on the Article 1114 environmental measures derogation, however interpreted, was thus rejected as immaterial. Secondly, the tribunal completely rejected the submissions of Mexican constitutional expert opinion that the municipality was acting fully within its authority. While acknowledging a construction permit may have been required, the tribunal accepted Metalclad’s argument that the federal jurisdiction over hazardous waste was paramount. The tribunal therefore held that the authority of the municipality only extended to the administration of proper adherence to the terms of federal permits. Consequently, the denial of the Metalclad permit by the municipality in contravention of the Convenio, coupled with the procedural and substantive deficiencies of the denial itself, led the tribunal to find that both the insistence upon and subsequent denial of a municipal construction permit was improper.

After finding Mexico in violation of the Fair and Equitable treatment requirement for failing to provide Metalclad with a predictable legal framework for its investment, the tribunal addressed the issue of expropriation. As an intervener, the United States argued in its submissions that Article 1110 was not intended to create a new definition for expropriation beyond that provided by pre-existing customary international law. Rather than looking to the Third Restatement, the tribunal rejected the American position and instead relied upon a purely textual interpretation of the Article 1110 text concluding:

...expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of

146 Ibid. at para. 98.
147 Article 1114 (1): Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns.
148 Metalclad, supra note 1 at para. 81.
149 Ibid. at para. 97.
151 Metalclad, supra note 1 at para. 103.
the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.

Based on this extremely broad definition of expropriation, the tribunal found that by tolerating the ultra vires actions of the municipality, Mexico undermined the right of Metalclad to operate the landfill. This failure to defend Metalclad in the face of unlawful municipal actions was thus deemed a measure tantamount to expropriation.\footnote{Ibid. at para. 104.}

Furthermore, almost as an after thought, the tribunal noted that after the municipality rejected the building permit for the landfill, the provincial SLP government issued a decree creating a 188,758 hectare ecological preserve around Guadalcazar for the protection of rare cacti. Although Mexico argued that the ecological decree allowed for current non-conforming uses and thus could not be considered expropriation, the tribunal was not persuaded. Under the terms of the environmental management programme set out in the Ecological Decree, any conduct that might involve the discharge of polluting agents on reserve soil, subsoil, running water, or water deposits was completely prohibited. Consequently, since the operation of a hazardous waste landfill site inexorably carries with it at least the possibility of discharging pollution, the Ecological Decree effectively forever barred the prospect of Metalclad successfully pursuing its investment interests.\footnote{Ibid. at para. 110. After finding this to be a violation of Article 1110, the tribunal maintained that it did not need to decide or consider the motivation or intent behind the creation of the ecological preserve.\footnote{Ibid. at para. 111. This conclusion was without any explanation, except the tribunal commented that its finding with respect to the creation of the ecological preserve was not essential to the decision. Nevertheless, the tribunal considered the Ecological Decree to be, in and of itself, an act tantamount to expropriation. The tribunal awarded US$ 16,685,000 as damages.}

**METALCLAD JUDICIAL REVIEW**

In response to the award, Mexico sought judicial review to have the decision quashed.\footnote{Award Review, supra note 3.} Vancouver was the designated place of arbitration before provincial court Justice Tysoe.\footnote{Tysoe J. determined that the dispute was subject to resolution under the International Commercial Arbitration Act, R.S.B.C. 1996, c.233 rather than domes-
assessing the decision, Tysoe J. took note of the reasoning in the *S.D. Myers* decision.\(^\text{157}\) According to the *S.D. Myers* tribunal:\(^\text{158}\)

The inclusion of a "minimum standard" provision is necessary to avoid what might otherwise be a gap. A government might treat an investor in a harsh, injurious and unjust manner, but do so in a way that is no different than the treatment inflicted on its own nationals. The "minimum standard" is a floor below which treatment of foreign investors must not fall, even if a government were not acting in a discriminatory manner.

Justice Tysoe determined that the words of Article 1105(1) express an overall concept and as such, must be read as a whole. Contrary to what the *Metalclad* tribunal concluded, the guarantee that "[e]ach Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security"\(^\text{159}\) does not extend to private actors the full protection and security of the NAFTA treaty. The rights accorded to private investment are discrete and expressly confined by the language in Section A of Chapter 11. Consequently, Justice Tysoe concluded that the words "international law" in Article 1105 refer strictly to customary international law, not treaty law. Indeed, three months after Justice Tysoe rendered his judgment, the NAFTA Free Trade Commission issued an interpretive statement on the ambit of Article 1105(1), unequivocally restricting the...
obligation to provide treatment in accordance with international minimum standards to principles of customary international law.\textsuperscript{160}

According to the \textit{S.D. Myers} tribunal, Article 1105 is violated "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."\textsuperscript{161} In this determination, a high measure of deference should be extended to "the right of domestic authorities to regulate matters within their own borders."\textsuperscript{162} The \textit{Metalclad} tribunal, however, argued that the reasoning in \textit{Pope & Talbot},\textsuperscript{163} which declined to follow the \textit{S.D. Myers} interpretation of Article 1105, was the correct statement of the law. The \textit{Pope & Talbot} tribunal concluded the language of Article 1105 entitles investors to "the international law minimum, plus the fairness elements."\textsuperscript{164} However, based on Article 31(1) of the \textit{Vienna Convention}, which requires that terms of treaties be given their ordinary meaning, Justice Tysoe declined to find any "additive" character in the word "including," since "plus" has virtually the opposite meaning of "including."\textsuperscript{165}

Consequently, in rejecting the \textit{Pope & Talbot} reasoning and finding no authority for the proposition that transparency was a customary norm of international law, Justice Tysoe concluded that the \textit{Metalclad} tribunal did not simply interpret the wording of Article 1105, it misstated the applicable law. It went beyond the terms of its authority and thus, it was open to the court to overturn the decision. The principle fault in the \textit{Metalclad} decision was its reliance on the objectives contained within Article 102(1). Although Article 102(2) provides that NAFTA be interpreted and applied in light of the objectives set out in Article 102(1), it does not require all provisions of NAFTA to be interpreted in light of these principles. Private investors are not party to the accord, but only enjoy rights under the express terms of Chapter 11 provisions. As a result, the entire structural core of the tribunal's analysis was grounded on a concept beyond the scope of its Chapter 11 mandate.\textsuperscript{166}

Turning to the question of an Article 1110 violation, Justice Tysoe concluded that the tribunal's \textit{ultra vires} transparency analysis of Article 1105 "infected" its perception of the expropriation issue.\textsuperscript{167} The tribunal


\textsuperscript{161} Award Review, \textit{supra} note 3 at para. 63.

\textsuperscript{162} \textit{Ibid.}.

\textsuperscript{163} \textit{Pope & Talbot Inc. v. Canada} (April 10, 2001).

\textsuperscript{164} Award Review, \textit{supra} note 3 at para. 64 [emphasis in original].

\textsuperscript{165} \textit{Ibid.} at para. 65.

\textsuperscript{166} \textit{Ibid.} at para. 72.

\textsuperscript{167} \textit{Ibid.} at para. 78.
had concluded that the federal government’s toleration of the municipality’s conduct amounted to unfair and inequitable treatment breaching Article 1105, and therefore, participated or acquiesced in the denial of Metalclad’s right to operate the landfill. In the tribunal’s opinion, this abrogation of responsibility to ensure legal clarity and lawful governmental conduct created a situation tantamount to expropriation due to the sterilisation of the Metalclad investment. However, since the tribunal based this conclusion on an ill-founded concept of a non-existent Chapter 11 transparency obligation, the interpretation was beyond the scope of its authority and thus had to be quashed.168

Although advanced as an apparent afterthought, the tribunal’s decision regarding the Ecological Decree proved to be determinative. Since the finding of an Article 1110 expropriation violation did not rely on the notion of a transparency duty, the tribunal’s analysis fell within its mandate.169

In order to determine whether the tribunal had correctly stated the applicable law, Justice Tysoe noted that the tribunal gave an "extremely broad definition" of expropriation. In addition to the more conventional notion of expropriation involving a taking of property,170

[T]he Tribunal held that expropriation under the NAFTA includes covert or incidental interference with the use of property which has the effect of depriving the owner, in

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168 Ibid. at para. 79.
169 Ibid. at para. 97. As such, Mexico argued that the standard of review should consider a "patently unreasonable error" as grounds for setting aside the award. The concept of "patently unreasonable" is a domestic administrative law concept designed to balance the value of expert tribunal autonomy with judicial accountability. Although a tribunal will be immune from judicial interference with respect to simple errors of law and fact, a court has the authority to overturn outrageous decisions. Pezim v. British Columbia (Superintendent of Brokers), [1994] 2 S.C.R. 557; Pushpanathan v. Canada (Minister of Citizenship and Immigration), [1998] 1 S.C.R. 982. As authority for importing this notion into international commercial arbitration, Mexico relied on the decision in Navigation Sonamar Inc. v. Algoma Steamships Ltd. [1987] R.J.Q. 1346; (1995), 1 M.A.L.Q.R. 1 (Que. S.C.) and argued in its submission that a patently unreasonable error is a prima facie excess of jurisdiction, the toleration of which would be contrary to public policy. Thus, it would be open to the court pursuant s. 34(2)(b)(ii) of the International CAA to overturn such an error. Although Tysoe J. expressed some reservation regarding this standard, since the concept was developed before the Supreme Court had adopted the "pragmatic and functional approach," he nevertheless did opt to apply this test. Since Tysoe J. ultimately found that the Metalclad tribunal did not make a "patently unreasonable error," no determination was needed concerning whether or not this domestic standard could be used to annul a NAFTA Chapter 11 award under the International CAA.

170 Ibid. at para. 99.
whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property. This definition is sufficiently broad to include a legitimate rezoning of property by a municipality or other zoning authority.

According to Mexico, this definition was overly broad. Although mindful of protecting the integrity of international business transactions, customary international law has resisted pressures to expand the obligations of states to compensate beyond actual deprivations of property. Compensation for investment-backed expectations would make it impossible for sovereign governments to take regulatory action for the common good of society.\textsuperscript{171} Thus, Mexico and Canada argued international law recognises the validity of police powers, as long as they are non-discriminatory in nature.\textsuperscript{172} On this point, Canada, as an intervener, urged the court to be mindful of the \textit{S.D. Myers} decision, which expressed the view that non-discriminatory regulatory measures taken in the public interest, particularly in relation to public health and the environment, should not be considered measures tantamount to expropriation.\textsuperscript{173} However, since the definition of expropriation offered by the \textit{Metalclad} tribunal was strictly a question of treaty interpretation, Justice Tysoe held that the court had to defer to its authority. The tribunal's finding of an Article 1110 violation was, despite the misgivings of the court regarding its wider implications for land use regulation, beyond the authority of the court to question, since the tribunal interpretation could reasonably be supported by the text of the provision.

\section*{THE CANADIAN BIODIVERSITY STRATEGY}

The lack of regard afforded environmental considerations in the \textit{Metalclad} decision stands in stark contrast to the importance the Supreme Court of Canada places on environmental regulation. In \textit{R. v. Hydro-Québec}, the Court held that "the protection of the environment is a major challenge of our time. It is an international problem, one that requires action by governments at all levels."\textsuperscript{174} Consequently, Justice Tysoe's warning that the definition of expropriation in the \textit{Metalclad} decision "is sufficiently broad to include a legitimate rezoning of property by

\begin{thebibliography}{9}
\bibitem{171} Tollefson, \textit{supra} note 128 at 217.
\bibitem{172} Canada's Submission (February 16, 2001) at para. 67, online: Department of Foreign Affairs and International Trade <http://www.dfait-maeci.gc.ca/tna-nac/documents/canada_submission-e.pdf>.
\bibitem{173} \textit{Ibid.}
\end{thebibliography}
a municipality or other zoning authority” could have profound implications for the implementation of future environmentally-minded land use zoning. As a particular example, Article 8 of the United Nations Convention on Biodiversity calls for measures "as far as possible" to establish "protected areas" to conserve biodiversity. This is exactly what occurred in Guadalcazar and it was found to be an Article 1110 violation, despite the fact that Metalclad had never actually established the legal right to operate the landfill development. In other words, investment-backed expectations had a greater right to exploit the environment than the community had to sustain its ecological integrity. This is not the view taken by the Supreme Court of Canada in its jurisprudence.

According to the Supreme Court in 114957 Canada Ltée (Spraytech, Société d’arrosage) v. Hudson (Town), "in an era in which matters of governance are often examined through the lens of the principle of subsidiarity ...law-making and implementation are often best achieved at a level of government that is not only effective, but also closest to the citizens affected and thus most responsive to their needs, to local distinctiveness, and to population diversity." The Court took judicial notice of the "realization that our common future, that of every Canadian community, depends on a healthy environment." The Supreme Court has stressed the recognition of the vital importance of preserving our natural heritage for over a decade. In Friends of the Oldman River Society v. Canada (Minister of Transport), the Court forcefully declared, "[E]veryone is aware that individually and collectively, we are responsible for preserving the natural environment... environmental protection [has] emerged as a fundamental value in Canadian society." More than two decades ago, within the context of a deepening appreciation of the weight the environment should have in the fair balancing of competing social interests, the Ontario Court of Appeal in Scarborough v. R.E.F. Homes Ltd. referred to municipal government as a "trustee of the environment." In the recent Spraytech decision, the Supreme Court acknowledged this fiduciary duty and reaffirmed the Court’s approval in R v. Hydro-Québec of a passage from the 1987 United Nations World Commission on the Environment and Development (the Brundtland

175 Award Review, supra note 3 at para. 99.
177 114957 Canada Ltée (Spraytech, Société d’arrosage) v. Hudson (Town), [2001] 2 S.C.R. 241 at para. 3 [Spraytech].
178 Ibid. at para. 1.
179 Friends of the Oldman River Society v. Canada (Min. of Transport), [1992] 1 S.C.R. 3 at pp. 16-17.
181 Spraytech, supra note 177 at para. 1.
Commission) report, which concluded that local governments needed to be "empowered to exceed, but not to lower, national norms."\textsuperscript{182}

The Brundtland Commission report is a seminal document in the evolution of environmental law. It sets out the standards by which the progress of nations towards sustainable development has been measured and has become a touchstone of Supreme Court environmental analysis. The importance of international standards is underscored by a passage in Spraytech, where the Supreme Court quotes R. Sullivan, \textit{Driedger on the Construction of Statutes} (3rd ed. 1994) with approval:\textsuperscript{183}

\begin{quote}
[T]he legislature is presumed to respect the values and principles enshrined in international law, both customary and conventional. These constitute a part of the legal context in which legislation is enacted and read. In so far as possible, therefore, interpretations that reflect these values and principles are preferred.
\end{quote}

A key demand of the Brundtland Commission was for governments, at all jurisdictional levels, to protect the full diversity of flora, fauna, and the ecosystems that support them. In its discussion of the importance of biodiversity conservation, the Brundtland report stated:\textsuperscript{184}

\begin{quote}
[B]efore science can focus on new ways to conserve species, policy makers and the general public for whom policy is made must grasp the size and the urgency of the threat ...Altering economic and land use patterns seems to be the best long-term approach to ensuring the survival of wild species and their ecosystems. This more strategic approach deals with the problems of species depletion at their sources in development policies, anticipates the obvious results of the more destructive policies and prevents damage now.
\end{quote}

In recognition of the worldwide negative impact of declining biodiversity, the global community negotiated the \textit{Biodiversity Convention}. The Canadian delegation was an active participant in these negotiations. Then Prime Minister Mulroney signed the Convention at the Rio Earth Summit in June 1992, and in December 1992, Canada was the first industrialised country to ratify it.

\textsuperscript{182} \textit{R. v. Hydro-Québec}, supra note 174 at para. 126.

\textsuperscript{183} \textit{Spraytech}, supra note 177 at para. 30.

One of the key obligations for parties that have ratified the Convention is to prepare a national strategy. In 1995, the federal government, provinces, and territories entered into a memorandum of understanding for the implementation of the Canadian Biodiversity Strategy, which states, "ecosystems are being degraded and species and genetic diversity reduced at an alarming rate due to the impact of our growing human and increasing resource consumption rates" and as such, the decline in biodiversity is "now recognised as one of the most serious environmental issues facing humanity." In an effort to ameliorate ecological degradation, the federal, provincial, and territorial governments committed themselves, inter alia, to "conserve biodiversity and use biological resources in a sustainable manner." According to the Canadian Biodiversity Strategy, the successful implementation of Canada's obligations under the United Nations Convention on Biological Diversity requires international, national, and local action. Yet, since it is through planning that land use is controlled, municipalities must be free to pursue environmentally-minded zoning policies. Any effective biodiversity strategy needs an effective municipal response; however, if the Metalclad tribunal's understanding of expropriation becomes an established principle of Chapter 11 interpretation, then it is likely that any efforts to protect dwindling biodiversity will be hamstrung.

Pursuant to the Canadian Biodiversity Strategy federal-provincial memorandum of understanding, all levels of government entered into the Accord for the Protection of Species at Risk in Canada, under which federal, provincial, and territorial ministers responsible for wildlife are committed to a national approach for the protection of species at risk. The goal of this agreement is to prevent species in Canada from becoming extinct because of human activity. Toward this end, the federal, provincial, and territorial governments recognise the need to establish complementary legislation and programs that will provide immediate legal protection for threatened or endangered species through habitat protection. Consequently, if the integrity of ecologically significant habitats is to be protected, municipalities, as "trustees of the environment," must give effect to the general goals of the strategy through environmentally conscience land use planning.

185 "Canada’s Biodiversity: A Commitment to its Conservation and Sustainable Use" (1995); Copy obtained from the Biodiversity Convention Office, 351 boul. St. Joseph, 9e étage, Gatineau, Québec.
186 Ibid.
187 Accord for the Protection of Species at Risk, online: Environment Canada <http://www.speciesatrisk.gc.ca/recovery/accord_e.cfm>.
188 Species at Risk is defined by Canadian Endangered Species Conservation Council (CESCC), Wild Species 2000: The General Status of Species in Canada, (Ottawa: Ministry of Public Works and Government Services, 2001).
This necessity has been recognised in international law under *Agenda 21* of the 1992 United Nations Conference on Environment and Development. Canada, as a signatory, assumed a large number of commitments that have important implications for local governments. Chapter 28 of *Agenda 21* recognises that some of the most challenging sustainable development problems concern land use regulation. An effective response to the dilemmas of ecologically-minded land use planning necessitates "[l]ocal authorities construct, operate and maintain economic, social and environmental infrastructure, oversee planning processes, establish local environmental policies and regulations, and assist in implementing national and subnational environmental policies." These broad powers need to be granted to municipalities since "[a]s the level of governance closest to the people, they play a vital role in educating, mobilizing and responding to the public to promote sustainable development."

The issue of sustainable development is particularly problematic with respect to the preservation of biodiversity in highly populated areas, where foreign investment is the greatest. Indeed, the principal dilemma of biodiversity is not how to save the wilderness, but rather, how to hold on to the last vestiges of what once was, but is now being consumed by urban sprawl. As one commentator stated in an essay entitled, "Biodiversity and the Challenge of Saving the Ordinary:"

A focus on the special implies that identifying and protecting a small number of key threads will achieve our goals. But the goal of biodiversity protection is nothing less than preservation of the entire tapestry in a form that allows its designs to be viewed and enjoyed. The loss of every thread diminishes the picture, but no thread is so special that its removal will cause the entire picture to disappear. Protecting the tapestry is a very different task than protecting the best, the most striking, or the most important individual threads or parts of the overall picture. We simply cannot save the whole by identifying and saving the most special parts.

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189 UN Department of Economic and Social Affairs, online: <http://www.un.org/esa/sustdev/agenda21text.htm>.
190 *Agenda 21* s.III (Strengthening The Role Of Major Groups) A.CONF/151/26 (Vol. III). Leadership in promoting and coordinating the Chapter 28 obligations was assumed by the ICLEI (International Council for Local Environmental Initiatives), headquartered in Toronto. Nineteen Canadian municipalities are ICLEI members. See online: ICLEI Local Governments for Sustainability <www.iclei.org> at Chapter 28.1.
192 H. Doremus, "Biodiversity and the Challenge of Saving the Ordinary" (2002) 38 Idaho L. Rev. 325 at 329.
Due to romantic preconceptions about what nature is and should look like, the distribution of threatened biodiversity does not closely correspond with that of protected environmental lands. According to a report by the Canadian Council of Forest Ministers, the "Mixedwood Plains ecozone" of southern Ontario and Québec "is a special genetic conservation priority. Less than 20% of the native forest cover remains, largely owing to forest land conversion for agricultural and urban development, and less than 1% of the ecozone is in highly protected areas."\(^{193}\) The degradation of the Mixedwood Plains ecozone is of great national concern since it contains the greatest diversity of tree species, with more than 100 species of the 180 species of trees native to Canada. Roughly ten million hectares of forests have been cleared in this ecozone, largely for agricultural and urban development.\(^{194}\) Thus, massive ecological degradation has resulted due to a slow, but relentless demise. Tree by tree, forests are disappearing. With less than twenty percent of the forest cover remaining, roughly sixty percent of Canada's threatened species are found in and around the urban centres of southern Ontario and Québec.\(^{195}\) Many species are barely surviving as suitable habitat dwindles. Vital natural features of the Mixedwood Plains ecozone are dangerously close to the threshold levels beyond which they will no longer be able to sustain themselves.

Aside from habitat loss, much of the damage to biodiversity has also been due to habitat fragmentation. The isolation of habitat into small ecological islands creates greater "edge habitat," which fosters increased numbers of predatory species such as crows, grackles, jays, and raccoons, as well as greater nest parasitism by cowbirds. A rise in the prevalence of predatory and parasitic species further diminishes biodiversity. Yet, all is not lost. For example, while ninety-seven percent of the Carolinian Forest of southern-western Ontario has been completely annihilated, nearly all of the plant species indigenous to the area have managed to tenaciously hang on to isolated fragments of their former range.\(^{196}\) Consequently,


\(^{194}\) *Ibid.*


\(^{196}\) T. Mosquin, "Status of and Trends in Canadian Biodiversity," in S. Bocking, ed., *Biodiversity in Canada* (Peterborough: Broadview Press, 2000), 50-70 at 65 states, "[I]n the Carolinian Forest of south-western Ontario, while some 97 percent of the forest has been annihilated, nearly all plant species originally present are still found locally in isolated fragments of their former range, although some are now very rare being reduced to one or two small colonies."
landscape ecology, conservation biology, and restoration ecology have developed strategies for conserving the remaining natural landscapes through landscape retention, environmental restoration, and ecosystem replacement. The key element of these strategies is the identification and protection of core conservation lands. This must be addressed through environmentally-minded land use controls. As long as private landowners are not accountable for the maintenance of critical ecological assets, lands of vital environmental significance will simply whither away.

CANADIAN EXPROPRIATION LAW AND ENVIRONMENTAL REGULATION

Although the political will to implement the stated goals of the Canadian Biodiversity Strategy has been lacking, this has not been due to a lack of legal authority to freeze private land development for public purpose. According to the Supreme Court in

197 In Ontario, the Municipal Board refuses to acknowledge that the rights bundled up in private land have concomitant responsibilities. *Re: Nepean (Twp.) Restricted Area By-law 73-76 (1978),* 9 O.M.B.R. 36 the Board stated, "This Board has always maintained that if any lands in private ownership are to be zoned for conservation or recreational purposes for the benefit of the public as a whole, then the appropriate authority must be prepared to acquire the lands within a reasonable time otherwise the zoning will not be approved," cited in *Minto Developments Inc. v. Ottawa (City)*; [2002] O.M.B.D. No. 1075. The Ontario Court of Appeal in *Russell v. Toronto (City)*, [2000] O.J. No. 4762 while not affirming the substantive content of the Nepean policy per se, recognised the inherent discretionary power of the Board under Ontario Municipal Board Act, R.S.O. 1990, c. O.28.

198 Provincial Policy Statement (PPS) can be issued pursuant s. 3 (5) of the *Planning Act*, R.S.O. 1990, c. P.13 states: In exercising any authority that affects a planning matter, the council of a municipality, a local board, a planning board, a minister of the Crown and a ministry, board, commission or agency of the government, including the Municipal Board, shall have regard to policy statements. In recognition of the importance of the PPS, the Species at Risk Section of the provincial government has expressly stated that PPS is integral to its commitment under the Accord since it "provides direction for municipal land-use planners on how to make sure that species at risk are protected during development and site alteration." See online: Ontario Parks’ Species at Risk Section <http://www.ontarioparks.com/english/sar-protect.html>. Likewise, the federal government has relied on the PPS principles articulated by the s. 2.3 Natural Heritage "significant wetlands” policy to demonstrate Canada’s compliance with the requirements set out under article 14 of the United Nations Convention on Biological Diversity, which demands that parties conduct impact assessments and to minimise pos-
Hartel Holdings, if a development freeze is implemented pursuant to a legitimate and valid planning purpose, then the resulting detriment to landowners is one that must be endured by them in the public interest. Moreover, in direct contradiction to general principles articulated by the *Metalclad* decision, there is no concomitant legal obligation to compensate the holders of private property due to the loss of potential value. As the ancient maxim states, *Privatum incommodum publico bono pensatur*, private disadvantage is made up for by public good. However, such power comes at a political cost and as of yet, provincial and municipal governments have been loath to offend particular vested interests for diffuse environmental benefits.

Nevertheless, there has been a certain degree of "greening" within the land use planning process. Commenting on a growing awareness that as the environment deteriorates, so does our quality of life, an article in the *Municipal and Planning Law Reports* observed:

Municipalities must now plan for future growth and development to ensure not only that an adequate municipal assessment and tax base will be maintained to financially sustain the municipality’s expenditures, but also that suitable parklands, green lands, waterfront lands and open space lands are preserved.

The power to implement such an agenda is described in an oft-quoted passage from *Canadian Law of Planning and Zoning*:

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199 *Hartel,* supra note 11.

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The law permits the appropriation of prospective development rights for the good of the community, but allows the property owner nothing in return. Although the courts have inveighed against this seeming injustice they have seldom invalidated municipal regulations having this effect. It is well settled that owners may be compelled to surrender some value or future value of their land to the local authority and no price has to be paid.

According to the Supreme Court in *Vancouver v. Simpson*, the guiding purpose of zoning is the public interest. The Supreme Court in *CMHC v. North Vancouver* reaffirmed this basic principle of common law. The case involved a petition to quash newly enacted land use controls on 640 acres of CMHC land. The only permissible uses would henceforth be parks, recreation, and open space. This forested property had been acquired three decades previously with the intention of developing it for residential purposes, but the land remained unused. The new bylaws sought to maintain the natural character of this area. The B.C. Court of Appeal held:

There are obvious policy reasons which justify the District’s decision to remove the land from the threat of immediate residential development. Whether the decision was a wise one is not for the court. But it is undoubtedly legitimate for a municipality to consider preserving large areas as parks or other uses which constitute open space. The effect of the rezoning was essentially to preserve for some period into the future the status quo which has existed with this land since CMHC acquired it and indeed before that.

As mentioned previously, in contrast to the *Metalclad* interpretation of Article 1110, no primacy is afforded private investment-backed expectations over public policy considerations. Property law within Canadian jurisprudence has moved away from the supremacy of private capital toward a contextual paradigm. Property rights are interpreted in terms of what individual holders have a right to expect as citizens of a community. As a consequence, the test for regulatory-based expropriation claims (referred to as "de facto expropriation" in Canadian law) has become a very

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arduous test.

The requisite elements for any successful claim of *de facto* expropriation were set out by the Supreme Court in *Manitoba Fisheries Ltd. v. R.*\(^{206}\) and *R. in Right of British Columbia v. Tener and Tener.*\(^ {207}\) The test for a complete "taking" or total extinguishment of rights is that (1) no compensation be paid; and (2) there must be a corresponding benefit in favour of the expropriating authority. Moreover, both elements must be satisfied. There must be a "taking" and a "receiving" by the state. Once this is established, compensation is due. Thus, in stark contrast to the *Metalclad* decision, under Canadian law the mere existence of regulations, in and of itself, no matter how severe, does not create a concomitant duty to compensate those affected. No doubt, it is a basic principle at common law that when such "takings" fall outside of statutory authority, there is a right to compensation. However, if there is statutory authorisation for such takings, the common law right to compensation ceases to exist. Nevertheless, even within statutory authority, the common law right to compensation for *de facto* expropriation can prevail in the interests of fairness.

In considering the elements of this test, an important distinction must be drawn between mere negative prohibitions and restrictions that effectively strip proprietors of all ownership rights. This principle was considered by the Nova Scotia Court of Appeal in *Mariner Real Estate Ltd.*, \(^{208}\) which held:

> The scope of claims of *de facto* expropriation is very limited in Canadian law. They are constrained by two governing principles. The first is that valid legislation (primary or subordinate) or action taken lawfully with legislative authority may very significantly restrict an owner's enjoyment of private land. The second is that the Courts may order compensation for such restriction only where authorized to do so by legislation. In other words, the only questions the Court is entitled to consider are whether the regulatory action was lawful and whether the *Expropriation Act* entitles the owner to compensation for the resulting restrictions.

The "taking" of property must be more than a mere restriction on use—the restriction must be of sufficient severity to remove virtually all rights

\(^{206}\) *Manitoba Fisheries Ltd.*, supra note 10.


associated with the property holder’s interest. Moreover, there must be a transfer of rights to the state. The mere extinguishment of rights is not sufficient to support a claim. Undoubtedly, such a strict test would be intolerable to a Chapter 11 tribunal.

It is useful to recall here that the Metalclad tribunal effectively imposed an obligation to pay compensation whenever a state party merely incidentally interferes with investor interests - even economic benefits that are nothing more than anticipated. As Justice Tysoe pointed out, any environmentally-minded zoning laws would be found in violation of this standard. Canadian de facto expropriation jurisprudence is far more permissive of regulatory action. In a review of the case law, only three instances could be found where the case for de facto expropriation had been established.209

The first case to establish de facto expropriation was Manitoba Fisheries. This dispute involved the creation of a government monopoly, which completely barred the complainants from pursuing their livelihood, thus destroying the commercial "goodwill" their firm built up over years of enterprise. Although the government had the discretionary statutory authority to compensate businesses, the plaintiffs received none, and brought an action for compensation. Since no actual assets were expropriated by the state, the Court needed to determine whether a "taking" had actually occurred. The Supreme Court held that the loss of goodwill built up over the long history of the company had indeed been "taken," and was thus compensable in the absence of clear statutory language:210

[In my opinion the Freshwater Fish Marketing Act and the Corporation created thereunder had the effect of depriving the appellant of its goodwill as a going concern and consequently rendering its physical assets virtually useless and that the goodwill so taken away constitutes property of the appellant for the loss of which no compensation whatever has been paid. There is nothing in the Act providing for the taking of such property by the Government without compensation and as I find that there was such a taking, it follows, in my view, that it was unauthorized having regard to the recognized rule that "unless the words of the statute clearly so demand, a statute is not to be construed so as to take away the property of a subject without compensation;"

210 Manitoba Fisheries Ltd., supra note 10 at 473.
per Lord Atkinson in *Attorney-General v. De Keyser's Royal Hotel*.

Likewise, in *Tener*, the other seminal *de facto* expropriation case, the Court needed to reconcile the fact that no actual property was taken by the government, but the complainants’ business had been effectively terminated by state action. In this case, the complainants possessed a mineral claim in a provincial park. Due to increasingly onerous regulations, they found that it had become impossible to exercise their rights. Eventually, the plaintiffs received a letter from the provincial government informing them that current policy prohibited development within the park. In considering this, the Supreme Court noted, "Ordinarily, in this country, the United States and the United Kingdom, compensation does not follow zoning either up or down."\(^{211}\) However, it was decided that the government had in effect expropriated the plaintiffs’ mineral interests since the "denial of access to these lands occurred under the *Park Act* and amounts to a recovery by the Crown of a part of the right granted to the respondents in 1937. This acquisition by the Crown constitutes a taking from which compensation must flow."\(^{212}\) The practical effect of the regulation was such that "the respondents now have no access to their claims, no ability to develop and realize on them and no ability to sell them to anyone else. They are effectively beyond their reach. They are worthless."\(^{213}\) The third and final successful *de facto* expropriation claim, *Casamiro*, was based upon a factual situation almost identical to that of the *Tener* case.\(^{214}\)

The *Mariner Real Estate Ltd.* is an interesting case for the purposes of contrasting the *Metalclad* expropriation standard with Canadian law.\(^{215}\) In this case, the complainants owned land that fell entirely within an area designated by the Minister of Natural Resources as "beach" land. In order to protect fragile beach ecosystems, *The Beaches Act*\(^ {216}\) set out numerous restrictions on the use of beach lands, including a prohibition against development without the approval of the responsible Minister. Compensation to landowners for the restrictions imposed by the *Act* was expressly precluded. The complainant landowners applied to the Minister for approval to build single-family dwellings, but the applications were

\(^{211}\) *Tener*, *supra* note 207 at 679.

\(^{212}\) *Ibid.* at 685 [emphasis added].


\(^{214}\) *Casamiro*, *supra* note 209.


\(^{216}\) R.S.N.S. 1989, c. 32, amended 1993, c. 9, s. 9.
rejected. Consequently, the trial division court held, "The fee simple in the lands has been stripped of its whole bundle of rights."\(^{217}\) Thus, like Metalcld, the complainants retained legal title to the land, but governmental action tantamount to expropriation had rendered it worthless. In order to fulfill the second branch of the test for *de facto* expropriation, the court found there had been a "taking" with a corresponding benefit to the Crown, since the value of the Crown land from the high water mark seaward had been enhanced. However, the result in *Mariner Real Estate* was over-turned by the Nova Scotia Court of Appeal, which held that the environmental land use restrictions were not of "sufficient severity" to warrant the lower court's finding. Moreover, despite the severe restrictions on land use suffered by the complainant, the court held that "for there to be a taking, there must be, in effect, as ...in *Tener*, an acquisition of an interest in land" and the enhanced value to adjacent Crown land "is not such an interest." To prove *de facto* expropriation, "an owner of an interest in land ...must conclusively prove that there has been, in effect, a confiscation of all reasonable private uses of the interest in the land in question and an acquisition of the same by the statutory authority."\(^{218}\)

This result was heavily influenced by the finding in the Manitoba case, *Steer Holdings*, which held:

> For there to be a statutory taking which gives rise to a claim for compensation, not only must the owner be deprived of the benefit in its property, there must also be a resulting enhancement or improvement conferred upon whatever entity the Legislature intended to benefit. Something must not only be taken away, it must be taken over.\(^{219}\)

Short of actually taking over the use of land, restrictions on land use are to be considered regulatory rather than confiscatory. While such regulations often affect the value of land, they do not give rise to a claim for compensation.

Based on this reasoning, the Nova Scotia Court of Appeal reversed the finding of *de facto* expropriation by the lower court in the *Mariner Real Estate* case. The Court of Appeal found that the loss of economic value could not be considered a "taking" under Canadian law. After an encyclopaedic review of the case law, the Court of Appeal observed:

\(^{217}\) *Mariner Real Estate, supra* note 215 at 746.


We have been referred to no Canadian case in which the decline of economic value of land, on its own, has been held to be the loss of an interest in land. Several cases, on the contrary, recognize the distinction between the value of ownership and ownership itself. This suggests that the loss of economic value of land is not the loss of an interest in land.220

Judicial notice was also taken of the fact that "[i]n this country, extensive and restrictive land use regulation is the norm."221 Almost without exception, such regulation has been found not to constitute compensable expropriation. Further analysing this point, the Court of Appeal quotes with approval the oft-cited passage from Canadian Law of Planning and Zoning, "The law permits the appropriation of prospective development rights for the good of the community but allows the property owner nothing in return."222 In its analysis, the Nova Scotia Court of Appeal expressly rejected the application of American takings jurisprudence to Canadian expropriation law. In Canada, property has no constitutional protection. Due to the "taking clause" in the Fifth Amendment, which prohibits the restriction of private property enjoyment "for public use, without just compensation," American expropriation jurisprudence operates on the basis of a fundamentally different set of assumptions. Indeed, because of this basic difference, the Nova Scotia Court of Appeal noted, "Canadian courts have no similar broad mandate to review and vary legislative judgments about the appropriate distribution of burdens and benefits flowing from environmental or other land use controls."223 Instead, property law in Canada conceives of rights in terms of what individual holders have a right to expect as citizens of a community to which certain duties are owed.

RECENT DEVELOPMENTS

DOMESTIC AND INTERNATIONAL EXPROPRIATION law seems irreconcilably torn between the assumption that no cause of action can arise from simply obeying the law and the notion that individuals should not bear public burdens. In Canada, however, the idea that responsibilities are also bundled with property rights is well entrenched. Consequently, there is fear among some observers that due to the supra-

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220 Mariner Real Estate (C.A.), supra note 218 at para. 71.
221 Ibid. at para. 42.
222 Ibid.
223 Ibid. at para. 101.
constitutional rights enjoyed by foreign investors under Chapter 11, the influence of American style takings law will inevitably become dominant.\textsuperscript{224} Indeed, this is probably a very real possibility. One American observer has commented: \textsuperscript{225}

Although NAFTA does not require that the protection of investments be harmonized among the Parties, such a result would be faithful to the spirit and intent of the Agreement as a method of encouraging foreign investment throughout all three countries. Affording weaker protections would provide disincentive to investment in Canada and Mexico. This is a particularly undesirable result for Mexico, for whom attracting investment is one of the most important goals of participation in the treaty. Thus, applying Article 1110 as an incorporation of U.S. law encourages foreign investment equally in each of the NAFTA countries, which affirms and furthers the free-trade goals of the treaty.

The unprecedented inclusion of a compensation provision for adverse economic impact due to regulatory measures in the new federal \textit{Species at Risk Act} suggests that the influence of American takings law may already be exerting itself. Nonetheless, as argued above, while the jurisprudence on regulatory takings in the United States tends to be more protective of private land interests, due to the police power exception, the difference between American and Canadian law should not be overstated.

In a case almost factually identical to \textit{Mariner Real Estate Ltd.},\textsuperscript{226} the U.S. Supreme Court in \textit{Lucas v. South Carolina Coastal Council}\textsuperscript{227} held that since "all economically beneficial or productive use of land" had been denied, compensation was required. Like the lower court in \textit{Mariner Real Estate Ltd.}, the U.S. Supreme Court recognised that the extraordinary regulatory constraint rendered the property valueless and as such, compensation was due. Yet, in other circumstances, the court indicated that even severe regulatory restrictions, requiring a proprietor to maintain ninety percent of a tract of land in its natural state, would not satisfy the test for regulatory expropriation.\textsuperscript{228} The determination of regulatory expropriation depends upon a factually based assessment of reasonable

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\bibitem{224} Schneiderman (1996), \textit{supra} note 9 at 537.
\bibitem{225} Lilley, \textit{supra} note 121 at 755.
\bibitem{226} \textit{Mariner Real Estate} (trial), \textit{supra} note 208.
\bibitem{227} \textit{Lucas}, \textit{supra} note 70.
\bibitem{228} \textit{Ibid}.
\end{thebibliography}
economic expectations of the proprietor and the nature of the public purpose governing the regulatory action. In effect, the American test for regulatory takings is practically very similar to the Canadian test for *de facto* expropriation, except instead of looking for a mechanical "taking and receiving" by the state, an American court will, on the basis of public policy, consider what public burdens a private citizen can reasonably be expected to bear. Considering the absolute nature of private property protection under Article 1110 according to the *Metalclad* interpretation, a move toward American style takings law by ISDM tribunals would be a positive development.

Indeed, in the United States, concerns about the lack of regard ISDM tribunals have given public policy considerations has become a source of much political consternation. Frank Loy, a former Under Secretary of State for Global Affairs in the Clinton Administration has complained that Chapter 11 "has unacceptably compromised our nations' right to legislate in a way so as to protect the environment and the health of their citizens."229 Such concerns have lead to the formation of a "no greater rights" lobby, lead by Senator John Kerry.230 Recently, a "no greater rights" political coalition successfully sponsored the *Trade Act of 2002*, which requires all future U.S. trade agreements to ensure that foreigners "are not accorded greater substantive rights with respect to investment protections than United States investors in the United States."231 In other words, the Americans have enacted their own version of the Calvo clause.232

Despite the concerns expressed among academics, citizen groups, and politicians about Article 1110, judging by the analysis in the recent *Feldman* ISDM decision,233 it seems that the broad definition of expropriation in the *Metalclad* decision may not be indicative of future tribunal interpretations. The dispute at issue in *Feldman* involved an American


231 19 U.S.C.A. 3802(b)(3): "Recognizing that Unites States law on the whole provides a high level of protection for investment, consistent with or greater than the level required by international law, the principal negotiating objectives of the United States regarding foreign investment are to reduce or eliminate artificial trade-distorting barriers to foreign investment, while ensuring that foreign investors in the United States are not accorded greater substantive rights with respect to investment protections than United States investors in the United States, and to secure for investors important rights comparable to those that would be available under United States legal principles and practice, by ... (D) seeking to establish standards for expropriation and compensation for expropriation, consistent with United States legal principles and practice."


233 *Feldman*, *supra* note 32.
tobacco trading company operating in Mexico that was denied certain tax refunds offered to its Mexican competitors. While the tribunal upheld its claim on the basis of national treatment, it refused to find any form of expropriation. In coming to its conclusion regarding the applicability of Article 1110, the tribunal observed, "The Article 1110 language is of such generality as to be difficult to apply in specific cases." Therein lies much of the problem concerning Article 1110. In a search for clarity, the Feldman tribunal, unlike the Metalclad tribunal, looked to the Third Restatement of the Law of the Foreign Relations of the United States for guidance to determine what does and does not constitute expropriation. The tribunal noted that according to the preferred U.S. standard:

A state is responsible as for an expropriation of property ... when it subjects alien property to taxation, regulation, or other action that is confiscatory, or that prevents, unreasonably interferes with, or unduly delays, effective enjoyment of an alien's property or its removal from the state's territory... A state is not responsible for loss of property or for other economic disadvantage resulting from bona fide general taxation, regulation, forfeiture for crime, or other action of the kind that is commonly accepted as within the police power of states, if it is not discriminatory.

Thus, while not expressly rejecting the Metalclad tribunal's holding that even "incidental interference with the use of property" will result in an obligation to compensate loss, the Feldman tribunal, on the basis of the preferred U.S. standard, adopted a more restrictive interpretation of what should be considered a reasonably-to-be-expected economic benefit. Consequently, the tribunal observed, "not all government regulatory activity that makes it difficult or impossible for an investor to carry out a particular business, change in the law or change in the application of existing laws that makes it uneconomical to continue a particular business, is an expropriation under Article 1110." It then emphasized, "Governments, in their exercise of regulatory power, frequently change their laws and regulations in response to changing economic circumstances or changing political, economic or social considerations. Those changes may well make certain activities less profitable or even uneconomic to continue."

As such, it would seem the Feldman tribunal interpretation of Article

234 Ibid. at para. 98.
235 Ibid. at para. 105 [emphasis in original].
236 Metalclad, supra note 1 at para. 103.
237 Feldman, supra note 32 at para. 112.
238 Ibid.
1110 conforms to the long-standing Canadian proposal that "normal regulation" should not be burdened with a concomitant duty to compensate.\(^{239}\) Previously, Canada issued an official memorandum highlighting the need to articulate clear rules to distinguish between compensable takings and non-compensable regulations.\(^{240}\) This suggestion, however, was received with little enthusiasm from both Mexico and the United States. Presumably, the Americans are confident that ISDM tribunal interpretations of Article 1110 will eventually conform to American takings law. Mexico, on the other hand, is far more interested in attracting foreign investment than regulating it.\(^{241}\) The Feldman tribunal’s interpretation of Article 1110 may have assuaged Canadian concerns regarding regulatory action.

Despite this, the problem of differential rights remains. In order to solve this dilemma, Canada advocates a procedural rather than a substantive interpretation of Article 1110 protection. The Canadian government has suggested that an interpretive statement be issued dictating that henceforth, the host-state’s domestic legal standard for expropriation will be the operative law for Article 1110 claims.\(^{242}\) Yet, due to the complete rejection of American takings jurisprudence within Canadian law and the generally low level of investor confidence in the Mexican legal system, it is unlikely this proposal will find much support.\(^{243}\) Since in direct response to the Metalclad case the NAFTA Free Trade Commission issued an interpretive statement clarifying the ambit of Article 1105, but ignored Article 1110, it is obvious that concern over the lack of clarity in expropriation protection is not great enough to initiate immediate reforms.\(^{244}\) Moreover, despite the American "no greater rights" lobby, on October 7, 2003, the NAFTA Free Trade Commission, celebrating the tenth anniversary of the accord, issued a series of statements on its future, none of which mentioned reform of Article 1110.\(^{245}\) Perhaps trade officials are convinced that the Metalclad decision was an aberration. Given the more restrictive view of the reasonably-to-be-expected economic benefit articulated by the Feldman decision, this may very well be the case. Indeed, the subsequent Methanex decision

\(^{239}\) Banks, supra note 9 at 499.

\(^{240}\) Published in Inside US Trade (Feb. 12, 1999), cited in Mann & von Moltke, supra note 9 at 41.

\(^{241}\) Gantz, supra note 85 at 651.

\(^{242}\) Beauvais, supra note 45 at 288.


stated that "as a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alia, a foreign investor or investment is not deemed expropriatory and compensable."\(^\text{246}\)

CONCLUSION

FROM A CANADIAN PERSPECTIVE, the greater protection afforded foreign investors under Article 1110 continues to present a dilemma. Returning to the example of the Biodiversity Convention, if a provincial or federal government actually begins to generate the political will to use the vast regulatory authority at its disposal to restrict land use pursuant the Canadian Biodiversity Strategy, the resulting differential property protection offered by Chapter 11 could create legal difficulties. Foreign investors would look to the ISDM to recover lost investment-backed expectations, while domestic investors would be forced to suffer losses without remedy. Aside from the domestic political cost, the financial burden of paying off adversely affected foreign investors would be prohibitive. Yet, forecasts of an impending regulatory chill are probably alarmist. Due to the influence of the "no greater rights" lobby in the United States, Article 1110 interpretation will probably eventually become an extension of American takings law. As such, the risk of regulatory paralysis is minimal. Nonetheless, within the Canadian context, the dilemma of differential property rights remains. Consequently, the compensation provision for adverse economic impact contained in the Species at Risk Act may well be a harbinger of future Canadian environmental regulation.

\(^{246}\) The above quote qualifies itself in that an investor my have legitimate expectations of compensation if "specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation." Methanex, supra note 122 at Part IV, Chapt. D at para. 7. While not following the Metalclad decision in substance, this supplementary condition does indicate that the Menthanex tribunal did not wish to preclude an expropriation claim if a factual situation arises similar to that of the Metalclad case.