

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

**BETWEEN**

**METHANEX CORPORATION  
(CLAIMANT/INVESTOR)**

**- AND -**

**UNITED STATES OF AMERICA  
(RESPONDENT/NAFTA PARTY)**

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**FINAL AWARD**

(of the tribunal on jurisdiction and merits)

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**The Tribunal:**

J. William F. Rowley  
Professor W. Michael Reisman  
V. V. Veeder (President)

**PART I - PREFACE**

1. The Claimant, Methanex Corporation ("Methanex"), initiated this arbitration against the Respondent, the United States of America (the "USA"), on 3rd December 1999 under Chapter 11 of the North American Free Trade Agreement ("NAFTA"), as a Canadian investor. As formulated in its Original Statement of Claim of 3rd December 1999, Methanex claimed compensation from the USA in the amount of approximately US\$ 970 million (together with interest and costs), resulting from losses caused by the State of California's ban on the sale and use of the gasoline additive known as "MTBE" (methyl tertiary-butyl ether) which was then intended to become legally effective on 31st December 2002. MTBE is a synthetic, volatile, colourless and

organic ether, with a turpentine-like taste and odour. Methanex was (and remains) the world's largest producer of methanol, a feedstock for MTBE. It has never produced or sold MTBE.

2. Methanex's claim was brought under Article 1116(1) NAFTA, based on the alleged breach by the USA of two provisions in Section A of Chapter 11 of NAFTA: Article 1105(1) and Article 1110(1).
3. The Tribunal was formed on 18th May 2000 to decide Methanex's claim. From the outset, the USA challenged the Tribunal's jurisdiction to decide Methanex's claim and alternatively disputed Methanex's claim on the merits. After several written submissions, procedural sessions and a jurisdictional hearing in July 2001 followed by further written submissions, the Tribunal decided, by its Partial Award of 7th August 2002, that there was no jurisdiction under Chapter 11 to decide Methanex's claim as formulated in its Original Statement of Claim. By permission from the Tribunal, Methanex significantly amended its claim in November 2002 in the form of a "Second Amended Statement of Claim". In all subsequent submissions, the USA maintained its challenge to the Tribunal's jurisdiction and its denial of Methanex's amended claim on the merits.
4. Methanex's amended claim had first been intimated to the Tribunal in the form of drafts prepared in January and February 2001 by its then newly instructed Counsel in these arbitration proceedings. Methanex's claim was there advanced under both Articles 1116(1) and 1117(1) NAFTA, based also on the alleged breach by the USA of Article 1102 NAFTA, in addition to Articles 1105(1) and Article 1110(1).
5. In regard to its draft Amended Statement of Claim of 12th February 2001, Methanex explained the reasons for amending its claim, as follows:

*"Methanex's decision to amend is the result of information it discovered in the fall of 2000 indicating that Archer-Daniels-Midland ("ADM"), the principal U.S. producer of ethanol, misled and improperly influenced the State of California with respect to MTBE. Specifically, Methanex discovered that - during the middle of his 1998 California gubernatorial campaign, and during a time when the future of all oxygenates in California was under active review - now-Governor Gray Davis met secretly with top executives of ADM. On*

August 4, 1998, after receiving an initial \$5,000 campaign contribution from ADM, he traveled to Decatur, Illinois, where ADM is headquartered, on a private plane owned by ADM, in order to confer with executives of ADM.

ADM has a reputation for seeking to create and control markets by influencing the political decision-makers who affect them; to that end, ADM makes large political contributions to both political parties in order to ensure that its interests are furthered. ADM is single-minded in pursuit of its corporate objectives, and its corporate behavior has been harshly condemned by the US Court of Appeals for the Seventh Circuit in a case involving another of ADM's products: 'The facts involved in this case reflect an inexplicable lack of business ethics and an atmosphere of general lawlessness that infected the very heart of one of America's leading corporate citizens. Top executives at ADM and its Asian co-conspirators throughout the early 1990s spied on each other, fabricated aliases and front organizations to hide their activities, hired prostitutes to gather information from competitors, lied, cheated, embezzled, extorted and obstructed justice' *United States v Andreas*, 216 F.3d 645, 650 (7th Cir. 2000).

Two weeks after the secret meeting at ADM's headquarters in Decatur, ADM made a \$100,000 contribution to the Davis campaign, and it made another \$55,000 in contributions over the next four months. Seven months after his initial meeting with ADM officials, the Governor issued the executive order banning MTBE and indicating that ethanol would be the preferred replacement. Shortly thereafter, ADM made yet another \$50,000 contribution to the Governor [Footnote 2 omitted: see below]. Once the MTBE ban was announced, ADM moved into the California oxygenate market: it began selling its U.S. ethanol, and it has been reported that it build an ethanol plant there. "

Two important features of Methanex's explanation, for seeking the Tribunal's permission to amend its case, may here be noted.

6. First, the application to amend was premised on Methanex's receipt of new information during the autumn of 2000, including Methanex's

discovery of a "secret" meeting between Mr Davis and ADM on 4th August 1998. Whilst this meeting undoubtedly took place, there later arose in these arbitration proceedings, after the Tribunal's permission to amend was granted to Methanex, significant issues as to how "secret" this meeting was and whether, in any event, Methanex knew of it in or shortly after August 1998, long before the preparation and submission of its original Statement of Claim of 3rd December 1999.

7. Second, as explained by Methanex in the footnote to this same passage cited above, Methanex made no allegation of bribery or criminal corruption against Mr Davis or ADM or that either otherwise "in any way violated U.S. or California campaign contribution statutes or other relevant laws". Subsequently, throughout these arbitration proceedings, Methanex has specifically *not* alleged any criminal act under the laws of California, Illinois or the USA against Mr Davis, ADM or ADM's officers and employees. Methanex has nevertheless characterised the conduct of Mr Davis as "corruption" (its own phrase), short of criminal or unlawful conduct under the laws of the USA, but nonetheless constituting (in its submission) violations by the USA of Articles 1102, 1105 and 1110 NAFTA.
8. After a series of further pleadings, written submissions and procedural sessions, including an oral procedural meeting in March 2003, Methanex and the USA presented their respective cases on Methanex's amended claim, in writing and orally, at the main hearing held in June 2004. In addition to the written testimony previously adduced by the Disputing Parties, the Tribunal heard oral testimony and received written submissions from Canada and Mexico as NAFTA Parties and from three NGO amici. This main hearing addressed all issues of jurisdiction and merits arising from Methanex's amended claim (excepting only quantum). By agreement of the Disputing Parties, it was held in public, excepting one procedural issue heard in camera at Methanex's request. By this Award, the Tribunal decides those issues and provides reasons for its several decisions.
9. This short recital of five years' legal proceedings disguises a difficult, controversial and complicated dispute, as to both procedure and substance. Given the way in which Methanex successively developed its case up to the end of the main hearing in June 2004, it is necessary to address in this Award several important procedural issues. As to substance, Methanex's and the USA's legal arguments on both jurisdiction and merits have required a close analysis of the factual

and expert evidence adduced by both Disputing Parties. The Tribunal therefore seeks no excuse for the length of this Award. Both Methanex and the USA, including others closely involved in this dispute, are entitled to know the reasons for the Tribunal's procedural and substantive decisions.

10. This Award is divided into six parts, including this Preface. In Part II, the Tribunal addresses the principal procedural matters, including the procedural applications made by Methanex and the USA which remained outstanding at the end of the main hearing in June 2004. In Part III, the Tribunal addresses the principal evidentiary matters, including the Disputing Parties' relevant testimony on factual and expert issues. In Part IV, the Tribunal decides in turn each of the jurisdictional issues and the relevant issues on the merits. In Part V, the Tribunal decides the issues of legal costs and the costs of the arbitration. Part VI records the Tribunal's operative order made by this Award.
11. From this Award and from the Partial Award also, it will be evident that the Tribunal has relied heavily on the submissions of Counsel, who were assisted by many others whose names do not appear on the transcript of the hearings. In adversarial proceedings addressing such a massive, complicated and difficult dispute over many years, it could not be otherwise. At the beginning of this Award, therefore, it is appropriate to record our appreciation of the scholarship and industry which Counsel for the Disputing Parties, Mexico and Canada as NAFTA Parties and the amici have deployed during these lengthy arbitration proceedings, together with their respective experts, assistants and other advisers.

## **ANNEX 1 TO PART I GLOSSARY**

ADM	Archer Daniels Midland
AIT	Canada's Agreement on Internal Trade
AMA	American Medical Association
API	American Petroleum Institute
BCRA	Bipartisan Campaign Reform Act
CAA	Clean Air Act
CAAA	Clean Air Act Amendments of 1990
Cal. EPA	California Environmental Protection Agency
CARB	California Air Resources Board

CaRFG2	California Phase II Reformulated Gasoline Regulations
CaRFG3	California Phase III Reformulated Gasoline Regulations
CEC	California Energy Commission
CEH	Chemical Economics Handbook-SRI International
CFTA	Canada-United States Free Trade Agreement
CIWMB	Cal. EPA, Integrated Waste Management Board
CO	Carbon Monoxide
EC	European Commission
EIA	United States Energy Information Administration
EPA	United States Environmental Protection Agency
ETBE	Ethyl Tertiary-Butyl Ether
FECA	Federal Election Campaign Act
FTC	Free Trade Commission
GAO	United States Governmental Accounting Office
GATT	General Agreement on Tariffs and Trade
GEC	Governors' Ethanol Coalition
IBA	International Bar Association
ICSID	International Centre for Settlement of Investment Disputes
ICJ	International Court of Justice
IEA	International Energy Annual
IARC	International Agency for Research on Cancer
LACMTA	Los Angeles County Metropolitan Transportation Authority
LUFTs	Leaking Underground Fuel Tanks
LUSTs	Leaking Underground Storage Tanks
MCL	Maximum Contaminate Level
METHANEX	Methanex Corporation (Claimant, Canada)
METHANEX-US	Methanex Methanol Company (Texas)
METHANEX-FORTIER	Methanex Fortier Inc (Delaware)
MMT	Methylcyclopentadienyl Manganese Tricarbonyl
MTBE	Methyl Tertiary- Butyl Ether
NAFTA	North American Free Trade Agreement
NIEHS	National Institute for Environmental Health Sciences
NOx	Nitrogen Oxide
NRDC	Natural Resources Defense Council
NTP	National Toxicology Program
OAL	Office of Administrative Law (California)
OEHHA	Office of Environmental Health Hazard Assessment (California)
OSPAR Convention	The Convention for the Protection of the Marine Environment of the North-East Atlantic

PCB	Polychlorinated Biphenyl
RFA	Renewable Fuels Association
RFG	Reformulated Gasoline
RFP	Request for Proposals
RVP	Reid Vapour Pressure
SWRCB	State Water Resources Control Board (California)
TAME	Tertiary-Amyl Methyl Ether
TBE	Tertiary-Butyl Ether
TSE	Toronto Stock Exchange
UC	University of California at Davis
UCLA	University of California, Los Angeles
USDA	United States Department of Agriculture
USDHHS	United States Department of Health and Human Services
USITC	United States International Trade Commission
UFTs	Underground Fuel Tanks
UNCITRAL	United Nations Commission on International Trade Law
USTs	Underground Storage Tanks
VCLT	Vienna Convention on the Law of Treaties
VOC	Volatile Organic Compound
WTO	World Trade Organisation

## **PART II - CHAPTER A**

### **INTRODUCTION**

#### **1) The Partial Award**

1. In Part II of this Award, as already indicated in the Preface, the Tribunal addresses the principal procedural matters arising from these arbitration proceedings.
2. Subsequent to the jurisdictional hearing in July 2001 and the Disputing Parties' posthearing written submissions running into 2002, the Tribunal made on 7th August 2002 its "First Partial Award of the Tribunal on Jurisdiction, Order on the Claimant's Application to Amend its Original Statement of Claim and Order on the Claimant's Application for Documentary Disclosure" (the "Partial Award"). In paragraphs 10-20 of that Partial Award<sup>1</sup>, the Tribunal described the procedural history of these arbitration proceedings up to July 2002. It is therefore unnecessary to repeat much of that description here.

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<sup>1</sup> Along with many other materials in these arbitration proceedings, the Partial Award and the Tribunal's Decisions have been published (but not by the Tribunal) on the internet: e.g. <http://www.naftaclaims.com> and <http://www.state.gov/s/1/c5818.htm>.

For ease of reference only, a copy of the Partial Award is attached hereto as Appendix 6, together with copies of the Tribunal's earlier Decisions on the "Place of Arbitration" and on "Petitions from Third Persons to Intervene as 'Amici Curiae'", as Appendix 4 and Appendix 5 respectively.

3. Accordingly, the Tribunal addresses here only the procedure of these arbitration proceedings subsequent to the Partial Award, including the series of procedural applications made by the Disputing Parties and developed in their written submissions, in procedural sessions held by telephone, at the oral meeting of 31st March 2003 and at the main hearing of June 2004. In addition, it is necessary to re-state certain procedural and other matters relating to the identities of the Disputant Parties and other persons, the applicable law, the re-constitution of the Tribunal, the submissions made respectively by Canada and Mexico under NAFTA Article 1128 and the role of the amici.

## **2) The Disputing Parties and Other Persons**

4. ***Methanex:*** The Claimant is Methanex Corporation ("Methanex"), a company originally incorporated under the laws of Alberta, Canada, and now continuing under the Canadian Business Corporations Act. Methanex produces, transports and markets methanol, with facilities in Canada, the USA, New Zealand, Chile and Trinidad and Tobago. Its headquarters are in Vancouver, British Columbia, Canada.
5. ***Methanex-US:*** Methanex Methanol Company ("Methanex-US") is a general partnership formed under the laws of Texas, USA. Its partners are Methanex Inc. and Methanex Gulf Coast Inc., both incorporated under the laws of Delaware, USA. It is part of Methanex's case that it owns, indirectly, all the shares of these two US companies and thereby, also indirectly, Methanex-US.
6. ***Methanex-Fortier:*** Methanex Fortier Inc. ("Methanex-Fortier") is a company incorporated under the laws of Delaware, USA. It is part of Methanex's case that it owns, indirectly, all the shares in this US company.
7. ***The United States of America:*** The Respondent is the USA which, along with Canada and Mexico, is one of the three Parties to the North American Free Trade Agreement (NAFTA).

8. **California:** The State of California is part of the USA. For ease of reference, the State of California, including California's Government and Legislature, are described below as "California". California is not itself a party to these arbitration proceedings. Nevertheless, its representatives have attended the oral meetings and hearings; and it is also evident to the Tribunal that its representatives have worked closely with the USA in formulating the USA's case in these arbitration proceedings.
9. **Mr Gray Davis:** Mr Davis is not a party to this arbitration; but his activities lie at the centre of the dispute raised by Methanex, successively as California's Lieutenant Governor and Governor. In 1998, Mr Davis was Lieutenant Governor of California (the Governor was then Mr Pete Wilson). On 3rd November 1998, Mr Davis was elected Governor of California; and he was re-elected in November 2002. In November 2003, having been subjected to a recall by California's electorate, Mr Davis lost his gubernatorial office and returned to private life. It was in his first capacity as Lieutenant Governor of California that, on 4th August 1998, Mr Davis attended the meeting over dinner with certain executives from Archer Daniels Midland ("ADM") in Decatur, Illinois. It was in his subsequent capacity as Governor of California that, on 25th March 1999, Mr Davis signed Executive Order D-5-99 (the "California Executive Order"), which is one of the two US measures challenged by Methanex under NAFTA Chapter 11. The Tribunal returns in detail to these matters in Chapters III A and III B of this Award below.
10. As part of its case, Methanex has sought to criticise Mr Davis severely. Although disclaiming any allegation of criminality, Methanex's Counsel has described Mr Davis in terms likely to offend any self-respecting person. The Tribunal addresses the merits of this part of Methanex's case in Part III below; but the Tribunal here addresses, as a matter of procedure, Mr Davis' own position. Mr Davis did not testify in this arbitration; nor was he obliged to do so. Nonetheless, as a person whose character was to be the subject of public criticism in these arbitration proceedings, the Tribunal was concerned that Mr Davis' interests were not overlooked and that he had been made aware of an opportunity to testify in his own defence, if he wanted to do so. Having inquired of the USA at the main hearing, the Tribunal understood that Mr Davis had been made aware of this dispute whilst still Governor of California but had disclaimed any interest in taking

any personal part in these proceedings<sup>2</sup>.

11. **ADM and the Andreas family:** ADM is the largest US producer of ethanol. At the relevant time, various members of the Andreas family held senior executive positions in ADM: Mr Dwayne Andreas was Chairman; Mr Allen Andreas was President and Chief Executive Officer; and Mr Marty Andreas was Senior Vice-President. Neither ADM nor any member of the Andreas family is a party to this arbitration; and yet their activities (as alleged by Methanex) also lie at the centre of the dispute. In particular, in 1998-1999, ADM made a series of financial contributions to the Gray Davis gubernatorial campaign in California; and ADM invited Lieutenant Governor Davis to attend the dinner in Decatur, Illinois on 4th August 1998.
12. As part of its case, Methanex has sought to criticise severely ADM and members of the Andreas family. Although again disclaiming any allegation of criminality, Methanex's Counsel has likewise described ADM's senior officers in terms likely to offend any self-respecting person. The Tribunal addresses the merits of this part of Methanex's case in Part III below; but again the Tribunal here addresses the procedural position of ADM and the Andreas family. Albeit that neither may be wholly unused to public criticism, the Tribunal was concerned that ADM and its senior officers were aware of the opportunity to testify in their own defence, if they wanted to do so. Those concerns were somewhat assuaged by the participation in these arbitration proceedings of Mr Roger Listenberger, at the relevant time Marketing Vice-President, Fuel, Ethanol for ADM and who (inter alios) attended the dinner representing ADM on 4th August 1998: Mr Listenberger gave evidence for the USA in this arbitration in writing and orally at the main hearing in June 2004.

### 3) The Arbitration Tribunal and Secretaries

13. **The Three Arbitrators:** The Arbitration Tribunal now comprises: (i) J. William Rowley Esq of McMillan Binch Mendelsohn LLP, BCE Place, Suite 4400, Bay Wellington Tower, 181 Bay Street, Toronto, Ontario

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<sup>2</sup> See Ms Menaker, Counsel for the USA, Transcript Day 2, p. 422. (For ease of reference in this Award, references to the corrected transcript of the main hearing in June 2004 are as follows: Transcript Day 1 [i.e. 7th June 2005] to Transcript Day 9 [i.e. 17th June 2005], with page number. The corrected transcript is currently available at e.g. <http://www.state.gov/s/1/c5818.htm>. Where reference is made to the transcript of, say, the procedural meeting of March 2003, this is made clear in the relevant footnote.)

M5J 2T3, Canada, having been appointed by Methanex; (ii) Professor W. Michael Reisman, Yale Law School, PO Box 208215, New Haven, CT 06520-8215, USA, having been appointed by the USA (following the resignation of Warren Christopher Esq of O'Melveny & Myers LLP); and (iii) Van Vechten Veeder Esq of Essex Court Chambers, 24 Lincoln's Inn Fields, London WC2A 3EG, England, having been appointed as third arbitrator and president of the Tribunal.

14. As indicated, one of the members of the Tribunal had originally been Mr Warren Christopher, appointed by the USA. Shortly after the Partial Award (which bore Mr Christopher's signature and was made unanimously), Methanex served a Notice of Challenge against Mr Christopher on 28th August 2002. The written basis for this challenge was an alleged relationship between Mr Christopher and his law firm, O'Melveny & Myers LLP, and Governor Davis. Mr Christopher provided a detailed response dated 20th September 2002<sup>3</sup>. He concluded that response by stating that although there was no justifiable basis for questioning his independence or impartiality as an arbitrator<sup>4</sup> in these proceedings, to avoid the continuing distractions of this issue to the Tribunal and to the Disputing Parties, he would withdraw voluntarily as arbitrator<sup>4</sup>. Professor Reisman was subsequently appointed by the USA on 4th October 2002. (Given Methanex's further application in regard to the Partial Award, the Tribunal returns to these events below, in Chapter II E of this Award).
15. **Legal Secretary:** Following the Partial Award, the Tribunal's legal secretary remained Samuel Wordsworth Esq., of Essex Court Chambers, 24 Lincoln's Inn Fields, London WC2A 3EG, England. Mr Wordsworth's appointment was made with the agreement of the Disputing Parties; and as legal secretary, he assumed the same obligations of impartiality, independence and confidentiality as the members of the Tribunal.
16. **Administrative Secretary:** The Tribunal's administrative secretary was Margrete Stevens Esq., Senior Counsel, ICSID, World Bank, Washington DC. The Tribunal also acknowledges the considerable support received from ICSID generally, particularly Mr Malkiat Singh.

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<sup>3</sup> The text of Mr Christopher's response of 20th September 2002 is set out below, in Chapter II E of this Award.

<sup>4</sup> The withdrawal of Mr Christopher later became a ground for Methanex's Request for Reconsideration of Chapters J and K of the Partial Award, considered below in Chapter II E of this Award.

17. At the end of the main hearing in June 2004, the Tribunal separately expressed its thanks to the many persons who provided other essential services to the arbitration<sup>5</sup>.

## **PART II - CHAPTER B APPLICABLE LAW, PROCEDURAL RULES AND RULES OF INTERPRETATION**

### **1) Introduction**

1. This is an international arbitration tribunal, with its place or legal seat fixed at the headquarters of the World Bank, Washington DC, USA in accordance with the Tribunal's Decision of 7th September 2000 on the Place of the Arbitration (Appendix 4 to this Award). Given these features and the terms of NAFTA, the UNCITRAL Arbitration Rules and (to the extent also agreed by the Disputing Parties) the IBA Rules on the Taking of Evidence, it is appropriate to set out here the Tribunal's general approach on applicable laws and rules of law, including rules for the interpretation of the NAFTA provisions at issue in these arbitration proceedings.

### **2) NAFTA and International Law**

2. *Article 1131(1) NAFTA*: Pursuant to Article 1131(1) NAFTA, the Tribunal "shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law".
3. *Article 38(1) of the ICJ Statute*: Methanex has rightly emphasised the reference in Article 1131(1) to "applicable rules of international law", and in this respect Methanex relies on Article 38(1) of the Statute of the International Court of Justice. It provides:

*"The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply:*

*a. international conventions, whether general or particular, establishing rules expressly recognized by the contesting states;*

*b. international custom, as evidence of a general practice accepted as law;*

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<sup>5</sup> Transcript Day 9, pp. 2199-2200.

- c. the general principles of law recognized by civilized nations;*
- d. subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law."*

The Tribunal accepts the approach so far submitted by Methanex; and indeed, that approach is uncontroversial between the Disputing Parties.

4. *GATT and WTO Jurisprudence:* However, Methanex then relies on Article 38(1) of the ICJ Statute in support of its submission that the Tribunal should place weight on jurisprudence developed in respect of the GATT when the Tribunal comes to interpreting the criterion of "likeness" under Article 1102 NAFTA<sup>1</sup>. In addition, Methanex has argued that the USA's protection of its domestic ethanol industry violates numerous provisions of the GATT<sup>2</sup>.
5. As regards the latter argument, the Tribunal does not construe Article 1131 NAFTA as creating any jurisdiction to decide on alleged violations of the GATT. Moreover, Methanex's ultimate position in oral argument was that such violations were not necessarily relevant to the Tribunal's decision on the merits of Methanex's claim under Chapter 11 NAFTA<sup>3</sup>. As interpreted by the Tribunal, its jurisdiction is here limited by Articles 1116-1117 NAFTA to deciding claims that the USA has breached an obligation under Section A of Chapter 11 (there being no allegation of any breach of Article 1503(2) or 1503(3)(a) in this case). There is no specific "envoi" to the GATT in any of the provisions of Section A, namely Articles 1102, 1105 and 1110 NAFTA, in respect of which Methanex alleges breach by the USA<sup>4</sup>. In the Tribunal's view, interpreting Article 1131(1) to create a jurisdiction extending beyond Section A of Chapter 11 would indeed be to transform it, as unwarranted under NAFTA as it was held to be under the OSPAR Convention, "into an unqualified and comprehensive jurisdictional regime, in which there would be no limit *ratione materiae* to the jurisdiction of a tribunal established under" Chapter 11 NAFTA<sup>5</sup>. From the language of Chapter 11, there is every indication that this was not the

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<sup>1</sup> See e.g. Mr Dugan, Counsel for Methanex, Transcript Day 8, pp. 1853-1854.

<sup>2</sup> Methanex's Reply, paras. 198-202.

<sup>3</sup> Mr Dugan for Methanex, Transcript Day 1, p. 155.

<sup>4</sup> Cf. Article 2101 NAFTA, on which Methanex also relies, considered further in Part IV below.

<sup>5</sup> *Access to Information under Article 9 of the OSPAR Convention (Ireland v. United Kingdom)*, para. 85, 42 ILM 1118, 1136.

intention of the NAFTA Parties; and accordingly the Tribunal here disclaims any power to decide Methanex's allegations that the USA has violated provisions of the GATT.

6. As regards Methanex's first argument, however, the position may be different. When it comes to interpreting the provisions of Section A of Chapter 11, in particular in the instant case Article 1102, the Tribunal may derive guidance from the way in which a similar phrase in the GATT has been interpreted in the past. Whilst such interpretations cannot be treated by this Tribunal as binding precedents, the Tribunal may remain open to persuasion based on legal reasoning developed in GATT and WTO jurisprudence, if relevant. If (as appears to be the case) Methanex's argument amounts to no more than this, it accords with the approach taken by the Tribunal<sup>6</sup>. The USA's position was little different: it did not argue that decisions on the meaning of provisions of the GATT fall outside the scope of "judicial decisions" that may be employed as "subsidiary means for the determination of rules of law" pursuant to Article 38 of the ICJ Statute. Rather, the USA maintained that such decisions were inapposite in this case given the significant differences between the relevant texts and the objects and purposes of the different treaties<sup>7</sup>. This is the significant point of difference between the Disputing Parties; and the degree to which the language of Article 1102 NAFTA and the language of Article III.4 of the GATT are similar and, more generally, the extent to which GATT and WTO jurisprudence can assist the Tribunal in this case are matters considered further below, in Part IV of this Award.

### 3) The UNCITRAL Arbitration Rules

7. Pursuant to Article 1120(1) NAFTA, Methanex submitted its claim to arbitration under the UNCITRAL Arbitration Rules (the "UNCITRAL Rules")<sup>8</sup>. It follows from Article 1120(2) NAFTA that the UNCITRAL Rules govern the procedure of the arbitration (except to the extent

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<sup>6</sup> Mr Dugan for Methanex, Transcript Day 1, p. 35: *"Now, is WTO law controlling? No, obviously not. But should it be treated as persuasive precedent if its analysis and its rules are well developed and consistent and logical? Yes, it should be."*

<sup>7</sup> Amended Statement of Defense, para. 304.

<sup>8</sup> See Methanex's Notice of a Submission of a Claim to Arbitration dated 3rd December 1999, p. 2. Article 1120(1) NAFTA provides: *"Except as provided in Annex 1120.1, and provided that six months have elapsed since the events giving rise to a claim, a disputing investor may submit the claim to arbitration under: ... (c) the UNCITRAL Arbitration Rules"*.

modified by Section B of Chapter 11)<sup>9</sup>.

8. By Article 33(1) of the UNCITRAL Rules, the Tribunal is required to apply the law designated by the parties as applicable to the substance of the dispute, namely NAFTA itself (including Article 1131) and applicable rules of international law.
9. To a limited extent, where the UNCITRAL Rules make no provision and the Disputing Parties have not agreed otherwise, the procedure of the arbitration may also be governed by the *lex loci arbitri* and any laws or rules of law thereby designated. This is an issue to which the Tribunal returns in part below in Chapter II I of this Award with regard to the USA's Application to Exclude Certain of Methanex's Evidence.

#### **4) The IBA Rules on the Taking of Evidence**

10. By virtue of an express, written agreement between the Disputing Parties contained in a joint letter to the Tribunal dated 14th August 2000 (subject to certain qualifications there set out), Articles 3, 4 and 5 of the IBA Rules on the Taking of Evidence in International Commercial Arbitration (the "IBA Rules") governed the exchange of documents and the presentation of testimony by expert and factual witnesses. For ease of reference, these provisions are set out in Annex 2 to this Chapter, below.

#### **5) Rules of Interpretation**

11. The Tribunal here addresses two separate sources of law relevant to the interpretation of the NAFTA provisions at issue in these arbitration proceedings: (i) the FTC "Interpretation" of July 2001, read with Article 1121(2) NAFTA; and (ii) the 1969 Vienna Convention on the Law of Treaties.
12. **i) FTC Interpretation:** Pursuant to Article 1131(2) NAFTA: "An interpretation by the [Free Trade] Commission of a provision of this Agreement shall be binding on a Tribunal established under this Section." On 31st July 2001, shortly after the end of the oral hearing of July 2001, the NAFTA Free Trade Commission (the "FTC") adopted certain "interpretations of Chapter Eleven in order to clarify and reaffirm the meaning of certain of its provisions".

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<sup>9</sup> Article 1120(2) NAFTA provides: "*The applicable arbitration rules shall govern the arbitration except to the extent modified by this Section.*"

13. Part A of the Interpretation concerns "Access to documents". It is not relevant for present purposes. Part B concerns Article 1105(1) NAFTA; and it provides:

*"B. Minimum Standard of Treatment in Accordance with International Law*

*1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.*

*2. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.*

*3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).*

*Closing Provision*

*The adoption by the Free Trade Commission of this or any future interpretation shall not be construed as indicating an absence of agreement among the NAFTA Parties about other matters of interpretation of the Agreement."*

14. At the time, not unreasonably, Methanex assumed that the FTC's interpretation was directed specifically at its own argument on Article 1105 NAFTA advanced against the USA in these arbitration proceedings. That argument was apparently made long before the FTC could have begun its interpretative deliberations. The Tribunal expressed a certain sympathy with Methanex's assumption in its Partial Award (paragraph 21, p. 11); but the USA now contends that every claimant invoking Article 1105 against any NAFTA Party has invariably made the same false assumption. Whatever the motive or the timing of the FTC's interpretation, the historical fact remains that the FTC has made what it characterises as an "interpretation" of Article 1105(1) NAFTA. Accordingly, the issue is whether Article 1131(2) NAFTA

applies with the result that the Tribunal is bound by that interpretation (as the USA contends) or whether it is not an interpretation at all but an amendment to Article 1105(1) NAFTA falling outside Article 1131(2) NAFTA (as Methanex contends<sup>10</sup>). That issue is considered further below by the Tribunal, in Part IV of this Award.

15. **ii) The Vienna Convention:** More generally, as was common ground between the Disputing Parties, the provisions of NAFTA are to be interpreted "in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose", in accordance with customary international law rules of interpretation reflected in Article 31(1) of the 1969 Vienna Convention on the Law of Treaties.
16. Article 31(1) of the Vienna Convention is comprised of three separate principles. The first general principle, good faith, requires no further explanation here. As to the second general principle, interpretation in accordance with the ordinary meaning of a term, several scholars have noted that this is not merely a semantic exercise in uncovering the mere literal meaning of a term<sup>11</sup>. As to the third general principle, the term is not to be examined in isolation or in abstracto, but in the context of the treaty and in the light of its object and purpose. One result of this third general principle, being relevant to Methanex's first argument on GATT jurisprudence and Article 1102 NAFTA, is that, as noted by the International Tribunal for the Law of the Sea in *The MOX Plant case* (as also applied in *The OSPAR case*): "the application of international law rules on interpretation of treaties to identical or similar provisions of different treaties may not yield the same results, having regard to, inter alia, differences in the respective contexts, objects and purposes, subsequent practice of parties and travaux préparatoires"<sup>12</sup>.
17. In accordance with Article 1131(1) NAFTA and Article 33(1) of the UNCITRAL Rules, the Tribunal has applied these general principles to the interpretation of the disputed provisions at issue in these proceedings.

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<sup>10</sup> See e.g. Mr Dugan for Methanex, Transcript Day 8, pp. 1836-1837.

<sup>11</sup> See e.g. Sinclair, *The Vienna Convention on the Law of Treaties*, 2nd ed., 1984, p.121. Bin Cheng, *General Principles of Law as Applied by International Courts and Tribunals*, 1953, p.114.

<sup>12</sup> *The MOX Plant case (Ireland v. United Kingdom)*, Order on Provisional Measures, 3rd December 2001, para. 51, 41 ILM 405, 413, quoted in *Access to Information under Article 9 of the OSPAR Convention (Ireland v. United Kingdom)*, para. 141, 42 ILM 1118, 1144.

18. *Articles 31(3) and 32 of the Vienna Convention*: It has also been necessary for the Tribunal to consider the application of Articles 31(3) and 32 of the Vienna Convention.

Article 31(3): *"There shall also be taken into account, together with the context:*

*(a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;*

*(b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;*

*(c) any relevant rules of international law applicable in the relations between the parties."*

Article 32: *"Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:*

*(a) leaves the meaning ambiguous or obscure; or*

*(b) leads to a result which is manifestly absurd or unreasonable."*

It is convenient below to consider each provision in turn.

19. *Article 31(3)(a)*: With respect to Article 31(3)(a) of the Vienna Convention, the USA relies on a "subsequent agreement" between the NAFTA Parties as to the meaning of Article 1110 NAFTA and the particular issue of whether expropriation requires a showing that a property right or interest has been taken<sup>13</sup>. Independent of the effect under Article 1131(2) NAFTA of the FTC's Interpretation of 31st July 2001, that "interpretation" also evidences, according to the USA, an agreement between the NAFTA Parties as to the meaning of Article 1105 NAFTA which it is appropriate for the Tribunal to take into account. In this respect, the Tribunal notes that whilst the language of Article 31(3)(a) is clear, it is useful also to refer for the purposes of confirmation to the International Law Commission's Commentary on

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<sup>13</sup> See Ms Menaker for the USA, Transcript Day 3, p. 566.

what was then Article 27(3)(a). This states that: "an agreement as to the interpretation of a provision reached after the conclusion of the treaty represents an authentic interpretation by the parties which must be read into the treaty for purposes of its interpretation"<sup>14</sup>. This passage was cited (with apparent approval) by the International Court of Justice in the *Kasikili/Sedudu Island case*<sup>15</sup>.

20. It follows from the wording of Article 31(3)(a) that it is not envisaged that the subsequent agreement need be concluded with the same formal requirements as a treaty; and indeed, were this to be the case, the provision would be otiose. According to Daillier et al., *Droit International Public*, as to a subsequent agreement on interpretation: "Il est admis que cet accord postérieur peut être tacite et résulter des pratiques concordantes des Etats quand ils appliquent le traité" ("It is accepted that this subsequent agreement may be tacit and result from the concordant practice of States when they apply the treaty")<sup>16</sup>. From the ICJ's approach in the *Kasikili/Sedudu Island case*, it appears that no particular formality is required for there to be an "agreement" under Article 31(3)(a) of the Vienna Convention.
21. In the light of these factors, the Tribunal has no difficulty in deciding that the FTC's Interpretation of 31st July 2001 is properly characterised as a "subsequent agreement" on interpretation falling within the scope of Article 31(3)(a) of the Vienna Convention. It is therefore unnecessary for the Tribunal here to decide whether or not the express consensus formed by the three NAFTA Parties in these arbitration proceedings, as represented by their written submissions as the Respondent (the USA) and as Parties exercising their procedural rights under Article 1128 NAFTA (Canada and Mexico), is also capable of qualifying as such an "agreement".
22. *Article 32*: With respect to Article 32 of the Vienna Convention, Methanex has sought disclosure from the USA of the negotiating history of Articles 1101, 1102, 1105 and 2101 NAFTA in order to resolve the issues of their interpretation, as considered further below in Chapter II H of this Award. For present purposes, it is sufficient to note that, pursuant to Article 32, recourse may be had to supplementary means of interpretation only in the limited circumstances there specified. Other than that, the approach of the Vienna Convention

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<sup>14</sup> *Yearbook of the International Law Commission, 1966*, Vol. II, p. 221, para. 14.

<sup>15</sup> *Kasikili/Sedudu Island (Botswana v. Namibia) 1999*, ICJ Rep. 1, para. 49.

<sup>16</sup> Daillier et al., *Droit International Public*, 6th ed., p. 254.

is that the text of the treaty is deemed to be the authentic expression of the intentions of the parties; and its elucidation, rather than wide-ranging searches for the supposed intentions of the parties, is the proper object of interpretation<sup>17</sup>.

23. Accordingly, in the Tribunal's view, Methanex's application for the disclosure of documents in this case by the USA, constituting NAFTA's preparatory work as a supplementary means of interpreting the relevant NAFTA provisions, has to meet these requirements of Article 32 of the Vienna Convention. As already indicated, the Tribunal considers this issue further in Chapter II H below.

## **ANNEX 2 TO PART II - CHAPTER B**

### **Articles 3, 4 and 5 of the IBA Rules**

#### **Article 3: Documents**

*1. Within the time ordered by the Arbitral Tribunal, each Party shall submit to the Arbitral Tribunal and to the other Parties all documents available to it on which it relies, including public documents and those in the public domain, except for any documents that have already been submitted by another Party.*

*2. Within the time ordered by the Arbitral Tribunal, any Party may submit to the Arbitral Tribunal a Request to Produce.*

*3. A Request to Produce shall contain:*

*(a) (i) a description of a requested document sufficient to identify it, or*

*(ii) a description in sufficient detail (including subject matter) of a narrow and specific requested category of documents that are reasonably believed to exist;*

*(b) a description of how the documents requested are relevant and material to the outcome of the case and;*

*(c) a statement that the documents requested are not in the possession, custody or control of the requesting Party, and of the reason why that Party assumes the documents requested to be in the possession, custody or control of the other Party.*

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<sup>17</sup> Yearbook of the International Law Commission, 1966, Vol. II, p. 223, para. 18.

4. *Within the time ordered by the Arbitral Tribunal, the Party to whom the Request to Produce is addressed shall produce to the Arbitral Tribunal and to the other Parties all the documents requested in its possession, custody or control as to which no objection is made.*
5. *If the Party to whom the Request to Produce is addressed has objections to some or all of the documents requested, it shall state them in writing to the Arbitral Tribunal within the time ordered by the Arbitral Tribunal. The reasons for such objections shall be any of those set forth in Article 9.2<sup>18</sup>.*
6. *The Arbitral Tribunal shall, in consultation with the Parties and in timely fashion, consider the Request to Produce and the objections. The Arbitral Tribunal may order the Party to whom such Request is addressed to produce to the Arbitral Tribunal and to the other Parties those requested documents in its possession, custody or control as to which the Arbitral Tribunal determines that (i) the issues that the requesting Party wishes to prove are relevant and material to the outcome of the case, and (ii) none of the reasons for objection set forth in Article 9.2 apply.*
7. *In exceptional circumstances, if the propriety of an objection can only be determined by review of the document, the Arbitral Tribunal may determine that it should not review the document. In that event, the Arbitral Tribunal may, after consultation with the Parties, appoint an independent and impartial expert, bound to confidentiality, to review any such document and to report on the objection. To the extent that the objection is upheld by the Arbitral Tribunal, the expert shall not disclose to the Arbitral Tribunal and to the other Parties the contents of the document reviewed.*
8. *If a Party wishes to obtain the production of documents from a person or organization who is not a Party to the arbitration and from whom the Party cannot obtain the documents on its own, the Party may, within the time ordered by the Arbitral Tribunal, ask it to take whatever steps are legally available to obtain the requested documents. The Party shall identify the documents in sufficient detail and state why such documents are relevant and material to the outcome of the case. The Arbitral Tribunal shall decide on this request and shall take the necessary steps if in its discretion it determines that the documents would be relevant and material.*
9. *The Arbitral Tribunal, at any time before the arbitration is concluded, may request a Party to produce to the Arbitral Tribunal and to the other Parties any documents that it believes to be relevant and material to the*

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<sup>18</sup> Article 9.2 sets out seven grounds (a) - (g), here incorporated by reference.

*outcome of the case. A Party may object to such a request based on any of the reasons set forth in Article 9.2. If a Party raises such an objection, the Arbitral Tribunal shall decide whether to order the production of such documents based upon the considerations set forth in Article 3.6 and, if the Arbitral Tribunal considers it appropriate, through the use of the procedures set forth in Article 3.7.*

*10. Within the time ordered by the Arbitral Tribunal, the Parties may submit to the Arbitral Tribunal and to the other Parties any additional documents which they believe have become relevant and material as a consequence of the issues raised in documents, Witness Statements or Expert Reports submitted or produced by another Party or in other submissions of the Parties.*

*11. If copies are submitted or produced, they must conform fully to the originals. At the request of the Arbitral Tribunal, any original must be presented for inspection.*

*12. All documents produced by a Party pursuant to the IBA Rules of Evidence (or by a non-Party pursuant to Article 3.8) shall be kept confidential by the Arbitral Tribunal and by the other Parties, and they shall be used only in connection with the arbitration. The Arbitral Tribunal may issue orders to set forth the terms of this confidentiality. This requirement is without prejudice to all other obligations of confidentiality in arbitration.*

#### **Article 4: Witnesses of Fact**

*1. Within the time ordered by the Arbitral Tribunal, each Party shall identify the witnesses on whose testimony it relies and the subject matter of that testimony.*

*2. Any person may present evidence as a witness, including a Party or a Party's officer, employee or other representative.*

*3. It shall not be improper for a Party, its officers, employees, legal advisors or other representatives to interview its witnesses or potential witnesses.*

*4. The Arbitral Tribunal may order each Party to submit within a specified time to the Arbitral Tribunal and to the other Parties a written statement by each witness on whose testimony it relies, except for those witnesses whose testimony is sought pursuant to Article 4.10 (the "Witness Statement"). If Evidentiary Hearings are organized on separate issues (such as liability and damages), the Arbitral Tribunal or the Parties by*

*agreement may schedule the submission of Witness Statements separately for each Evidentiary Hearing.*

*5. Each Witness Statement shall contain:*

*(a) the full name and address of the witness, his or her present and past relationship (if any) with any of the Parties, and a description of his or her background, qualifications, training and experience, if such a description may be relevant and material to the dispute or to the contents of the statement;*

*(b) a full and detailed description of the facts, and the source of the witness's information as to those facts, sufficient to serve as that witness's evidence in the matter in dispute;*

*(c) an affirmation of the truth of the statement; and*

*(d) the signature of the witness and its date and place.*

*6. If Witness Statements are submitted, any Party may, within the time ordered by the Arbitral Tribunal, submit to the Arbitral Tribunal and to the other Parties revised or additional Witness Statements, including statements from persons not previously named as witnesses, so long as any such revisions or additions only respond to matters contained in another Party's Witness Statement or Expert Report and such matters have not been previously presented in the arbitration.*

*7. Each witness who has submitted a Witness Statement shall appear for testimony at an Evidentiary Hearing, unless the Parties agree otherwise.*

*8. If a witness who has submitted a Witness Statement does not appear without a valid reason for testimony at an Evidentiary Hearing, except by agreement of the Parties, the Arbitral Tribunal shall disregard that Witness Statement unless, in exceptional circumstances, the Arbitral Tribunal determines otherwise.*

*9. If the Parties agree that a witness who has submitted a Witness Statement does not need to appear for testimony at an Evidentiary Hearing, such an agreement shall not be considered to reflect an agreement as to the correctness of the content of the Witness Statement.*

*10. If a Party wishes to present evidence from a person who will not appear voluntarily at its request, the Party may, within the time ordered by the*

*Arbitral Tribunal, ask it to take whatever steps are legally available to obtain the testimony of that person. The Party shall identify the intended witness, shall describe the subjects on which the witness's testimony is sought and shall state why such subjects are relevant and material to the outcome of the case. The Arbitral Tribunal shall decide on this request and shall take the necessary steps if in its discretion it determines that the testimony of that witness would be relevant and material.*

*11. The Arbitral Tribunal may, at any time before the arbitration is concluded, order any Party to provide, or to use its best efforts to provide, the appearance for testimony at an Evidentiary Hearing of any person, including one whose testimony has not yet been offered.*

**Article: 5 Party-Appointed Experts**

*1. A Party may rely on a Party-Appointed Expert as a means of evidence on specific issues. Within the time ordered by the Arbitral Tribunal, a Party-Appointed Expert shall submit an Expert Report.*

*2. The Expert Report shall contain:*

*(a) the full name and address of the Party-Appointed Expert, his or her present and past relationship (if any) with any of the Parties, and a description of his or her background, qualifications, training and experience;*

*(b) a statement of the facts on which he or she is basing his or her expert opinions and conclusions;*

*(c) his or her expert opinions and conclusions, including a description of the method, evidence and information used in arriving at the conclusions;*

*(d) an affirmation of the truth of the Expert Report; and*

*(e) the signature of the Party-Appointed Expert and its date and place.*

*3. The Arbitral Tribunal in its discretion may order that any Party-Appointed Experts who have submitted Expert Reports on the same or related issues meet and confer on such issues. At such meeting, the Party-Appointed Experts shall attempt to reach agreement on those issues as to which they had differences of opinion in their Expert Reports, and they shall record in writing any such issues on which they reach agreement.*

*4. Each Party-Appointed Expert shall appear for testimony at an Evidentiary Hearing unless the Parties agree otherwise and the Arbitral Tribunal accepts this agreement.*

5. *If a Party-Appointed Expert does not appear without a valid reason for testimony at an Evidentiary Hearing, except by agreement of the Parties accepted by the Arbitral Tribunal, the Arbitral Tribunal shall disregard his or her Expert Report unless, in exceptional circumstances, the Arbitral Tribunal determines otherwise.*

6. *If the Parties agree that a Party-Appointed Expert does not need to appear for testimony at an Evidentiary Hearing, such an agreement shall not be considered to reflect an agreement as to the correctness of the content of the Expert Report.*

## **PART II - CHAPTER C THE ARBITRAL PROCEDURE**

### **1) Introduction**

1. In this Chapter, the Tribunal summarises the significant procedural events culminating in the main hearing held in June 2004 and subsequent events to the date of this Award. It is not necessary to deal here with less significant events which are recorded at length in the extensive correspondence passing between the Disputing Parties and the Tribunal; all relevant matters are recorded in the files and papers of the arbitration which are in the possession of the Disputing Parties (and a full set of the papers is in the ICSID archives).

### **2) Methanex's Requests for Clarification and Reconsideration of the Partial Award**

2. At the outset of the arbitration, as indicated in the Preface above, Methanex's claim was set out in a Statement of Claim dated 3rd December 1999 and later in a draft Amended Statement of Claim dated 12th February 2001. That draft was significantly clarified by Methanex in subsequent oral and written submissions up to the end of the procedural hearing in July 2001.

3. In the Partial Award, the Tribunal decided that, pursuant to Article 1101(1) NAFTA, it had no jurisdiction in respect of Methanex's claim as pleaded in the Statement of Claim of 3rd December 1999. The Tribunal also decided, in the light of Methanex's written and oral clarifications, that part of Methanex's draft Amended Statement of Claim could potentially meet the jurisdictional requirements of Article 1101(1). Accordingly, Methanex was invited by the Tribunal to serve a

"fresh pleading" in respect of its allegations of a malign intent behind the US measures to favour the US ethanol industry and to harm "foreign" MTBE producers and "foreign" methanol producers such as Methanex. (The meaning and effect of the Partial Award is an issue between the Disputing Parties; and the Tribunal returns to this issue later in this Award).

4. Shortly after the Partial Award, on 28th August 2002, Methanex made a Request for Interpretation of the Partial Award, to which the Tribunal responded in writing by letter dated 25th September 2002. Much later, on 28th January 2004, Methanex made a further Request for Reconsideration of Chapters J and K of the Partial Award. Contrary to apparent suggestions otherwise, Methanex now accepts that it made no request for clarification or reconsideration of the Partial Award between 28th August 2002 and 28th January 2004<sup>1</sup>. The Tribunal considers Methanex's further Request of 28th January 2004 below, in Chapter II E of this Award.

### **3) Methanex's First and Subsequent Requests for Additional Evidence**

5. On 4th October 2002, Methanex lodged its "First Request for Additional Evidence", seeking an order from the Tribunal enabling it to obtain certain witness and documentary evidence. This Request was made by reference to the IBA Rules and 28 U.S.C. §1782. This Request was subsequently refined by Methanex; and it generated numerous written and oral submissions from the Disputing Parties which are set out and considered by the Tribunal below, in Chapter II G of this Award.

### **4) Methanex's Second Amended Statement of Claim**

6. Pursuant to the Tribunal's invitation by the Partial Award and by letter dated 21st October 2002, Methanex served its "fresh pleading" in the form of the Second Amended Statement of Claim on 5th November 2002, with accompanying evidential materials<sup>2</sup>. This amended claim was pleaded in respect of two measures adopted by the State of California: (i) the California Executive Order signed by the Governor

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<sup>1</sup> Mr Dugan for Methanex, Transcript Day 8, p. 1819.

<sup>2</sup> This title "Second Amended Statement of Claim" is the name given to this pleading by Methanex. In fact, in the Partial Award, the Tribunal did not allow Methanex's application to amend its claim as set out in the draft Amended Statement of Claim dated 12th February 2001. Thus, although the pleading of 5th November 2002 is here described as the Second Amended Statement of Claim, it is strictly Methanex's first Amended Statement of Claim in these arbitration proceedings. For ease of reference, however, the Tribunal is content to follow Methanex's nomenclature.

of California on 25th March 1999 and (ii) the California Regulations adopted on 2nd September 20003. Methanex contended that in enacting these measures California intended to discriminate against and thereby harm Methanex and all foreign methanol producers. Methanex alleged breach by the USA of three provisions in Section A of Chapter 11 of NAFTA: Articles 1102, 1105 and 1110 NAFTA; and it relied on Articles 1116 and 1117 NAFTA to found its substantive complaints against the USA.

7. Also pursuant to the Tribunal's order by letter dated 21st October 2002, Methanex served a Summary of Evidence, together with supporting factual materials on 31st January 2003.
8. Pursuant to Article 1121 NAFTA, Methanex appended to its Second Amended Statement of Claim a consent to arbitration and waiver of other dispute settlement procedures. There had initially been a dispute raised by the USA as to the validity of Methanex's waiver, but this particular dispute was resolved by agreement prior to the Partial Award<sup>4</sup>. Much later, Methanex's application of 13th June 2004 to amend its Second Amended Statement of Claim (during the main hearing) raised new issues with respect to the scope of the existing consent to arbitration and waiver; and these issues are considered by the Tribunal below, in Chapter II F of this Award.

### **5) The Procedural Meeting of 31st March 2003**

9. In paragraphs 168 and 172(4) of the Partial Award, the Tribunal indicated that after considering the scope and nature of Methanex's fresh pleading and accompanying evidential materials, it intended to consult the Disputing Parties and then to decide how to proceed further in the arbitration proceedings. In a telephone conference-call of 7th February 2003, the Tribunal heard submissions from the Disputing Parties on the issue of whether the USA should plead in turn, as a fresh pleading, an Amended Statement of Defense (including all subsisting and any new jurisdictional objections) in answer to Methanex's Second Amended Statement of Claim; and if so, what should be the scope of that pleading and when that pleading should be filed by the USA.
10. Having considered the Disputing Parties' submissions, on 12th February 2003, the Tribunal invited the USA to submit a "fresh pleading", setting out its jurisdictional objections to Methanex's Second

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<sup>4</sup> Partial Award, paras. 13 and 93.

Amended Statement of Claim and also responding to that pleading insofar as Methanex's case on "Intent" was concerned. The Tribunal also ordered both Disputing Parties to provide the Tribunal with brief written submissions setting out their respective positions on the nature and timing of the next stages of the arbitration proceedings.

11. The USA served a Supplemental Statement of Defense on Intent on 21st March 2003 which, together with a letter from the USA of the same date, requested an evidential hearing limited to the issue of "intent", namely whether California intended the relevant measures to address suppliers to MTBE producers, i.e. methanol producers such as Methanex. A Response was served by Methanex on 26th March 2003, by which Methanex opposed the USA's application.
12. The Disputing Parties' written submissions were developed at a procedural meeting held in Washington DC on 31st March 2003<sup>5</sup>. It took place at the World Bank, Washington DC. The hearing was recorded by transcript<sup>6</sup>.
13. In summary, the USA submitted that an evidential hearing limited to the issue of discriminatory "intent" would be appropriate for two principal reasons: (i) it would be the most efficient way for the Tribunal to proceed, given that it would not require the Tribunal at that stage to consider bulky scientific evidence adduced by Methanex on the MTBE ban or the relative merits of MTBE and ethanol, and (ii) by reference to Article 21(4) of the UNCITRAL Rules, it was for the Tribunal to rule on the USA's jurisdictional challenges as a preliminary question before holding any full hearing on the merits. On this approach, the USA proposed a procedure leading to an oral hearing in September 2003, lasting not more than three days.
14. In summary, Methanex contended that the most efficient way to proceed would be to move to a full hearing on the merits, with the Tribunal ruling on the USA's jurisdictional challenges in its final award. On this approach, Methanex proposed an evidential hearing of indeterminate length (but roughly estimated at eight days), originally suggested for January 2004 but, on further reflection at the procedural meeting, for about April 2004.

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<sup>5</sup> The Disputing Parties also made submissions on Methanex's application in respect of further evidence (considered below, in Chapter II G of this Award).

<sup>6</sup> Part II - Chapter C - Page 5 The transcript is available at <http://www.state.gov/documents/organization/19455.pdf>.

## 6) The Tribunal's Orders of 2nd and 30th June 2003

15. By order of 2nd June 2003, the Tribunal decided not to rule as a preliminary question on the USA's extant jurisdictional challenges. It decided following Methanex's proposal and pursuant to the exceptional procedure set out in Article 21(4), second sentence, of the UNCITRAL Rules to join all such jurisdictional challenges to the merits of the dispute and to proceed to a main hearing to address all such issues, excluding issues of quantum (which, if appropriate, were to be addressed at a subsequent hearing).
16. The Tribunal's order by letter of 2nd June 2003 is set out in full below:

*"The Tribunal has now concluded its deliberations on the future form of these arbitration proceedings under Article 21 of the UNCITRAL Arbitration Rules; and I set out the Tribunal's decision below:*

*In Paragraphs 166 to 168 of the Partial Award of August 2002 (page 70), the Tribunal indicated that the resumption of the jurisdictional stage after Methanex's fresh pleading was not an attractive option; the USA's jurisdictional challenges depended on issues intimately linked to the merits of Methanex's case; and there was a forensic need for an evidential hearing, at least in part. Nonetheless, the Tribunal was concerned to identify one or more threshold or other determinative issues on which limited testimony could be adduced at that evidential hearing, without proceeding necessarily to a full hearing of all factual and expert witnesses.*

*Following Methanex's fresh pleading and materials served in January 2003, the USA requested an evidential hearing limited to the issue of discriminatory "intent", namely whether California intended the relevant measures to address suppliers to MTBE producers, such as Methanex: see the USA's letter dated 21st March 2003, its enclosed Supplemental Statement of Defense on Intent and its oral submissions advanced at the procedural meeting of 31st March 2003. The USA submitted that such an evidential hearing would be appropriate for two principal reasons: (i) it would be the most efficient way for the Tribunal to proceed, given that it would not require the Tribunal at this*

*stage to consider the bulky scientific evidence adduced by Methanex on the MTBE ban or the relative merits of MTBE and ethanol and (ii), by reference to the "general" approach required by Article 21(4) of the UNCITRAL Arbitration Rules, the Tribunal should rule on the USA's jurisdictional challenges as a preliminary question before holding any full hearing on the merits. On this approach, the USA proposed a procedure leading to an oral hearing in September 2003, lasting not more than three days. Methanex opposed the USA's application in its written and oral submissions. In summary, Methanex contended that the most efficient way to proceed would be a full hearing on the merits, with the Tribunal ruling on the USA's jurisdictional challenges in its final award. On this approach, Methanex proposed an evidential hearing of indeterminate length (but roughly estimated at eight days), originally suggested for January 2004 but on further reflection at the procedural meeting, two or more months later.*

*The choice for the Tribunal and the Disputing Parties is stark; the practical difference is significant; and whilst the choice is not complicated, the decision for the Tribunal was particularly difficult in this arbitration. After much consideration, given in particular the new shape of Methanex's pleaded case, we have decided broadly in favour of the procedure suggested by Methanex, subject to certain important explanations. Accordingly, the Tribunal decides not to rule as a preliminary question on the USA's extant jurisdictional challenges but, pursuant to the exceptional procedure set out in Article 21(4), second sentence, of the UNCITRAL Arbitration Rules, to join all such jurisdictional challenges to the merits of the dispute and to proceed to a main hearing currently intended to address all such issues (excluding issues of quantum), resulting in an award in which the Tribunal may rule on both jurisdictional and merit issues. This procedure requires the following time-table:*

*(1) By [30th September 2003], the USA shall complete its Fresh Pleading, together with all evidential materials adduced in support of its case, in answer to Methanex's Fresh Pleading (excluding all issues of quantum);*

*(2) By [31st October 2003], Canada and Mexico are invited to make any submissions pursuant to NAFTA Article 1128;*

*(The Tribunal invites the Disputing Parties to comment whether amici curiae should be requested to make any written submissions at this stage or at a later stage);*

*(3) By [1st December 2003], Methanex shall submit a Reply to the USA's Fresh Pleading, together with all further evidential materials in rebuttal of the USA's evidential materials;*

*(4) By [2nd February 2005], the USA shall submit a Rejoinder to Methanex's Reply, together with all further evidential materials in rebuttal of Methanex's evidential materials;*

*(5) As regards witness statements and expert witness reports, the Disputing Parties shall follow the requirements of Articles 4 and 5 of the IBA Rules, respectively;*

*(6) Depending on the differences between the expert reports adduced by the Disputing Parties, the Tribunal may make one or more orders under Article 5(3) of the IBA Rules, requesting the expert witnesses to "meet and confer" and make a joint or supplementary report prior to the main hearing;*

*(7) Not later than thirty days before the start of the main hearing, Methanex and the USA shall advise the Tribunal of the identity of any witness advanced by the other which it requires to cross-examine at the hearing; and upon such notification, unless otherwise ordered by the Tribunal, that witness shall be available as an oral witness at the main hearing; and*

*(8) Beginning on [a date in March/April 2005], there shall be a hearing at the World Bank, Washington DC (not to exceed eight days) at which principally (i) the Disputing Parties shall address all the USA's extant jurisdictional challenges, including the USA's new challenge made in Paragraphs 109 to 113 of its Supplemental Statement of Defense on Intent (pages 35-37); (ii) the Disputing Parties shall address the merits of Methanex's Claim, excepting all issues of quantum; and (iii) the relevant factual and expert oral witnesses shall be examined by the Disputing Parties before the Tribunal.*

*(It may be necessary later to modify or add further items to this timetable, including a further procedural meeting).*

*As indicated above, this order requires three particular explanations. First, given that the Tribunal did not have an opportunity to review the timetable's specific dates with the Disputing Parties at the procedural meeting held in Washington DC on 31st March 2003, we have placed the specific dates in square brackets to allow the Disputing Parties an opportunity to comment in writing on a more appropriate timetable, such comments to be received by the Tribunal within the next 14 days. (It should be noted, however, that no further comment is requested from the Disputing Parties on the issues of principle already decided by the Tribunal).*

*Second, it should be self-evident that nothing should be assumed from this order as to the relative merits of the USA's jurisdictional challenges and Methanex's opposition to such challenges. Those challenges and opposition are maintained in full before the Tribunal; and the Tribunal has yet to deliberate on such challenges, still more to make any jurisdictional ruling on such challenges. It is procedurally possible for the Tribunal to rule in favour of one or more such challenges in its award, rendering any decision on the merits unnecessary; and equally, it is procedurally possible for the Tribunal to reject all such challenges.*

*Third, the Tribunal intends that the proposed procedure should work in a broadly neutral manner for both Disputing Parties, notwithstanding that Methanex proposes it and the USA opposes it. By virtue of Articles 38-40 of the UNCITRAL Arbitration Rules, the Tribunal has jurisdiction to award costs in its discretion; and the Tribunal's decision on jurisdictional and/or merit issues might be an important factor in the exercise of that discretion. In other words, the Tribunal is not disempowered from making an order for costs against Methanex (as a solvent claimant) if the Tribunal should decide eventually in favour of the USA's one or more jurisdictional challenges, i.e. that the Tribunal had no jurisdiction over the Disputing Parties' dispute. If the position were otherwise (and we do not understand Methanex to so contend), the Tribunal's order would take a materially different form.*

*Lastly, the Tribunal has still to address certain other matters raised by the Disputing Parties relating to 28 US § 1782, the role of the amici curiae and other procedural issues. It will do so as soon as practicable, after resolving the specific dates required for this new timetable."*

17. After receiving written submissions from the Disputing Parties on the issue of timetabling, by order of 30th June 2003 the Tribunal fixed the timetable for service of written submissions and other materials. It also fixed the date for the main hearing of issues of jurisdiction and the merits to commence on Monday, 7th June 2004, estimated to last eight days (but not estimated to last more than ten days).

### **7) The Tribunal's Orders of 10th October 2003 and 28th May 2004**

18. Between June 2003 and June 2004, there were a number of procedural applications and sessions held by telephone conference-call. It is only necessary here to record two procedural matters.
19. (i) *Expert Reports*: By letter of 27th August 2003, the USA requested an order requiring Methanex to supply all the materials that its scientific experts had relied upon in preparing their expert reports. The USA relied upon paragraph 163 of the Partial Award, which required Methanex to file with its fresh pleading "copies of all evidential documents on which it relies (unless identified as documents previously filed with the Tribunal)", and Article 3.1 of the IBA Rules, which provides in relevant part "each Party shall submit to the Arbitral Tribunal and to the other Parties all documents available to it on which it relies, including public documents and those in the public domain". In addition, the USA made a specific request for the underlying programming and key assumptions used in one of the tables (Table 1) to the report of Methanex's expert witness, Professor Gordon Rausser.
20. Methanex objected to the USA's request by letter of 3rd September 2003 on the basis that it was relying on the expert reports, not on the underlying materials that the expert in question relied on when drafting his or her report. It maintained that, under the IBA Rules (Article 6.5), the right of a party to examine information relied on by an expert related only to a tribunal-appointed expert (as opposed to party-appointed expert witness), and that nothing in the Partial Award or the IBA Rules provided for what was in effect a traditional request for expert discovery by the USA. (Article 6.5 of the IBA Rules was not part of the Disputing Parties' agreement to apply Articles 3, 4 & 5 of the IBA Rules to these proceedings). Methanex also confirmed that all of the material referenced in its expert reports was either publicly available or had been supplied to the USA, save for one specified water control survey of March 2001. The USA responded by letter of 4th September 2003, arguing inter alia that Methanex was plainly relying on the data that its scientists relied upon and that the

USA was entitled to know that part of the case that it (the USA) had to meet at the main hearing.

21. On 10th October 2003, the Tribunal ordered that Methanex's expert reports (just as the expert reports of the USA) must comply fully with the requirements of the relevant IBA Rules and the Tribunal's orders. With respect to publicly available information, Methanex was ordered to provide identification of this information to the USA and its designated experts. With respect to the water control survey of March 2001, Methanex was ordered to provide access to this documentation for the USA and its designated experts. No order was made in respect of Table 1 to Professor Rausser's expert report. Before the main hearing in June 2004, Methanex complied with the Tribunal's order.
22. *ii) Main Hearing Procedure:* Following the procedural session held by telephone conference-call with the Disputing Parties on 24th May 2004, the Tribunal made a further procedural order in regard to the procedure for the main hearing beginning on 7th June 2004, by letter dated 28th May 2004. It suffices here to cite only a part of this order:

*"(iv) Draft Time-Table: The Disputing Parties will seek to agree and, no later than 2nd June 2004, shall submit to the Tribunal a draft hearing timetable setting out (inter alia) the anticipated dates, times and order in which it is currently intended that the designated witnesses of the USA will be called at the Main Hearing. This draft timetable is intended only for the fair and efficient planning of the main hearing, including the personal convenience of witnesses; and it is understandably subject to change, depending upon the main hearing's actual circumstances;*

*(v) Opening Oral Statements: In accordance with the wishes expressed by the Disputing Parties, Methanex shall make its opening statement on Monday, 7th June 2004 (taking not more than one day); and the USA shall make its opening statement on Tuesday and Wednesday, 8th and 9th June 2004 (taking not more than two days). If Methanex should finish its statement before the end of Day 1, the main hearing shall break until the beginning of Day 2 when the USA shall make a clean start with its statement; and likewise if the USA should finish its statement before the end of Day 3, the first witness shall nevertheless not begin his or her testimony before the beginning of Day 4;*

*vi) Equality of Time: Broadly, the Tribunal intends to operate the time available to the Disputing Parties on the basis of equality, subject to the overriding requirement of fairness and recognizing that Methanex will require more time than the USA in cross-examining the designated oral witnesses;*

*(vii) Oral Witnesses: The designated witnesses shall be examined as follows: (a) brief examination-in-chief (direct examination) by the USA, (b) cross-examination by Methanex, and (c) re-examination (re-direct) by the USA. Whilst the USA may examine its witnesses in chief (direct examination), it is nonetheless understood that the existing written witness statement should stand as evidence-in-chief (direct evidence) and that such examination-in-chief should therefore not last more than ten minutes without the prior permission of the Tribunal. It is also understood that the scope of cross-examination shall be confined to the scope of the witness's written testimony and any additional evidence-in-chief. Likewise, it is also understood that the scope of any re-examination (re-direct evidence) shall be confined to the scope of the cross-examination. Any departure from these understandings will require the prior permission of the Tribunal, which in the circumstances will not lightly be granted. Factual and Expert Witnesses will not be allowed in the hearing room whilst another witness is being examined (unless the witness in question has already completed his or her testimony);*

*(viii) Closing Oral Statements and Post-Hearing Written Submissions: Each Disputing Party shall make an oral closing statement once the examination of the witnesses has been concluded, with Methanex to go first, followed by the USA. As requested by the Disputing Parties, the Tribunal will re-visit at the main hearing the question whether post-hearing written submissions will be necessary. Likewise, the Tribunal will address, in consultation with the Disputing Parties, at what stage any further oral or written submissions from Canada and Mexico would be received by the Tribunal (if any); ...*

*(x) USA's Motion to Exclude Certain of Methanex's Evidence: Methanex shall serve no later than 31st May 2004 a written response to the USA's Motion of 18th May 2004. It is understood that Methanex may likewise seek to exclude certain*

*of the USA's evidence; and if so, that application shall be made in writing also not later than 31st May 2004. Subject to further order next week, both Disputing Parties should be ready to develop their respective submissions on this matter in their opening statements at the main hearing;*

*(xi) Methanex's Request for Disclosure of the NAFTA Negotiating History: The USA shall serve no later than 3rd June 2004 a written response to Methanex's request made by letter of 10th May 2004. Subject to further order next week, both Disputing Parties should be ready to develop their respective submissions on this matter also in their opening statements at the main hearing;*

*(xii) Other Applications: At the main hearing, the Disputing Parties may develop their respective submissions in respect of Methanex's Request for a reconsideration of Chapters J and K of the First Partial Award and Methanex's application in respect of 28 USC § 1782. (The Disputing Parties have confirmed that there are no other procedural applications currently outstanding or about to be made to the Tribunal); ..."*

The Disputing Parties produced time-tables prior to the main hearing; and at the main hearing the Disputing Parties jointly decided not to submit post-hearing briefs, limiting themselves to oral closing statements at the end of that hearing.

## **8) Methanex's Application Concerning Evidentiary Matters**

23. On 31st May 2004, Methanex submitted its Motion Concerning Evidentiary Matters, divided into three parts. First, Methanex submitted that the USA should be bound by official admissions made by the USA and California, including inter alia the 1993 admission of the US Environmental Protection Agency (EPA) to the effect that a primary impact of mandating ethanol use would be severely to damage foreign methanol producers such as Methanex. Second, Methanex submitted that the Tribunal should adopt adverse inferences where the USA had failed to produce evidence, notably in respect of the failure to produce the negotiating history of NAFTA, the absence of key witnesses and blocking Methanex from gathering third party evidence. Third, Methanex responded to the USA's Motion dated 18th May 2004 (which is considered separately below).

24. Methanex did not develop the first and second parts of this Motion

as separate matters at the main hearing in June 2004, but developed them as part of its general oral submissions on the evidence. The Tribunal therefore approaches the Motion in the same light; and Methanex's contentions in respect of admissions against interest and the drawing of adverse inferences are considered separately below. In short, however, the Tribunal has declined to accept the so-called admissions or to draw the general inferences invoked by Methanex, both being unwarranted on the factual evidence.

## **9) The Disputing Parties' Pre-Hearing Written Submissions**

25. Prior to the main hearing of June 2004, and in accordance with the procedure and timetable established by the Tribunal's orders of 2nd and 30th June 2003 (with subsequent minor amendments as to time tabling thereafter), the Disputing Parties made written submissions to the Tribunal as set out below, alongside the written submissions made by Canada and Mexico as NAFTA Parties pursuant to Article 1128 NAFTA:

*5th December 2003:* USA Amended Statement of Defense.

*30th January 2004:* Fourth Submission of Canada under Article 1128 NAFTA.

*30th January 2004:* Mexico Submission under Article 1128 NAFTA.

*19th February 2004:* Methanex Reply to the Amended Statement of Defense.

*23rd April 2004:* USA Rejoinder; and

*23rd April 2004:* Methanex Reply to the Article 1128 Submissions of Canada and Mexico.

## **10) The Amici**

26. By order of 15th January 2001, the Tribunal ruled that certain amici curiae - the International Institute for Sustainable Development, Communities for a Better Environment and the Earth Island Institute - might make amicus submissions to the Tribunal in writing; and that the Tribunal might invite these amici to make further submis-

sions whether in writing or orally if it considered this to be appropriate to the conduct of the arbitration. (A copy of the Tribunal's Ruling appears at Appendix 5 to this Award).

27. On 7th October 2003, the FTC, noting that no provision of NAFTA limits a tribunal's discretion to accept written submissions from a person or entity that is not a disputing party, issued a statement on non-disputing party participation. This statement recommended (inter alia) procedures for the participation of non-disputing parties in proceedings under NAFTA Chapter 11<sup>7</sup>. On 31st October 2003, Methanex wrote on behalf of both Disputing Parties to suggest that the Tribunal adopt the FTC statement subject to two common understandings concerning (i) identification by amici of any entity with which it collaborated in preparing submissions; and (ii) a right to respond to any NAFTA Article 1128 submissions from Canada or Mexico on amicus submissions. This suggestion was agreed by the USA; and the Disputing Parties' agreement was adopted by the Tribunal.
28. In accordance with the procedures of the FTC statement, as put in place by the Tribunal with the agreement of the Disputing Parties, the Tribunal received two applications for permission to file a non-disputing party submission: (i) the application for amicus curiae status by International Institute for Sustainable Development dated 9th March 2004, and (ii) the application of non-disputing parties for leave to file a written submission by Earthjustice on behalf of Bluewater Network, Communities for a Better Environment and Center for International Environmental Law, also dated 9th March 2004. In each case, as provided in the FTC statement, the application was accompanied by the written submission that the amicus curiae sought to submit to the Tribunal. By letter of 26th March 2004, the USA submitted that the Tribunal should grant the permission requested by the potential amici, whilst by letter of the same date Methanex indicated that it did not object to the granting of such permission by the Tribunal<sup>8</sup>.

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<sup>7</sup> The full text of this statement may be obtained from <http://www.dfait-maeci.gc.ca/nafta-alena/Nondisputing-en.pdf>.

<sup>8</sup> The Tribunal notes that in its joint statement of 16th July 2004, the FTC stated: *"We are pleased that the transparency initiatives we took during our October 2003 meeting have already begun to improve the operation of the investment chapter investor-state dispute-settlement mechanism. Earlier this year, for the first time a tribunal accepted written submissions from a non-disputing party and adopted the procedures that we recommended following our October 7, 2003 meeting in Montreal, for the handling of such submissions."*

29. The Tribunal does not seek to summarise here the contents of the amici submissions, which were detailed and covered many of the important legal issues that had been developed by the Disputing Parties<sup>9</sup>.
30. On 23rd April 2004, Methanex submitted its Reply to the Submissions of Earthjustice and the International Institute for Sustainable Development as amici. At the main hearing in June 2004, the legal representatives of the amici had no special status, although they were of course entitled to attend (and did attend) in the special room set aside for members of the public at the World Bank to witness the main hearing.

### **11) Canada and Mexico: Article 1128 NAFTA**

31. On 30th January 2004, the Tribunal received written submissions made pursuant to Article 1128 NAFTA from both Canada and Mexico. The submission of Canada concerned the interpretation of Articles 1102 and 1110 NAFTA. In brief, Canada submitted that the "like circumstances" test under Article 1102 was not the same as the "like products" test under the GATT and that, with respect to Article 1110, as a matter of international law, expropriation did not result from bona fide regulation by the State.
32. The submission of Mexico concerned the interpretation of Articles 1101, 1102, 1105, 1110, 1116-1117, 1131 and 1139 NAFTA. In brief, Mexico submitted that Article 1102 concerned only the case where "less favourable treatment" was accorded because of the investor's nationality; and that the fact that a measure offended one of Articles 1102 or Article 1105 did not mean that it offended the other. It submitted that Article 1110 incorporates the principle that States are generally not liable to compensate aliens for economic loss resulting from nondiscriminatory measures taken to protect the public interest; and that goodwill, market share and customer base are not investments within Article 1139 and therefore cannot be expropriated within the meaning of Article 1110. It also submitted that Articles 1116-1117 incorporate a standard of proximate causation.
33. These written submissions are considered further, as appropriate, in Part IV below. No oral submissions were made by either Canada or Mexico at the main hearing in June 2004. On 24th June 2004, Canada and Mexico were invited by the Tribunal to make any further submissions

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<sup>9</sup> These submissions are available on the internet at <http://www.state.gov/s/1/c5818.htm>.

pursuant to Article 1128 NAFTA. However, both NAFTA Parties confirmed (by letters dated 5th and 8th July 2004 respectively) that they did not wish to make further submissions to the Tribunal.

## 12) The Main Hearing of June 2004

34. The oral hearing on the USA's challenges to jurisdiction and on the merits of Methanex's claim took place over nine days at the World Bank, Washington DC, from Monday, 7th June to Thursday, 17th June 2004. It was recorded by transcript, subsequently corrected by agreement of the Disputing Parties. The Disputing Parties were represented by Counsel, as follows:
- a. *Methanex*: Christopher F. Dugan, Esq., Claudia Callaway, Esq., Alexander W. Koff, Esq., Sabina Rose Smith Esq., and Matthew S. Dunne Esq., all of Paul, Hastings, Janofsky & Walker LLP, 1299 Pennsylvania Avenue NW, 10th Floor, Washington, DC 20004-2400, USA;
  - b. *The USA*: William H. Taft IV, Esq., Ronald J. Bettauer Esq., Mark A. Clodfelter, Esq., Barton Legum, Esq., Andrea J. Menaker, Esq., David A. Pawlak, Esq., Jennifer I. Toole, Esq., CarrieLyn D. Guymon, Esq., and Mark S. McNeill, Esq., all of the US Department of State, Office of the Legal Adviser, Suite 203, South Building, 2430 E Street NW, Washington, DC 20037-2800, USA.
35. Mexico and Canada were represented as follows:
- a. *Canada*: G. Colin Barker Esq., Trade Policy Analyst - International Trade Canada, Stephen de Boer Esq., Head of Section - International Trade Canada; Carolyn Knobel Esq., Counsel - International Trade Canada, and Douglas M. Heath Esq., First Secretary - Embassy of Canada, Washington, D.C.
  - b. *Mexico*: Adriana González Arce Brilanti Esq., Counsel - Secretariat of the Economy, Salvador Behar Lavalle Esq., Legal Counsel for International Trade - Embassy of Mexico, Washington DC, J. Christopher Thomas QC, J. Cameron Mowatt Esq of Thomas & Partners, Vancouver, Canada and Stephan E. Becker Esq of Shaw Pittman LLP, Washington DC.
36. In addition, each Disputing Party was attended by other persons whose names are recorded in the files and need not be repeated here, including (for the USA) representatives from the Office of the

US Trade Representative, the US Department of Treasury, the US Department of Labor, the US Environmental Protection Agency, the California Environmental Protection Agency and the California State Water Resources Control Board.

37. At the main hearing in June 2004, oral testimony was heard from the following witnesses of fact and expert witnesses:

(A) *Methanex Factual Witnesses (in order of appearance):*

- (1) *Mr Robert Puglisi*, Private Investigator, M. Morgan Cherry & Associates Limited [Day 3, x 589, xx 617, xxx 671]10;
- (2) *Ms Claire N. Morisset*, Paralegal, at an un-named law firm in Washington DC [Day 3, x 680, xx 709, no xxx];
- (3) *Mr James A. Stirwalt*, Private Investigator, Bonanza Investigations, Inc. (testimony by videolink) [Day 7, x 1603, xx 1607, no xxx]; and
- (4) *Mr Patrick McAnish*, Private Investigator, Beach Investigations (testimony by videolink) [Day 7, x 1619, xx 1628, xxx 1678].

The USA did not request the cross-examination of any other factual or expert witness proffered by Methanex in its evidential materials, namely its expert witnesses from Exponent, Professor Gordon Rausser, Professor C. Herb Ward and Dr Pamela Williams; nor its other legal experts (not as such proffered as witnesses by Methanex), Sir Robert Jennings and Dr Claus-Dieter Ehlerman.

(B) *USA Factual Witnesses (in order of appearance):*

- (5) *Mr Roger Listenberger*, Marketing Vice-President, Fuel, Ethanol for ADM [Day 4, x 769, xx 778, no xxx];
- (6) *Mr Daniel Weinstein*, Managing Director of Wetherly Capital Group (testimony by videolink) [Day 4, x 813, xx 821, no xxx];
- (7) *Mr Richard Vind*, Chairman and Chief Executive Officer, Regent International [Day 4, x 936, xx 950, xxx 1022]; and
- (8) *Mr Dean C. Simeroth*, Chief of the Criteria Pollutants Branch, CARB [Day 5, x 1268, xx 1271, no xxx].

(C) *USA Expert Witnesses (in order of appearance):*

- (9) *Mr Kenneth Dexter Miller*, independent engineering consultant to the petrochemicals industry (testimony by telephone) [Day 4, x 904, xx 911, no xxx];
- (10) *Dr Anne Happel*, Managing Director of EcoInteractive Inc [Day 5, x 1103, xx 1115, no xxx];
- (11) *Professor Graham E. Fogg*, Professor of Hydrogeology at the University of California [Day 5, x 1217, xx 1229, no xxx];
- (12) *Mr Bruce F. Burke*, Vice-President Petroleum and Chemicals at Nexant Inc. [Day 6, x 1404, xx 1415, no xxx]; and
- (13) *Professor Dr William Edward Whitelaw*, Professor of Economics at the University of Oregon, President of ECONorthwest [Day 6, x 1491, xx 1505, no xxx].

Methanex did not request the cross-examination of any other factual or expert witness proffered by the USA in its evidential materials, namely Mr Shannon Faith Baxter and Mr James Caldwell, or its legal experts (not proffered as witnesses by the USA) Professor Joseph R. Grodin and Professor Detlev V. Vagts.

- 38. The Methanex factual witnesses listed above had not originally been scheduled to testify at the main hearing; and they testified only with respect to the USA's application dated 18th May 2004 for the exclusion of certain evidence submitted by Methanex (which is considered further by the Tribunal below, in Chapter II I of this Award).
- 39. At the end of the main hearing on 17th June 2004, subject to Article 29(2) of the UNCITRAL Rules and the receipt of specified written materials from the Disputing Parties and Canada and Mexico, the Tribunal closed the hearings pursuant to Article 29(1) of the UNCITRAL Rules<sup>11</sup>.

### 13) Post-Hearing Written Submissions

- 40. Following the hearing of June 2004, and in accordance with the

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<sup>11</sup> Transcript Day 9, p. 2198. Article 29(1) provides: "*The arbitral tribunal may inquire of the parties if they have any further proof to offer or witnesses to be heard or submissions to make and, if there are none, it may declare the hearings closed.*"

directions of the Tribunal, the Tribunal received further written submissions as follows:

- 1) On 29th June 2004, Methanex submitted its "History and Amendments to California Phase Three Reformulated Gasoline (CaRFG3)"; and
  - 2) By joint letter dated 29th June 2004, the Disputing Parties submitted agreed corrections to the transcript of the main hearing of June 2004.
41. On 19th July 2004, pursuant to the Tribunal's directions given on 17th June 2004, the Tribunal received submissions on costs from both Disputing Parties. Methanex in its brief submission advised the Tribunal that the order of magnitude of costs sought from the USA was US \$11-12 million. This figure was said to include costs estimates for (i) the Tribunal, (ii) expert and factual witnesses, (iii) non-legal advisors, (iv) legal costs, (v) travel, and (vi) allowance for internal salary allocation. The USA's submission was more detailed and supported by witness statements of Barton Legum Esq. (Counsel for the USA), Ms Mary Reddy (Personnel Officer of the US State Department) and Mr John Rinaldi (Budget Analyst of the US State Department). The USA sought an order from the Tribunal that Methanex bear the costs of the arbitration as well as the USA's costs for legal representation and assistance in the amount of US \$2,989,423.76.
  42. By letter dated 2nd August 2004, the USA submitted first that Methanex's "two paragraph" letter was wholly inadequate for the purpose of Articles 38 and 40 of the UNCITRAL Rules. Second, the USA submitted that Methanex's claim "highlights" the reasonableness of the USA's request for less than US \$3 million under Article 38(e) of the UNCITRAL Rules.
  43. As already indicated above, the Tribunal received no further submissions from Canada and Mexico pursuant to Article 1128 NAFTA, both having separately confirmed by letters dated 5th and 8th July 2004 (respectively) that neither wished to take up the opportunity offered by the Tribunal's letter dated 24th June 2004 to make any further submission.
  44. By letter dated 29th June 2004, as amici, the International Institute for Sustainable Development, Bluewater Network, Communities for

a Better Environment and the Center for International Law, sought permission from the Tribunal to make a further written submission on a legal issue. Methanex opposed that application by letter dated 30th June 2004; and by letter dated 23rd July 2004 the Tribunal stated that it would not accede to the request of the amici.

## **PART II - CHAPTER D THE DISPUTE: METHANEX'S CLAIM, THE US MEASURES, AND THE USA'S DEFENCES**

### **1) Introduction: MTBE, Methanol and Ethanol**

1. It is here convenient to summarise briefly the essential characteristics of the claim as eventually advanced in Methanex's Second Amended Statement of Claim of November 2002, it being recalled that Methanex's claim was originally set out in its Statement of Claim of December 1999 and subsequently in drafts of January and February 2001. The Tribunal also here sets out briefly the essential characteristics of the USA's Amended Statement of Defense of December 2003, pleaded in response to Methanex's Second Amended Statement of Claim.
2. **MTBE:** As already indicated earlier in this Award, Methanex's claim is brought in relation to the production and sale of a methanol-based source of octane and oxygenate for gasoline which is known as methyl tertiary-butyl ether or, in short, MTBE. According to Methanex, MTBE is a safe, effective and economic component of gasoline; and it is the oxygenate of choice "in markets where free and fair trade is allowed"<sup>1</sup>. It is also said to produce significant environmental and other benefits; and that it does not pose a risk to human health or the environment<sup>2</sup>.
3. **Methanol:** Methanex does not produce or sell MTBE. It is Methanex's case that its sole business is the production, transportation and marketing of methanol; and that it is the world's largest producer and marketer of methanol, accounting for approximately 17% of global capacity. It is Methanex's case that approximately one third of its methanol production is utilised in the fuel sector, principally for use in methanol-based MTBE. According to Methanex, there are no methanol production plants located in California; and, in the period 1993-2001, only a small amount of the methanol directly consumed in California was produced anywhere in the USA (an average of 20.2 thousand met-

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<sup>1</sup> Second Am. Claim, paras. 12 and 89.

<sup>2</sup> Id., paras. 91-94 and 101-102.

ric tons out of a total consumption figure of 185.5 thousand metric tons). It is Methanex's case that most of the methanol consumed in that period (72%) was produced in Canada, and that Methanex was the largest supplier to the California marketplace for Methanol<sup>3</sup>.

4. It is uncontested that methanol is the essential oxygenating element of MTBE. According to Methanex, methanol can also be used directly as a fuel oxygenate<sup>4</sup>. This is contested by the USA.
5. **Ethanol:** Ethanol is a source of octane and oxygenate for gasoline, generally manufactured from biomass feedstocks, such as corn. According to Methanex, ethanol is plainly an inferior product to MTBE, both environmentally and economically<sup>5</sup>. It is Methanex's case that the ethanol industry in the USA is almost entirely a domestic industry which exists solely as a result of US governmental protection<sup>6</sup>.
6. **Interchangeability:** It is an important part of Methanex's case that methanol and ethanol are essentially interchangeable with one another as oxygenates, as are their respective ethers MTBE and ETBE. Methanex claims that, as recognised by the US Clean Air Act Amendments 1990, both methanol and ethanol can be used directly as oxygenates. Alternatively, both can be used as a feedstock to produce a derivative ether oxygenate, MTBE and ETBE respectively. Accordingly, Methanex claims that oxygenate consumers have a binary choice between methanol and ethanol. It is Methanex's case that there are three significant groups of oxygenate consumers (i) integrated oil refineries, (ii) merchant ether-oxygenate producers and (iii) wholesale gasoline blenders; and that methanol competes with ethanol for the business of each of these three groups<sup>7</sup>.

## 2) The 1997 California Bill and the US "Measures"

7. During these arbitration proceedings, Methanex has attacked four legislative texts as "measures"; and it is convenient to list each in turn.
8. **(i) The 1997 California Bill:** In its Statement of Claim of 3rd December 1999, Methanex challenged Bill 521 of the California Senate dated 9th October 1997 (the "California Bill"; also referred to below as "California Senate Bill 521"). Methanex subsequently withdrew this challenge; and the California Bill is *not now* a "measure"

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<sup>3</sup> Id., para. 86.

<sup>4</sup> Id., para. 70.

<sup>5</sup> Id., para. 93.

<sup>6</sup> Id., para. 158.

<sup>7</sup> Id., paras. 77-83. There appears to be some overlap so far as concerns catego-

impugned by Methanex in these proceedings<sup>8</sup>. (A copy is attached as Appendix 1 to this Award).

9. Nevertheless, the California Bill remains of considerable importance to an understanding of the US measures that Methanex does challenge in these proceedings. Section 2 of the California Bill provided:

*"The Legislature hereby finds and declares that the purpose of this act is to provide the public and the Legislature with a thorough and objective evaluation of the human health and environmental risks and benefits, if any, of the use of methyl tertiary-butyl ether (MTBE), as compared to ethyl tertiary-butyl ether (ETBE), tertiary amyl methyl ether (TAME) and ethanol, in gasoline, and to ensure that the air, water quality, and soil impacts of the use of MTBE are fully mitigated."*

10. Section 3(a) of the California Bill appropriated US \$500,000 to the University of California to conduct this "thorough and objective evaluation", to be applied not only to MTBE but also (inter alia) ethanol<sup>9</sup>. The Bill also provided at Section 3(d) that a draft of the assessment report would be submitted to the Governor of California for transmittal to the US Geological Survey and the Agency for Toxic Substances and Disease Registry at the Centers for Disease Control. There would then be a series of public hearings on the draft report and the comments of these two bodies.

11. Sections 3(e) and (f) of the California Bill provided as follows:

*"(e) Within 10 days from the date of the completion of the public hearings ... the Governor shall issue a written certification as to the human health and environmental risks of using MTBE in gasoline in this state. The certification shall be based solely upon the assessment and the report submitted pursuant to this section and any testimony presented at the public hearings. The certification shall state either of the following conclusions:*

*(1) That, on balance, there is no significant risk to human health or the environment of using MTBE in gasoline in this state.*

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ries (ii) and (iii). See e.g. Mr Dugan for Methanex, Transcript, Day 1, pp. 27-28.

<sup>8</sup> Nor is it covered by the waiver annexed to the Second Am. Claim.

<sup>9</sup> A sum that Methanex claims to be inadequate to fund properly the assigned work: see Second Am. Claim, para. 112.

(2) That, on balance, there is a significant risk to human health or the environment of using MTBE in gasoline in this state.

(f) If the Governor makes the certification described under paragraph (2) of subdivision (e), then, notwithstanding any other provision of law, the Governor shall take appropriate action to protect public health and the environment."

The Tribunal has supplied the underlined emphases in this legislative text, points considered later in this Award.

12. In addition, Section 4(a) provided:

*"(a) If the sale and use of gasoline is discontinued pursuant to subdivision (f) of Section 3 of this act, the state shall not thereafter adopt or implement any rule or regulation that permits or requires the use of MTBE in gasoline."*

13. Pursuant to the California Bill, the Report of the University of California (the "UC Report") was completed on 12th November 1998. It was accompanied by the public hearings and scientific peer review required under the California Bill. According to Methanex, the UC Report is one of a series of events leading up to the measures that Methanex challenges; and it is thus on any view highly relevant to Methanex's claims in these proceedings<sup>10</sup>. It is Methanex's case that the UC Report found that replacing MTBE with ethanol would not alleviate all the perceived problems with MTBE, and that it was crucial that ethanol or any other substitutes for MTBE be further evaluated before they were widely used as MTBE substitutes<sup>11</sup>. The UC Report is considered further below, in Part III of this Award.
14. **(ii) The 1999 California Executive Order:** This is now the first US measure impugned by Methanex. The California Executive Order signed by the Governor of California on 25th March 1999 recorded the Governor's certification that "on balance, there is significant risk to the environment from using MTBE in gasoline in California". (A copy of this California Executive Order is attached as Appendix 2 to this Award).
15. This certification was made by Governor Gray Davis pursuant to Section 3(e)(2) of the California Bill. As noted by the Tribunal, Governor Davis was obliged by law to make a timely certification under the Bill, within ten days from the completion of the public

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<sup>10</sup> Id., para. 21.

<sup>11</sup> Id., paras. 114-116.

hearings; and the only alternative for him under the law was either to make a certification of the significant risk to human health or that "on balance, there is no significant risk to human health or the environment of using MTBE in gasoline" in California, under Section 3(e)(1) of the California Bill. The Governor had no other discretion in making the statutorily required certification. Moreover, under the California Bill and as appears from the recital to the Executive Order, the Governor based his certification on the UC Report, its peer review by other agencies and experts, the public meetings and the ensuing findings and recommendations that: "while MTBE has provided California with clean air benefits, because of leaking underground fuel storage tanks MTBE poses an environmental threat to groundwater and drinking water ...".

16. The California Executive Order also provided (inter alia):

*"4. The California Energy Commission (CEC), in consultation with the California Air Resources Board, shall develop a timetable by July 1, 1999 for the removal of MTBE from gasoline at the earliest possible date, but not later than 31st December 2002." (Paragraph 4)*

*"10. The California Air Resources Board and the State Water Resources Control Board shall conduct an environmental fate and transport analysis of ethanol in air, surface water, and groundwater. The Office of Environmental Health Hazard Assessment shall prepare an analysis of the health risks of ethanol in gasoline..." (Paragraph 10)*

*"11. The California Energy Commission (CEC) shall evaluate by December 31, 1999 and report to the Governor and the Secretary for Environmental Protection the potential for development of a California waste-based or other biomass ethanol industry. CEC shall evaluate what steps, if any, would be appropriate to foster waste-based or other biomass ethanol development in California should ethanol be found to be an acceptable substitute for MTBE." (Paragraph 11)*

17. In addition, the California Executive Order required the California Air Resources Board to develop regulations that would require that gasoline containing MTBE be labelled prominently at the pump to enable consumers to make an informed choice on the type of gasoline they wished to purchase (Paragraph 7).

18. Methanex and methanol did not appear, expressly, in the California

Bill and California Executive Order.

19. **(iii) The California Regulations:** The California Phase III Reformulated Gasoline Regulations implemented the California Executive Order. They constitute the second US measure now impugned by Methanex. California Code of Regulations title 13 §§ 2273 required gasoline pumps containing MTBE to be labelled in California as follows: "Contains MTBE. The State of California has determined that use of this chemical presents a significant risk to the environment." In particular, §§ 2262.6 provided at sub-section (a)(1) that: "Starting December 31, 2002, no person shall sell, offer for sale, supply or offer for supply California gasoline which has been produced with the use of methyl tertiary-butyl ether (MTBE)".
20. Methanex alleges that these California Regulations went beyond merely banning MTBE: it claims that the California Regulations provided that only ethanol could be used as an oxygenate in California gasoline. Consequently, by September 2000, the California Regulations banned both MTBE, and (implicitly) methanol from competing with ethanol in the California oxygenate market, with intended legal effect from 31st December 2002<sup>12</sup>. (A copy of the Regulations is at Appendix 3 to this Award.)
21. These California Regulations do not refer, expressly, to methanol or Methanex.
22. **(iv) The Amended California Regulations:** Methanex also claims, as set out in its letter dated 13th June 2004, that the California Regulations as amended with effect from 1st May 2003 ("the Amended California Regulations of May 2003") expressly banned the use of methanol as an oxygenate in California.
23. As clarified in its closing oral argument at the main hearing in June 2004, Methanex relies on the amended measure not only as evidence of California's earlier intent to harm methanol producers (including foreign methanol producers, such as Methanex), but also as a new "measure" in its own right, albeit hitherto unpleaded as such by Methanex. Methanex sought, insofar as it was necessary, permission from the Tribunal to re-amend its claim in this respect. (The application to re-amend Methanex's Second Statement of Claim, and the Amended California Regulations of May 2003, are considered further below in Chapter II F of this Award).

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<sup>12</sup> *Id.*, para. 22. See further Part III below.

### 3) Methanex's Allegations as to the True Motives behind the US Measures

24. Methanex claims that California's stated concerns over MTBE resulted from the poor regulation of underground storage tanks for gasoline (USTs), which allowed not only MTBE but many other chemicals to escape into the environment via gasoline leaks. Nonetheless, California banned only MTBE. If, as California acknowledged, the true problem was leaking USTs, it was irrational for California to ban only one component of reformulated gasoline (MTBE) whilst allowing dangerous and potentially lethal components, such as benzene, to continue to contaminate California's groundwater<sup>13</sup>. Ethanol has also been detected in California's water supply<sup>14</sup>. According to Methanex, the cost of remedying the leaking USTs was far less than the projected cost of banning MTBE. The fact that California chose its irrational course of action demonstrates its intent to effectuate a discriminatory transfer of the oxygenate market from (a) methanol and MTBE producers to (b) ethanol producers<sup>15</sup>.
25. In brief, Methanex alleges that the US measures came into being because California intended rank protectionism of ethanol and concomitant punishment of methanol, methanol-based MTBE, and indeed Methanex. It claims that the facts, and the inferences that can reasonably be drawn from the facts, establish that California, in enacting the US measures, intended to create a local ethanol industry where no significant industry had previously existed in California; to benefit the US ethanol industry; to accomplish these goals by banning ethanol's competition, namely methanol and MTBE; and that California was motivated to protect ethanol in part by political and financial inducements (but not bribes) provided by the US ethanol industry; and in part because of nationalistic biases, both inherent and overt, to discriminate against and thereby harm Methanex as a Canadian entity and all other foreign methanol producers<sup>16</sup>.

### 4) Alleged Breaches of Articles 1102, 1105 and 1110 NAFTA

26. **Article 1102:** As to Article 1102 NAFTA, Methanex alleges that California and thereby the USA plainly intended to deny foreign

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<sup>13</sup> Id., paras. 89-90 and 191-201.

<sup>14</sup> Id., para. 105.

<sup>15</sup> Id., paras. 105-110.

<sup>16</sup> Id., paras. 141 and 143.

methanol producers, including Methanex, the best treatment it has accorded to domestic ethanol investors, thus violating Article 1102<sup>17</sup>.

27. **Article 1105:** As to Article 1105 NAFTA, Methanex alleges that the US measures were intended to discriminate against foreign investors and their investments, and intentional discrimination is by definition unfair and inequitable<sup>18</sup>.
28. **Article 1110:** As to Article 1110 NAFTA, Methanex alleges that a substantial portion of its investments, including its share of the California and larger US oxygenate market, were taken by patently discriminatory measures and handed over to the domestic ethanol industry. Methanex alleges that such a taking is at a minimum tantamount to expropriation under the plain language of Article 1110<sup>19</sup>.

### **5) Articles 1116 and 1117 NAFTA**

29. Methanex advances its claims under Article 1116 NAFTA "Claim by an Investor of a Party on Its Own Behalf". Methanex claims as an investor of a NAFTA Party (Canada) that another NAFTA Party (the USA) has breached obligations under Section A of Chapter 11 (Articles 1102, 1105 and 1110 NAFTA), and that Methanex has suffered grave damage as a result of those breaches, both directly and through its US investments<sup>20</sup>.
30. Methanex also advances its claims under Article 1117 NAFTA "Claim by an Investor of a Party on Behalf of an Enterprise". Methanex claims as an investor of a NAFTA Party (Canada), which indirectly owns and controls Methanex-US and Methanex-Fortier which are US enterprises, that another NAFTA Party (the USA) has breached obligations under Section A of Chapter 11 (Articles 1102, 1105 and 1110 NAFTA), and that Methanex-US and Methanex-Fortier have suffered grave damage as a result of those breaches<sup>21</sup>.

### **6) Methanex's Alleged Loss and Damage**

31. A summary of the damages claimed by Methanex is contained at paragraphs 321-327 of the Second Amended Statement of Claim.

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<sup>17</sup> Id., para. 296.

<sup>18</sup> Id., para. 313.

<sup>19</sup> Id., para. 317.

<sup>20</sup> Id., paras. 282-285 and 296.

<sup>21</sup> Id., paras. 286-290.

Methanex claims (inter alia) that the US measures have deprived and will continue to deprive Methanex and Methanex-US of a substantial portion of their customer base, goodwill and market for methanol in California. Methanex claims that California has essentially taken part of the US business of Methanex and Methanex-US and handed it directly to its competitor, the US ethanol industry. It also claims that the US measures have contributed to the continued idling of the Methanex-Fortier plant, and that the measures have reduced the return to Methanex, Methanex-US and Methanex-Fortier on capital investments, increased their cost in capital and reduced the value of their investments. It claims that the immediate damage to Methanex, its investments and its shareholders is evidenced by the direct and immediate drop in Methanex's market value following the issue of the California Executive Order, and that Methanex's share price and capitalization have never recovered from the damage inflicted by the US measures.

32. Methanex claims damages of approximately US\$ 970 million<sup>22</sup>. It also claims costs and interest. However, in its closing oral argument, and conscious of the fact that issues of quantum were not being decided at the June 2004 hearing, Methanex stated that its current damages calculation would almost certainly be different from the calculation originally made in 1999<sup>23</sup>. (Whilst the precise quantum of Methanex's claim is not an issue here decided in this Award, the Parties addressed the Tribunal at the main hearing on issues of causation).

## **7) The USA's Amended Statement of Defense**

33. The USA pursues the jurisdictional objection under Article 1101 NAFTA that was the principal decision in the Tribunal's Partial Award. The USA contends that Methanex has still not shown that the US measures "relate to" methanol producers or Methanex and that, accordingly, the Tribunal lacks jurisdiction pursuant to Article 1101 NAFTA. The USA submits that methanol is not interchangeable with MTBE and does not compete with ethanol in the market for oxygenates used in gasoline and that, contrary to Methanex's claims, there is no "binary choice" between methanol and ethanol. The USA also submits that the decision to ban MTBE was firmly grounded in the administrative record and the recommendations and findings of the UC Report.

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<sup>22</sup> Id., para. 327.

<sup>23</sup> Mr Dugan for Methanex, Transcript Day 8, p. 1998.

34. On the merits of Methanex's claim, the USA submits that there has been no breach of Articles 1102, 1105 or 1110 NAFTA and, independently, that Methanex has failed to establish to the applicable standard of causation (being "proximate causation") that the damages it alleges were caused by the US measures. The USA also submits that Methanex has in fact suffered no quantifiable loss at all. Finally, it claims that Methanex has failed to establish ownership of Methanex-US and Methanex-Fortier; and that for this reason also Methanex's claim should be dismissed by the Tribunal, with costs. In short, Methanex has not discharged any relevant part of the legal and evidential burden required to prove its pleaded claim against the USA.
35. As is apparent from the Partial Award and the Tribunal's order of 2nd June 2003, it remains appropriate for the Tribunal to decide together the USA's cases on jurisdiction and the merits under Article 21(4) of the UNCITRAL Rules.

## **PART II - CHAPTER E**

### **METHANEX'S PROCEDURAL REQUESTS FOR INTERPRETATION AND RECONSIDERATION OF THE PARTIAL AWARD**

#### **1) Introduction**

1. The Tribunal here considers: (i) Methanex's Request dated 28th August 2002 for Interpretation of the Partial Award of 7th August 2002; and (ii) Methanex's Request dated 28th January 2004 for Reconsideration of Chapters J and K of the Partial Award. Both Requests addressed the Tribunal's decisions in the Partial Award regarding the jurisdictional requirements of Article 1101 NAFTA (Chapters J and K of the Partial Award, at pages 53-71, concern the meaning of Article 1101(1) and its application in the present case).

#### **2) The Partial Award of 7th August 2002**

2. Although the full text of the Partial Award is attached as Appendix 5 to this Award, it is convenient at this stage to summarise both its broad effects and also the contentions of Methanex on "intent" that were then before the Tribunal. In brief, the effect of the Partial Award was to reject various objections to jurisdiction and admissibility made

by the USA<sup>1</sup>, but to leave for the Tribunal's further decision the USA's primary challenge to its jurisdiction under Article 1101(1) NAFTA. That challenge was to be addressed towards Methanex's subsequent "fresh" pleading in the form of the Second Statement of Claim, as permitted by the Tribunal.

3. In the Partial Award, the Tribunal decided that the phrase "relating to" in Article 1101(1) signifies something more than the mere effect of a measure on an investor or an investment and that it requires a legally significant connection between them<sup>2</sup>. It found that Methanex's claim, as pleaded in its Original Statement of Claim of 3rd December 1999, did not meet the essential requirement of alleging facts establishing a legally significant connection between the US measures, Methanex and its investments. The Tribunal accordingly decided that it had no jurisdiction to hear the claim as then pleaded by Methanex in its Original Statement of Claim<sup>3</sup>.
4. However, as already explained above, the Tribunal also decided that a part of Methanex's draft Amended Statement of Claim could potentially satisfy the jurisdictional requirements of Article 1101(1) NAFTA. This part of the claim concerned an allegedly malign intent, as pleaded by Methanex, behind the US measures to favour the US ethanol industry and the major US ethanol producer, ADM, and to harm "foreign" MTBE producers and "foreign" methanol producers, such as Methanex.
5. It is convenient to set out Methanex's relevant contentions on "intent" at the time, as recorded in the Partial Award:

*"Methanex contends, as characterised in its Reply Submission of 27th July 2001 (page 9), "that Gov. Davis intended to benefit the US ethanol industry and to penalise foreign producers of methanol and MTBE". ...*

*The relevant assumed facts, summarised in Chapter E above [of the First Partial Award], can be recalled briefly: ADM drives the US ethanol industry's political and lobbying*

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<sup>1</sup> Partial Award, paras. 172(1) and (7). The Partial Award also contains decisions on Methanex's application to amend its Statement of Claim and Methanex's request for documentary disclosure: see Chapters F and G of the Partial Award.

<sup>2</sup> In relevant part, Article 1101(1) provides that Chapter 11 of NAFTA "applies to measures adopted or maintained by a Party relating to: (a) investors of another Party; (b) investments of investors of another Party in the territory of the Party ...".

<sup>3</sup> Partial Award, paras. 129-147, 150 and 172(2).

*machine, ADM has launched a systematic attack on MTBE; ADM has characterised MTBE as a "foreign" product; ADM had a secret meeting with Governor Davis during his election campaign; this meeting concerned ethanol; ADM made substantial campaign contributions to Governor Davis; and after being elected, Governor Davis made the California Executive Order (leading to the California Regulations) banning MTBE, notwithstanding that MTBE is a safe product and other rational solutions exist for addressing California's drinking water problems. From these alleged facts, Methanex also invites the Tribunal to make a series of inferences:*

*(i) That, at the secret meeting, ADM stated that MTBE was a "foreign" product and that banning MTBE would be a patriotic step to reduce US dependence on fuels;*

*(ii) That in bringing about the US measures Governor Davis acted on what he was told by ADM;*

*(iii) That in bringing about the measures Governor Davis acted to favour ADM and the US ethanol industry; and*

*(iv) That Governor Davis also acted to disadvantage, relative to ADM and the US ethanol industry, the "foreign" producers of MTBE. ...*

*... Methanex also alleges that it supplies the majority of methanol in California; that California had no methanol industry of its own; and that as regards MTBE in California, it is essentially Methanex's methanol which provides the relevant "foreign" characteristic which allowed ADM to promote ethanol to Governor Davis to the disadvantage of MTBE. Whatever the position elsewhere in the USA, methanol and Methanex were "foreign" in California; and this, it is suggested, explains why anti-foreigner action could be taken against methanol in California which on its face would appear to hurt US producers of methanol. In short, it is contended, as regards Governor Davis, that his constituency was the State of California; a "foreign" product was a product foreign to California, which to him, as influenced by ADM, signified methanol produced by Methanex, a "foreign" product produced by "foreigners"; and his intent was to harm Methanex.<sup>4</sup>*

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<sup>4</sup> Id., paras. 151, 153, 157.

6. In the Partial Award, the Tribunal decided that the case presented by Methanex was not sufficiently clear to enable the Tribunal to determine whether or not Methanex's allegations based on "intent" were credible, and therefore whether or not one of the US measures could "relate to" Methanex or its investments for the jurisdictional purposes of Article 1101(1) NAFTA . Accordingly the Tribunal invited Methanex to re-plead its case in a fresh pleading and postponed its decision on the USA's jurisdictional objection with respect to Article 1101(1) NAFTA.
7. Given the importance of this order to the scope of the proceedings on the merits, the Tribunal sets out below the relevant paragraphs of the Operative Part of the Partial Award:

*"(2) Jurisdiction - Original Statement of Claim: As regards the USA's jurisdictional challenge under Article 1101(1) NAFTA, the Tribunal decides that Methanex's Original Statement of Claim fails to meet the requirements of that provision; and, as there pleaded, the Tribunal would have no jurisdiction to hear Methanex's claims;*

*(3) Jurisdiction - Amended Statement of Claim<sup>5</sup>: Subject to paragraph 4 below, as regards the USA's jurisdictional challenge under Article 1101(1) NAFTA, the Tribunal decides that Methanex's Amended Statement of Claim, as a whole, likewise fails to meet the requirements of that provision; and as there pleaded, the Tribunal would have no jurisdiction to hear Methanex's Amended Statement of Claim as a whole;*

*(4) As regards part of Methanex's Amended Statement of Claim (as subsequently supplemented by its written and oral submissions), the Tribunal decides that certain allegations relating to the "intent" underlying the US measures could potentially meet the requirements of Article 1101(1) NAFTA, thereby allowing part of Methanex's case to fall within the jurisdiction of the Tribunal.*

*It is impossible for the Tribunal now to make a ruling on jurisdiction in regard to this part of Methanex's case without a fresh pleading from Methanex accompanied by evidential*

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<sup>5</sup> This is a reference to the draft Amended Statement of Claim of 12th February 2001.

*materials, to be followed (subject to consultation with the Disputing Parties) by a pleading and evidential materials from the USA and an evidential hearing which may be limited to one or more threshold or determinative issues arising from Methanex's fresh pleading.*

*Accordingly, that jurisdictional ruling will be postponed by the Tribunal until one or more further awards pursuant to Articles 21(4) and 32(1) of the UNCITRAL Arbitration Rules;*

*(5) New Pleading: Within a period not more than ninety days from the date of this Award, Methanex shall submit a fresh pleading, complying with Articles 18 and 20 of the UNCITRAL Arbitration Rules and conforming to the decisions contained in this Award; and that pleading shall be accompanied by the evidential materials described in this Award.<sup>6</sup>*

At the time of the Partial Award, it was the Tribunal's understanding that Methanex's case, if pleaded in the "fresh" pleading, would advance broadly the same case on "intent" as had previously been advanced in its draft Amended Statement of Claim and as subsequently explained by Methanex to the Tribunal in its written and oral submissions.

8. In other words, it was not the Tribunal's Partial Award, or the Tribunal's interpretation of Article 1101(1) in the Partial Award, which led Methanex to advance its case based on California's malign intent. That was a case which Methanex had itself already advanced earlier in order (inter alia) to meet the USA's jurisdictional challenge under Article 1101 NAFTA. In particular, as explained later in this Award, it is not correct that the Tribunal, in its Partial Award, confined its interpretation of the relevant phrase - "relating to" - to cases of malign intent. There could be cases of a "legally significant connection" without such malign intent; but that was not Methanex's case at that time. Nor did Methanex then seek permission to amend its Statement of Claim to plead a new case based on grounds other than such an alleged malign intent by California; and the Tribunal's permission allowing Methanex to submit a "fresh pleading" did not extend to such a new case. Given Methanex's present criticisms of the Partial Award, it is therefore helpful to keep in mind what were and what were not

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<sup>6</sup> Partial Award, paras. 172(2)-(5). See also paras. 151-161, 169.

Methanex's submissions made to the Tribunal at the relevant time.

### **3) Methanex's First Request for Interpretation of the Partial Award**

9. On 28th August 2002, within three weeks of the Partial Award, Methanex timeously made a Request for Interpretation of the Partial Award under Article 35 of the UNCITRAL Rules. (Article 35(1) provides: "Within thirty days after receipt of the award, either party, with notice to the other party, may request that the arbitral tribunal give an interpretation of the award").
10. Methanex sought the interpretation and clarification of the Partial Award in respect of four matters: (i) the meaning of the requirement under Article 1101(1) NAFTA of a "legally significant connection" as decided by the Tribunal at paragraph 147 of the Partial Award; (ii) the contents and scope of the "fresh pleading" ordered by the Tribunal at paragraph 172(4) of the Partial Award; (iii) the requirements imposed by the Tribunal in regard to the evidence to be submitted by Methanex; and (iv) the nature and timetable for future proceedings.
11. The Tribunal invited written comments from the USA, which were made by letter of 23rd September 2002. The USA contended that the Partial Award was in no way ambiguous; and that Methanex was not in truth requesting any clarification of the Tribunal's decision, but rather a different decision which was not permitted by Article 35 of the UNCITRAL Rules.
12. The Tribunal responded by letter dated 25th September 2002. So far as concerns Methanex's Request for Interpretation<sup>7</sup>, the Tribunal considered that it did not fall within the scope of Article 35 of the UNCITRAL Rules; and it formally declined to respond to Methanex's Request. Nonetheless, the Tribunal chose to address certain of the points raised by Methanex. As the USA's jurisdictional objection with respect to Article 1101(1) NAFTA remains a significant issue to be decided in this Award, it is useful to set out below that part of the Tribunal's letter of 25th September 2002 that concerns the requirement under Article 1101(1) NAFTA of a "legally significant connection":

*"4. At paragraph 147 of the Partial Award (page 62), the*

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<sup>7</sup> With respect to certain "Further Matters" raised by Methanex, particularly Methanex's renewed request for an order compelling the USA to produce any potentially relevant parts of NAFTA's negotiating history, see below, at Chapter II H of this Award.

*Tribunal concluded that the phrase "relating to" in Article 1101(1) NAFTA signifies something more than the mere effect of a measure on an investor or an investment and that it requires a legally significant connection between them. In its Request, Methanex queries this conclusion, addressing Paragraph 138 of the Partial Award (page 58). There the Tribunal found that Methanex's interpretation of the phrase "relating to" as "affected" would produce a surprising, if not absurd, result given that the possible consequences of human conduct are infinite; and by analogy the Tribunal noted that in a traditional legal context, both in the USA and Canada under the laws of contract and civil wrong, a limit is imposed restricting the consequence for which conduct is to be held accountable. This paragraph forms only part of the Tribunal's reasons which, on this point, are set out in Chapter J of the Partial Award (pages 53 to 62).*

*5. Methanex seeks confirmation of its understanding that the Partial Award suggests that a NAFTA Party in breach of its Chapter 11 obligations will be liable only for those types of consequences that are actionable in analogous legal circumstances, such as where there is foreseeable, direct or intended injury, or competitive harm. Alternatively Methanex seeks an interpretation of the phrase "legally significant connection". It is said that without such an interpretation, Methanex is placed in the difficult and unfair position of marshalling evidence and arguments to meet an undefined standard. For two reasons, Methanex's several requests are unfounded.*

*6. First, at Paragraphs 172(2) and (3) of the Partial Award (page 73), the Tribunal decided that Methanex's Original Statement of Claim and its Amended Statement of Claim (as a whole) failed to meet the jurisdictional requirements of Article 1101(1) NAFTA. At paragraph 172(4), however, with respect to part of Methanex's Amended Statement of Claim (as subsequently supplemented by its written and oral submissions), the Tribunal decided that certain allegations relating to the "intent" underlying the US measures could potentially meet the requirements of Article 1101(1) NAFTA.*

*7. As appears from Chapter K of the Partial Award (pages*

63 to 71), the Tribunal postponed its ruling on jurisdiction in respect of that one part of Methanex's case and ordered a fresh pleading from Methanex because the Tribunal found it impossible to make such a ruling without such a fresh pleading, accompanied by evidential materials. It follows that the difficulties raised by Methanex are illusory. The Tribunal has already decided that insofar as it may have jurisdiction in respect of Methanex's claim, such jurisdiction can exist only in respect of that part of the claim alleging an "intent" underlying the US measures to benefit the US ethanol industry and to penalise foreign methanol producers, such as Methanex. Accordingly, in this case, Methanex's claim is not concerned with different factual circumstances (i.e. where that intent is absent).

8. Second, albeit related to this first reason, the interpretation of Article 1101(1) NAFTA in the Partial Award is to be read as a whole, as applied to this particular case. It serves no purpose for Methanex to isolate one particular paragraph in order to construct an ambiguity which does not in fact exist, or if it did, is irrelevant to the circumstances of this case. In our view, the legal requirements of Article 1101(1) are clear for this case, even though one Disputing Party might disagree with our interpretation and although there may be difficulties in defining for all cases the exact dividing line between a legally significant and insignificant connection: see Paragraph 139 of the Partial Award (page 59). Nonetheless, such difficulties do not exist in this case for the remaining part of Methanex's claim, based on "intent".

13. By letter of 30th September 2002, Methanex stated that the Tribunal's letter of 25th September 2002 had provided helpful clarification and guidance. Methanex then made no further requests for interpretation of the Partial Award or the Tribunal's letter dated 25th September 2002. Nor did Methanex exercise such legal options as existed to challenge to the Partial Award in a court of competent jurisdiction.

#### **4) Methanex's Second Request for Reconsideration of Chapters J and K of the Partial Award**

14. On 28th January 2004, almost 18 months after the date of the Partial Award (7th August 2002), Methanex submitted a second request to the Tribunal. This was a Request for Reconsideration of Chapters J

and K of the Partial Award. In this Request, Methanex submitted that a violation of national treatment did not require a finding of "intent" and that, in requiring a showing of "intent" in the relevant Chapters of the Partial Award, the Tribunal had failed to apply accepted principles of international law and had misconstrued Article 1101(1) NAFTA. Methanex further submitted that the creation of an additional "gatekeeper" restriction in Article 1101(1), that was more stringent than the express gatekeeper restrictions that already appeared in Article 1102 NAFTA and the remainder of Chapter 11, was inconsistent with international law and undermined NAFTA. Methanex requested a reconsideration and amendment of Chapters J and K of the Partial Award by the Tribunal to eliminate any "intent" requirement.

15. The timing and content of this Second Request was startling, particularly in the absence of any prior request to the Tribunal or any timely challenge to the Partial Award in a court of competent jurisdiction. Moreover, Methanex's comments on "intent" indicated a significant departure from the legal and factual basis on which Methanex's own application to amend its case had been made to the Tribunal for the purpose of the Partial Award. Methanex subsequently clarified its Second Request; and the Tribunal here addresses it as advanced by Methanex orally and in writing up to the end of the main hearing in June 2004.
16. In summary, Methanex submits that the Tribunal has the power to grant the Request for Reconsideration under Articles 15 and 22 of the UNCITRAL Rules; and it also submits that the resignation of one member of the Tribunal (Mr Warren Christopher) due to an appearance of partiality (as alleged by Methanex) warrants this Tribunal's reconsideration of the Partial Award. It will be recalled that Mr Christopher resigned voluntarily as a member of the Tribunal more than 16 months prior to Methanex's Second Request and that the Partial Award was made unanimously by all three arbitrators.
17. By letter of 20th February 2004, the Tribunal invited Methanex to clarify the procedural grounds on which its application was advanced. Methanex responded by letter of 8th March 2004. It contended that nothing in the UNCITRAL Rules precluded reconsideration of the Partial Award (including Article 22), whilst pursuant to Article 15(1) Methanex was to be afforded a full, which also meant a fair, opportunity to present its case.
18. Article 15 of the UNCITRAL Rules provides as follows:

*"Subject to these Rules, the arbitral tribunal may conduct the arbitration in such manner as it considers appropriate, provided that the parties are treated with equality and that at any stage in the proceedings each party is given a full opportunity of presenting its case."*

Article 22 of the UNCITRAL Rules provides:

*"The arbitral tribunal shall decide which further written statements, in addition to the statement of claim and the statement of defence, shall be required from the parties or may be presented by them and shall fix the periods of time for communicating such statements."*

19. Methanex contended that it had not been afforded a full and fair opportunity to present its case by the Tribunal: the requirements of Article 15 could not be considered met where one of the members of the Tribunal responsible for the Partial Award harboured an apparent conflict of interest that, shortly after the Partial Award was issued, caused him to resign from the Tribunal. Methanex contends that this creates an inescapable appearance of bias that only reconsideration of the Partial Award could erase. Methanex also maintained in its letter of 8th March 2004 that the reconsideration of the Partial Award would not cause any prejudice to the USA.
20. By letter of 16th March 2004, the Tribunal invited further written submissions from the Disputing Parties on this issue; and it is necessary to summarise them below.
21. **The USA's Response:** By letter of 30th March 2004, the USA submitted that the Tribunal had no authority to reconsider the Partial Award. It contended that Article 15 of the UNCITRAL Rules did not authorise reconsideration by the Tribunal. It submitted that Article 15 is to be read subject to Article 32(2) of the UNCITRAL Rules, which provides that the award "shall be final and binding on the parties"; and that the Partial Award is just such a final and binding award under Article 32(1) of the UNCITRAL Rules. Article 32(2) in this respect is said to reflect the general principle of *res judicata*. So far as concerns the resignation of Mr Christopher, the USA contended that the UNCITRAL Rules provided for no exception to Article 32(2) where an arbitrator withdrew after challenge and that, moreover, pursuant to Article 11(3) of the UNCITRAL Rules, withdrawal cannot imply the validity of a challenge. The USA also noted that the record established no basis whatsoever to question Mr Christopher's

impartiality or independence; and that it had been open to Methanex to challenge the Partial Award on grounds of actual bias within three months of the date of the Award; and, significantly, that Methanex had not made any such challenge to any court.

22. ***Methanex's Submissions:*** Methanex responded by letter of 14th April 2004. It submitted that it was not seeking the reversal of the Partial Award, but only a reconsideration of the interpretation of the legal standard that the Tribunal planned to apply as to the requirement of a "legally significant connection" under Article 1101(1) NAFTA. Methanex contended that its objection to the Tribunal's formulation of the "legally significant connection" standard had been raised in its Second Amended Statement of Claim (at paragraph 293); but that this pleading had not been addressed by the Tribunal or by the USA. Further, if the Request for Reconsideration did require reconsideration of the Partial Award itself, this reconsideration by the Tribunal was not precluded by Article 32(2) of the UNCITRAL Rules which concerned only final awards, not partial awards. The principle of *res judicata* had no application to a matter that was not finally decided because the proceedings were still underway before the Tribunal. Methanex submitted that the Tribunal should refer instead to the "law of the case" doctrine, which did not limit a court's power to reconsider earlier conclusions. So far as concerns the USA's contentions on the *lex loci arbitri*, Methanex submitted that US law required reconsideration in cases where an undisclosed relationship existed between an arbitrator and a party, and that the three months' time limit applied only in respect of applications to the US Federal Courts (and not to an arbitral tribunal) and in any event only applied to final awards. Methanex also submitted that the "specific intent to harm" standard had not been endorsed by the USA in its Amended Statement of Defense or correspondence; and that the USA should not be entitled to hold Methanex to an inappropriately high burden of proof while remaining free to argue before other NAFTA tribunals that this Tribunal had "got it wrong".
23. At the main hearing of June 2004, the USA developed its earlier written submissions in oral argument to the Tribunal. It contended that Methanex had recognised that the Partial Award was an award within Article 32(2) of the UNCITRAL Rules by making its first Request for Interpretation of 28th August 2002. That Request had been made pursuant to Article 35(1) of the UNCITRAL Rules, providing that a party may "request that the arbitral tribunal give an interpretation of the award"; and Methanex thereby recognised the existence of an "award". In addition to Article 32(1) of the UNCITRAL Rules, the USA also relied on the *travaux préparatoires* of the UNCITRAL Rules and the jurisprudence of the Iran-US Claims Tribunal to show that a partial award fell

within the rubric of "award" for the purposes of Article 32(2)<sup>8</sup>.

24. The USA also submitted that, by reference to Article 12 of the UNCITRAL Rules, it was not for the Tribunal to address a challenge made to one of its members and that, in any event, by his letter of 20th September 2002, Mr Christopher had expressly rebutted the factual allegations now repeated in Methanex's letter of 14th April 2004<sup>9</sup>. So far as concerned Methanex's submission that it had raised the objection to the Tribunal's formulation of the "legally significant connection" standard in its Second Amended Statement of Claim, the USA pointed out that in the very paragraph cited by Methanex, Methanex had expressly stated that it did *not* seek to re-litigate the Tribunal's decision on Article 1101 NAFTA. So far as concerned the alleged failure on the part of the USA to endorse the legal standard adopted by the Tribunal in respect of Article 1101(1), the USA had made clear in its Rejoinder that it considered that the Partial Award had correctly stated the law on Article 1101(1) NAFTA.
25. Methanex did not develop its written submissions orally at the main hearing in June 2004, save to respond to two questions put by the Tribunal. The first question addressed Methanex's apparent suggestion that Methanex had made a request to the Tribunal for reconsideration of the Partial Award in the Second Amended Statement of Claim (see above). Methanex then confirmed that there had been *no* such request to the Tribunal. The second question addressed timeliness. Methanex stated that the relevant date was the date of the second Request for Reconsideration, i.e. 28th January 2004. Methanex also confirmed that it had no further submissions that it wished to make in respect of the USA's submissions on timeliness<sup>10</sup>.

### **5) Mr Christopher's Response of 20th September 2002 to Methanex's Notice of Challenge**

<sup>8</sup> Referring to *Ford Aerospace & Comm. Corp. v. Air Force of Islamic Republic of Iran*, 6 Iran-US CTR, 104, 109; and van Hof, *Commentary on the UNCITRAL Arbitration Rules*, p. 218: "... Although the preliminary draft did not define the term "award", it was meant to include interim, interlocutory or partial awards, as well as final awards. After a suggestion at the Commission's deliberation, an explicit provision to this effect was included in this article, the present para. 1. The present para. 2 was included in the earlier draft as part of para. 1, which was later renumbered. The second sentence was only added after it was made a separate sentence."

<sup>9</sup> Methanex's letter of 14th April 2004 stated: "Mr. Christopher personally pitched a case to Governor Davis after this case had commenced, and Governor Davis personally decided, over the objection of his Attorney General, to award a lucrative representation to Mr. Christopher's firm". Mr Christopher stated in his Response of 20th September 2002: "I did not make a personal appeal to the Governor to obtain that representation for O'Melveny over the opposition of the Attorney and, indeed, I have never spoken to Governor Davis about the case". See further below.

<sup>10</sup> Mr Dugan for Methanex, Transcript Day 8, pp. 1818-1819.

26. Given Methanex's reliance on Mr Christopher's resignation as an arbitrator in these proceedings, it is necessary to set out below Mr Christopher's Response of 20th September 2002 to Methanex's Notice of Challenge of 28th August 2002:

*" ... I have received and reviewed the "Notice of Challenge" dated August 28, 2002, submitted by Messrs Dugan and Wilderotter of Jones, Day, Reavis & Pogue on behalf of Methanex Corporation ("Methanex") questioning my impartiality and independence in this matter and requesting that I either resign as arbitrator or be disqualified from continuing to act as such<sup>11</sup>. Methanex submits this challenge more than two years after the retention of O'Melveny & Myers LLP ("O'Melveny") in the Williams v State of California case, more than 20 months after Methanex filed its Amended Complaint based upon Governor Davis' alleged secret meeting with executives of ADM, and following the tribunal's Partial Award dated August 15, 2002. This is my response.*

*O'Melveny, the law firm of which I am senior partner, represents a broad range of clients in California, both public and private. In addition, I have served the State in various pro bono roles over the years, most recently as co-chairman of an advisory panel on hate crimes appointed by Governor Davis. As is shown by the attachments to the Notice of Challenge, Methanex and its counsel were aware of these circumstances at the time I was appointed to this arbitral tribunal. Methanex, through its prior counsel, expressed its satisfaction that these circumstances did not implicate my impartiality or independence with respect to the matters at issue here.*

*In the Notice of Challenge, however, new counsel for Methanex assert that they had recently learned of a representation undertaken by O'Melveny subsequent to my appointment that, in their view, raises an issue in that regard, namely, O'Melveny's representation of the State of California and certain of its officials (but not Governor Davis) in Williams v State of California, San Francisco Superior Court Case No 312235 (the "Williams Action"). The plaintiffs in the Williams Action complain of alleged shortcomings in the State's oversight of public education in California. There*

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<sup>11</sup> This is a reference to the new Counsel then acting for Methanex in place of its original Counsel at the time of Mr Christopher's appointment. (Subsequently, Paul Hastings, Janofsky & Walker LLP acted as Counsel for Methanex).

*is no relationship between the issues in controversy in that action and the matters in controversy here, and the Notice of Challenge does not suggest the contrary. Nevertheless, Methanex urges that O'Melveny's representation of California in the Williams Action calls into question my impartiality and independence because of what Methanex believes was my role in O'Melveny's obtaining that representation.*

*The press reports from which Methanex has drawn its view of my role in O'Melveny's retention in the Williams Action paint a distorted and inaccurate picture. Although I see no reason to undertake a point-by-point refutation of the hearsay and gossip contained in the newspaper clippings attached to the Notice of Challenge, it will be useful to set forth the facts as I recall them regarding my limited connection to the Williams Action.*

*My recollection is that in June 2000, during a discussion I had with a lawyer from the Governor's office on unrelated matters, we discussed the recent and well-publicized filing of the Williams Action. The lawyer from the Governor's office indicated a desire to retain an outside law firm to represent the State because the action was particularly complex and he anticipated that its defense would impose excessive demands upon the State's counsel. He was specifically interested in knowing if O'Melveny had attorneys with the requisite expertise in the matters that would be litigated in the Williams Action. I suggested that he speak with Fram Virgee, an O'Melveny partner whom I knew to have had extensive experience in matters involving public education.*

*I did not make a personal appeal to the governor to obtain that representation for O'Melveny over the opposition of the Attorney General, and indeed, I have never spoken to Governor Davis about the case. I understand that Mr Virgee made a written submission setting forth his ideas regarding the defense of the action, and detailing his expertise and that of other O'Melveny attorneys whom he proposed for the representation. I played no role in the preparation of that submission and was not one of the attorneys proposed for the representation of the State. I have never had my name on any pleadings in the case, and never charged any time on the Williams case file.*

*Based upon the foregoing facts, I believe there is no justifiable basis to question my independence or impartiality. However, to avoid the continuing distractions of this issue for the tribunal and the parties, I have concluded that I should withdraw as arbitrator, and I do so with the consent of the U.S.A., effective as of this date ..."*

Methanex has not sought to challenge the factual content of Mr Christopher's Response in an appropriate court or body and within prescribed time limits.

## **6) The Tribunal's Decision**

27. In the Tribunal's view, the first issue is whether, once a partial award is made by a tribunal<sup>12</sup>, it is final and binding within Article 32(2) of the UNCITRAL Rules and, if so, whether the tribunal has any jurisdiction to re-consider such an award at a later stage of the same arbitration proceedings. As explained below, the Tribunal decides that its Partial Award was an award which was final and binding upon the Disputing Parties; and that, as such, the Tribunal has no jurisdiction to reconsider the Partial Award in the form sought by Methanex in its Second Request made in January 2004, i.e. admittedly more than thirty days after Methanex's receipt of the Partial Award in August 2002.
28. The Tribunal does not accept Methanex's contention that, in seeking reconsideration by its Second Request, it is seeking something other than a reversal of a significant decision in the Partial Award, namely that "certain allegations relating to the 'intent' underlying the US measures could potentially meet the requirements of Article 1101(1) NAFTA, thereby allowing part of Methanex's case to fall within the jurisdiction of the Tribunal" but that otherwise the Tribunal lacked jurisdiction over Methanex's claim<sup>13</sup>. Methanex's Second Request seeks to reverse the core of the Partial Award.
29. The Tribunal's decision is not based on a mere technicality or semantic point under the UNCITRAL Rules. The application of these arbitration rules was triggered by Methanex's own choice in its 1999 Notice of Arbitration; and it should also be noted that, at the end

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<sup>12</sup> There is no dispute as to the jurisdiction of the Tribunal to make a partial, as opposed to a final, award. That jurisdiction is expressly established by Article 32(1) of the UNCITRAL Rules.

<sup>13</sup> Partial Award, para. 172(4); also paras. 172(2) and (6).

of the jurisdictional hearing in July 2001, the Tribunal expressly asked the Disputing Parties whether the award that the Tribunal was intending to make should have any particular form, bearing in mind that the award might be subjected to challenge in a court of competent jurisdiction<sup>14</sup>. It was then agreed by both Methanex and the USA that the award would be called a partial award (as, on any reading, it could not dispose of all matters potentially arising for decision by the Tribunal<sup>15</sup>) and that the partial award would be final and enforceable<sup>16</sup>. In the Tribunal's view, there was a common intention, expressly shared by Methanex at that time, that the partial award would be final and binding, within the meaning of Article 32 of the UNCITRAL Rules. It will be recalled that under Articles 32(1) and (2) of the UNCITRAL Rules, a "partial" award is expressly "final and binding on the parties".

30. Further, it appears to have been Methanex's position subsequent to the making of the Partial Award that this award was indeed "final and binding". In Methanex's first Request for Interpretation dated 28th August 2002, Methanex's "request that the arbitral tribunal give an interpretation of the award" was made pursuant to Article 35(1) of the UNCITRAL Rules. This request necessarily recognised the existence of an award that was final and binding on Methanex pursuant to Article 32(2) of the UNCITRAL Rules. Otherwise, Methanex could not have invoked Article 35 of the UNCITRAL Rules which applies only to an "award". (As expressed in its letter of 25th September 2002, the Tribunal considered that Methanex's Request did not fall within the scope of Article 35 of the Rules because the Tribunal considered that what Methanex sought was not an interpretation, i.e. not because the Tribunal had not made an "award" within Article 32(2) of the Rules).
31. The Tribunal also rejects, for present purposes, any distinction between a partial award and a final award which leaves the arbitration tribunal *functus officio*. A partial award is a final and binding award within Article 32(2) of the UNCITRAL Rules in regard to the matter it decides, although it does not leave the tribunal *functus officio*. It is presented as an award; and as an award it disposes finally of certain issues in the arbitration proceedings. No question here

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<sup>14</sup> Transcript of 12th July 2001, p. 364.

<sup>15</sup> Even if the Tribunal had upheld one or more of the USA's challenges, it would still have had to make a further award on costs as issues on costs had not been fully debated before the Tribunal.

<sup>16</sup> Transcript of 13th July 2001, pp. 541-542.

arises as to the distinction between a tribunal's decision, ruling or order and an award (whether partial or final), such as confronted the French Court in *Brasoil* (1999) or the US Court in *Publicis* (2000)<sup>17</sup>: Methanex's arguments rest only upon the difference between a "partial" award and a "final" award.

32. The Tribunal therefore rejects Methanex's contention that the Partial Award is not a final and binding award under Article 32(2) of the UNCITRAL Rules and the contention that Article 32(2) concerns only final awards, not partial awards. That contention runs counter to the ordinary meaning of the Articles 32(1) and (2) as a matter of the English language. In the Tribunal's view, no weight is to be placed on the fact that "award" is not further defined in Article 32(2) expressly to include (inter alia) a partial award. It follows that, where reference is made to an award under Article 32(2), that is intended to include a partial award made under Article 32(1) of the UNCITRAL Rules.
33. Turning to the issue under Article 15(1) of the UNCITRAL Rules, there is nothing there to suggest that an arbitration tribunal has a broad jurisdiction to reconsider a final and binding award that it has already made. (The possible exception for fraud by a party is here irrelevant). To the contrary, both the ordinary meaning and the context of Article 15(1) lead to the opposite conclusion. Article 15(1) is located in Section III of the Rules, "Arbitral Proceedings"; and it is a general provision that regulates the conduct of the arbitral proceedings. By contrast, Article 32 is to be found in Section IV, "The Award"; and it is concerned with the form and effect of an award. Article 15(1) cannot be read as creating such a huge derogation from Article 32; it has a significantly different subject-matter. Moreover, Article 15(1) requires that a party be given a full opportunity of presenting its case "*at any stage of the proceedings*". This accepts that arbitral proceedings may comprise differing stages, as also appears from Article 15(2), and a given stage in the proceedings may of course be brought to an end by a final and binding award. It would both undermine Article 32 and lead to an inequality between the parties if at any time the losing party could seek to re-litigate matters contained in an award simply by invoking Article 15(1) of the UNCITRAL Rules.
34. Turning next to the impact of Mr Christopher's resignation, the Tribunal notes that under the UNCITRAL Rules it has no role (unlike

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<sup>17</sup> *Braspetro Oil Services Co. v. Great Man-Made River Project* (1999) XXIVa ICCA YBCA 296; *Publicis Communications v. True North Communications Inc* 203 F.3d 725 (7th Cir. 2000); (2000) XXV ICCA YBCA 1152.

an ICSID tribunal) to decide upon any challenge by a party to any of the arbitrators. All decisions on challenges to members of this Tribunal are reserved to the appointing authority pursuant to Article 12(1) of the UNCITRAL Rules, in this case the Secretary-General of ICSID or his designated alternate. The Tribunal has therefore no jurisdiction to decide that an undisclosed relationship did or not exist between an arbitrator and a party, as Methanex has alleged. In the Tribunal's view, it likewise lacks any jurisdiction to decide Methanex's further contentions that US law requires reconsideration in such cases and that there is or is not a three month's time-limit under US law. Moreover, Mr Christopher's resignation was voluntary; and his resignation cannot be treated as an admission of Methanex's factual allegations. To the contrary, Article 11(3) of the UNCITRAL Rules expressly provides that resignation "does not imply acceptance of the validity of the grounds for the challenge".

35. In conclusion, for all these reasons, the Tribunal decides that Methanex's Second Request was procedurally inappropriate and in no sense made in a timely or efficient manner<sup>18</sup>; and it therefore rejects Methanex's Request dated 28th January 2004 for Reconsideration of Chapters J and K of the Partial Award.

## **PART II - CHAPTER F**

### **METHANEX'S APPLICATION TO AMEND ITS SECOND AMENDED STATEMENT OF CLAIM**

#### **1) Introduction**

1. In the course of its oral opening submissions at the main hearing in June 2004<sup>1</sup> and by subsequent letter of 13th June 2004 during that hearing, Methanex confirmed that it was now relying on § 2262.6(c) of the California Regulations as amended with effect from 1st May 2003, which amendment expressly prohibited the use of methanol as a "covered oxygenate" in California<sup>2</sup>. In its closing oral argument

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<sup>18</sup> If relevant, the Tribunal would have found that reconsideration of the Partial Award would have caused prejudice to the USA. There is little point in any arbitration tribunal making jurisdictional decisions intended and understood to be final and binding on the parties if, much later, a disappointed party can reargue its jurisdictional case and turn the arbitration into the equivalent of Sisyphus's torment or the film "Groundhog Day".

<sup>1</sup> Mr Dugan for Methanex, Transcript Day 1, pp. 120-123.

<sup>2</sup> A proposed draft regulation, substantively in the same form as was subsequently adopted on 1st May 2003, had been annexed to Methanex's Second Am. Claim and was referred to in that pleading, at para. 122.

at the main hearing, Methanex made clear that it was now relying on the amended § 2262.6(c) both as evidence of California's intent to harm methanol producers under the earlier measures, including the California Regulations in their earlier forms, and also as a new third additional US "measure" in its own right<sup>3</sup>.

2. Both in its letter of 13th June 2004 and in its closing oral argument, Methanex sought, insofar as it was necessary, permission from the Tribunal to amend its claim to enable it to rely on the amended § 2262.6(c). Methanex placed considerable weight on the new § 2262.6(c)(4), and the express reference there to methanol, for the purposes of satisfying the "relating to" requirement of Article 1101(1) NAFTA as interpreted and applied in the Partial Award. Methanex submitted that the Partial Award had emphasised the fact that the US measures did not on their face mention methanol; hence it had required a showing of an intent to harm methanol producers including Methanex; and it was now clear that the US measures did make express mention of methanol<sup>4</sup>.

## **2) The History of the Amended California Regulations of May 2003**

3. The genesis of the amendments to the California Regulations is historically complicated; and the Tribunal has largely taken the following chronology from Methanex's history and accompanying texts, submitted to the Tribunal (at its request) on 29th June 2004 after the main hearing. Given the Tribunal's decision on Methanex's application, the Tribunal has not thought it necessary to invite the USA's further comments on Methanex's chronology. This chronology begins with the amendments made in 2000.
4. **1999-2000:** On 9th December 1999, the California Air Resources Board ("CARB") conducted a hearing to discuss proposed changes to the California Regulations. After this and all subsequent hearings had been completed, the final regulation order was adopted on 16th June 2000<sup>5</sup>. On 26th June 2000, the changes were submitted to the Office of Administrative Law ("OAL"), the branch of the California Government that ensures compliance with statutory standards; OAL approved the changes on 2nd September 2000; and this proposed text was filed with the California Secretary of State also on 2nd September 2000<sup>6</sup>.

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<sup>3</sup> Mr Dugan for Methanex, Transcript Day 8, pp. 1787-1789.

<sup>4</sup> Mr Dugan for Methanex, Transcript Day 8, pp. 1810-1811.

<sup>5</sup> Exhibit 1 to Methanex's History and Amendments to California Phase Three Reformulated Gasoline (CaRFG3) (referred to below as Methanex's History).

<sup>6</sup> Methanex cited this text in its Amended Article 1119 Notice to the USA of 22nd December 2000 and its Request to Extend or Suspend the Current Jurisdictional Schedule also of 22nd December 2000.

5. Section 2262.6 specifically banned the use of MTBE (as cited above) and purported to ban the use of other oxygenates. In regard to the latter, the text also stated in Section 2262.6(c):

*"(c)Use of oxygenates other than ethanol or MTBE in California gasoline on or after December 31, 2002. Starting December 31, 2002, no person shall sell, offer for sale, supply or offer for supply California gasoline which has been produced with the use of any oxygenate other than ethanol or MTBE unless a multimedia evaluation of use of the ether [emphasis supplied] in California gasoline has been conducted and the California Environmental Policy Council established by Public Resources Code section 71017 has determined that such use will not cause a significant adverse impact on the public health or the environment."*<sup>7</sup>

The use of the term "ether" made it at least unclear whether methanol (which is an alcohol and not an ether) was covered by this text.

6. The position was partly clarified by CARB. In paragraph 6 of Attachment B to CARB Resolution 99-39, CARB proposed amending the language of Section 2262(c) so that the prohibition should apply to all "alcohols other than ethanol"<sup>8</sup>:

*"6. Expand the prohibition of ethers other than MTBE to include any oxygenate other than MTBE or ethanol unless a multimedia evaluation of use of the oxygenate in California gasoline has been conducted and the California Environmental Policy Council has determined that such use will not cause a significant adverse impact on the public health or the environment. The originally proposed regulatory language inadvertently failed to reflect staff's intent, expressed at page 23 of the Staff Report, that the prohibition apply to alcohols other than ethanol; and this should appropriately be extended to any other oxygenates such as esters. - Section Affected: Modifications to proposed section 2262.6(c)."*

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<sup>7</sup> Exhibit 1 to Methanex's History, p. 24.

<sup>8</sup> Cal. Air Resources Bd., Res. 99-39, 3rd December 1999, 16 JS Tab 24 to the USA's Am. Defense; Exhibit 2 to Methanex's History, p. 2.

As explained below, CARB eventually amended the regulations to use the term "oxygenate" throughout the proposed legislation, thus prohibiting methanol as an oxygenate in California gasoline. However, this did not happen immediately but, as recited below, it took two more years.

7. CARB again proposed amendments to the CaRFG3 regulations in 2000. These amendments did not include a change in the text of section 2262.6 (the section banning MTBE and other oxygenates). These amendments were later approved on 20th August 2001, becoming effective the same day.
8. **2001:** There were no changes to the California Regulations, other than those proposed in 2000 (as noted in the previous paragraph, which occurred in August 2001).
9. **2002:** CARB proposed amendments to the California Regulations again, intending to defer the prohibition on MTBE and other oxygenates from 31st December 2002 to 31st December 2003. The text was approved by CARB on 25th July 2002 and submitted to OAL on 8th November 2002. OAL approved the amendments for filing with the California Secretary of State on 24th December 2002; and these amendments became law on the same date. In this version of Section 2262.6(c)<sup>9</sup>, the term "ether" was replaced with the term "oxygenate," indicating that methanol, as an oxygenate, was covered by this regulation, albeit not expressly named.
10. At this point, Section 2262.6(c) (as amended) provided:

*"Use of oxygenates other than ethanol or MTBE in California gasoline on or after December 31, 2003. Starting December 31, 2003, no person shall sell, offer for sale, supply or offer for supply California gasoline which has been produced with the use of any oxygenate other than ethanol or MTBE unless a multimedia evaluation of use of the oxygenate in California gasoline has been conducted and the California Environmental Policy Council established by Public Resources Code section 71017 has determined that such use will not cause significant adverse impact on the public health or the environment."*

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<sup>9</sup> Cal. Air Resources Bd., Final regulation Order, Amendments to Postpone Imposition of the CaRFG3 Standards, 8th November 2002, 14 JS Tab 17 to the USA's Am. Defense (the new regulations being cited at para. 75, p. 28, of that pleading); and Exhibit 4 to Methanex's History, p. 13.

11. **2003:** On 20th March 2003, CARB adopted additional amendments to the California Regulations<sup>10</sup>. On 1st May 2003, OAL approved these amendments, and the Amended California Regulations became legally effective the same day. These amendments expressly named methanol, in Section 2262.6(c)(4), in the list of "Covered oxygenates"<sup>11</sup>.
12. Accordingly, the relevant parts of the Amended California Regulations of May 2003 now provided as follows:

*"Section 2262.6(c): Use of oxygenates other than ethanol or MTBE in California gasoline on or after December 31, 2003.*

*1. Starting December 31, 2003, no person shall sell, offer for sale, supply or offer for supply California gasoline which has been produced at a California production facility with the use of any oxygenate other than ethanol or MTBE unless a multi-media evaluation of use of the oxygenate in California gasoline has been conducted and the California Environmental Policy Council established by Public Resources Code section 71017 has determined that such use will not cause a significant adverse impact on the public health or the environment.*

*2. Starting December 31, 2003, no person shall sell, offer for sale, supply or offer for supply California gasoline which contains a total of more than 0.10 weight percent oxygen collectively from all of the oxygenates identified in section (c)(4).*

*3. Starting July 1, 2004, no person shall sell, offer for sale, supply or offer for supply California gasoline which contains a total of more than 0.06 weight percent oxygen collectively from all of the oxygenates identified in section (c)(4).*

*4. Covered oxygenates. Oxygen from the following oxygenates is covered by the prohibitions in section 2262.6(c)(1), (2) and (3):*

*Methanol  
Isopropanol  
n-Propanol*

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<sup>10</sup> Exhibit 5 to Methanex's History, p. 5; see also Cal. Air Resources Bd., Proposed Regulation Order, Amendments to the California Phase 3 Gasoline Regulation to Refine the Prohibitions of MTBE. In November 2002, these proposed amended regulations had not been brought into force.

<sup>11</sup> Exhibit 6 to Methanex's History, p. 2.

*n-Butanol*  
*iso-Butanol*  
*sec-Butanol*  
*tert-Butanol*  
*Tert-pentanol (tert-amylalcohol)*  
*Ethyltert-butylether (ETBE)*  
*Diisopropylether (DIPE)*  
*Tert-amylmethylether (TAME) ..."*

13. Although, as appears from above, the earlier forms of the California Regulations did not expressly refer to methanol, Methanex has contended that, implicitly, methanol was always covered by the California Regulations. Accordingly, Methanex submits that the "relating to" requirement of Article 1101(1) NAFTA is satisfied in this case.

### **3) The Grounds for Methanex's Application**

14. Methanex contends that its application for permission to amend its pleadings should be allowed by the Tribunal on both procedural and substantive grounds. As to procedure, Methanex relied on Article 20 of the UNCITRAL Rules as establishing the Tribunal's power to allow an amendment. It provides:

*"During the course of the arbitral proceedings either party may amend or supplement his claim or defence unless the arbitral tribunal considers it inappropriate to allow such amendment having regard to the delay in making it or prejudice to the other party or any other circumstances. However, a claim may not be amended in such a manner that the amended claim falls outside the scope of the arbitration clause or the separate arbitration agreement."*

As regards discretion, Methanex maintained that the amendment would cause no prejudice to the USA.

15. Moreover, as noted above, Methanex contended that all the new regulation did was to make explicit what had been implicit in the previous version of § 2262.6(c), i.e. the ban of all oxygenates other than ethanol (including methanol), and that it had relied on § 2262.6(c) as a measure from the date of its draft Amended Statement of Claim dated 12th February 2001. For that same reason, and also because this amendment of May 2003 post-dated the Partial Award of August

2002, Methanex maintained that the amendment would not be caught by paragraphs 162 and 172 (4) and (5) of the Partial Award, which provided that Methanex's fresh claim should not exceed the limits of Methanex's existing case as then pleaded<sup>12</sup>. Methanex also contended that if the amendment were not allowed, and if it were unsuccessful in its claim before this Tribunal, it would be open to it simply to file a new NAFTA claim against the USA by reference to the new § 2262.6(c) as a "measure" not considered by the Tribunal in these arbitration proceedings.

#### **4) The USA's Response**

16. The USA contended that Methanex was seeking impermissibly and belatedly to introduce a new claim that fell outside the scope of the Partial Award, which in any event could not give rise to any possible damages recoverable by Methanex. Methanex had expressly conceded that the prohibition of methanol pursuant to the new § 2262.6(c) had not impacted methanol producers, including Methanex. The USA also contended that § 2262.6(c) of May 2003 did not effect an absolute prohibition of methanol, but merely a conditional prohibition for so long as there had been no multimedia evaluation of its use in California gasoline and a determination that such use would not cause a significant adverse impact on public health or the environment; and it thus failed as a "measure" both as a matter of jurisdiction and the merits.
17. As to the first of these contentions, the USA maintained that § 2262.6(c) had not been pleaded as a measure in the draft Amended Statement of Claim of 12th February 2001, and that it had been unclear from the Second Amended Statement of Claim to what extent Methanex had been seeking to rely on § 2262.6(c). That lack of clarity had been removed in subsequent pleadings, including Methanex's Reply where it was unambiguously stated that Methanex was not introducing a new claim and that the prohibition was being relied on solely as evidence of an intent to discriminate against methanol producers<sup>13</sup>. It followed that Methanex was seeking to amend its claim at far too late a stage of the proceedings.
18. In addition, the formal requirements of Articles 1119 and 1121 NAFTA had not been met by Methanex. For this reason, and also because the proposed amendment went beyond what was ordered by

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<sup>12</sup> Mr Dugan for Methanex, Transcript Day 8, pp. 1790-1792, 1811.

<sup>13</sup> See Methanex's Reply, paras. 30 and 246.

the Partial Award, the Tribunal lacked jurisdiction under Article 20 of the UNCITRAL Rules to allow the amendment. It was also unfair, inefficient, costly and prejudicial for the USA to have to respond to Methanex's ever-shifting assertions of its case. Finally, the USA submitted that it was undisputed that the conditional prohibition of methanol had no effect at all on methanol producers, including Methanex, as methanol had not been used as an oxygenate in California (or the USA). It followed that there could be no claim of loss or damage under Articles 1116 or 1117 and that Methanex's contention that it could simply bring a new claim if the amendment were not allowed was an idle threat<sup>14</sup>.

### 5) The Tribunal's Decision

19. The Tribunal decides that, insofar as Methanex is relying on the amended § 2262.6(c) as *evidence* of California's intent to harm methanol producers, Methanex should be allowed to amend its Second Amended Statement of Claim to that limited effect. This allegation is not a radical development from its existing case; the point is implicitly made in Methanex's existing pleadings, albeit not expressly; and there is no sufficient prejudice to the USA which could make this argument unfair. The Tribunal also decides that Methanex need not formally amend its Second Amended Statement of Claim to advance this argument.
20. However, for the reasons which follow, insofar as Methanex is relying on the amended § 2262.6(c) as an *additional* "measure" under Article 1101 NAFTA, the Tribunal decides that Methanex cannot advance the proposed amendment to its case in these arbitration proceedings.
21. Methanex has never previously pleaded the amended § 2262.6(c) as an additional measure under Article 1101 NAFTA. Accordingly, any such plea would clearly require an amendment to its Second Amended Statement of Claim; and such an amendment would also require the permission of the Tribunal. Pursuant to Article 20 of the UNCITRAL Rules, a claim may not be amended in such a manner that the amended claim falls outside the scope of the arbitration clause,

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<sup>14</sup> Mr Legum for the USA, Transcript Day 9, pp. 2030-2046. The USA had also contended that, as explained in a Statement of Reasons issued by the California Air Resources Board, the 11 compounds were listed in § 2262.6(c)(4) because they comprised all the compounds listed in the test method for the presence of oxygenates in gasoline as set out by the American Society of Testing and Materials. The USA maintained that its contentions in this regard had not been challenged by Methanex (Am. Defense, fn. 267 at p. 60, Transcript Day 2, pp. 326-327).

in this case, Section B of Chapter 11. In seeking to introduce a new claim relying on amended § 2262.6(c) as a measure for the purposes of Article 1101(1) NAFTA, in the Tribunal's view, Methanex fails to meet the essential requirements for bringing a claim under Section B of Chapter 11 and Article 20 of the UNCITRAL Rules.

22. First, as Methanex accepted at the main hearing<sup>15</sup>, no waiver for the purposes of Article 1121 NAFTA had been provided by Methanex in respect of the amended claim under NAFTA. Article 1121(1) provides in pertinent part:

*"A disputing investor may submit a claim under Article 1116 to arbitration only if:*

*(a) the investor consents to arbitration in accordance with the procedures set out in this Agreement; and*

*(b) the investor and, ... the enterprise waive their rights to initiate or continue before any administrative tribunals or court under the law of any Party, or other dispute settlement procedures, any proceedings with respect to the measure of the disputing Party that is alleged to be a breach referred to in Article 1116 ..." [emphasis added].*

Similar language is contained at Article 1121(2) with respect to claims brought under Article 1117.

23. Pursuant to Article 1121(1), Methanex appended to its Notice of Arbitration a Consent to Arbitration and Waiver dated 2nd December 1999. The USA disputed the validity of this waiver. Methanex submitted a new waiver document on 25th May 2001 and, as already noted elsewhere, the Disputing Parties resolved the issue concerning the waiver by agreement (see the Partial Award, paragraph 13). This agreement was recorded by joint letter to the Tribunal dated 13th July 2001, the material terms of which provide:

*"The parties have agreed to the following resolution of the United States' preliminary objection based on the adequacy of the waivers submitted by Claimant Methanex Corporation pursuant to NAFTA Article 1121:*

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<sup>15</sup> Mr Dugan for Methanex, Transcript Day 8, p. 1797.

1. *Although it continues to maintain that the other waivers submitted by Methanex do not comply with the article's requirements, Respondent United States of America agrees that the waivers submitted by Methanex on May 25, 2001 satisfy the requirements of Article 1121;*

2. *Although it continues to maintain that the waivers it previously submitted complied with the article's requirements, Methanex does not now claim in this proceeding that California Senate Bill 521 is a measure that violates the NAFTA;*

3. *The parties agree that waivers complying with the requirements of Article 1121 must be submitted as provided in Article 1137, in order for a claim under Chapter Eleven of NAFTA to be considered submitted to arbitration and jointly request that the Tribunal note this agreement in its decision on the United States' preliminary objections;*

4. *In consideration of the foregoing, the United States hereby withdraws its objection to the Tribunal's jurisdiction based on the adequacy of the waivers provided by Methanex pursuant to Article 1121" [emphasis added].*

24. The waiver document submitted by Methanex on 25th May 2001 was attached as Exhibit F to Methanex's Second Amended Statement of Claim. The waiver provides, in pertinent part, that:

*"pursuant to Articles 1120 and 1121 of the North American Free Trade Agreement (NAFTA) and the UNCITRAL Arbitration Rules, Claimant/Investor Methanex Corporation hereby:*

*(a) waives its rights ... with respect to any measure that Claimant/Investor alleges to be a breach of NAFTA referred to in Articles 1116 and 1117."*

25. Identical waivers by Methanex-US and Methanex-Fortier were contained in the same document. Although these waivers are expressed in broad terms, they were made in May 2001 using the present tense. In the Tribunal's view, these waivers could not legitimately be construed to cover a possible future claim in respect of future

regulations still to be introduced by California in May 2003. To construe these past waivers otherwise, as Methanex contends, would introduce a large degree of uncertainty where absolute certainty, as to what the investor claimant was or was not waiving, is procedurally essential for both the investor and the NAFTA Respondent Party.

26. Second, even if an amendment were to be allowed subject to Methanex now making satisfactory waivers under Article 1121, the requirements of Article 1116 and/or 1117 could not be met with respect to its new claim based on the amended § 2262.6(c) as a separate "measure". An essential component of each of these two provisions is a claim that the investor/enterprise has incurred loss or damage by reason of or arising out of the breach of an obligation under Chapter 11 NAFTA. The Tribunal construes Articles 1116 and 1117 as requiring a claim of loss or damage that originates in the measure adopted or maintained by the NAFTA Party.
27. Methanex makes no such claim in respect of the amended § 2262.6(c). Methanex cannot, and does not, contend that it has suffered any loss as a result of a breach of one of the substantive provisions of Chapter 11 by virtue of the introduction of this amended § 2262.6(c). Methanex has never supplied methanol to the California market for use as an oxygenate in reformulated gasoline; and methanol could not, at any time relevant to these proceedings, lawfully be used as an oxygenate in reformulated gasoline, whether in California or elsewhere in the United States. Thus, the express prohibition of the use of methanol in May 2003 (pending a multimedia evaluation and positive determination by the California Environmental Policy Council or otherwise) cannot possibly lead to any loss or damage for Methanex or any enterprise of Methanex. This much is readily admitted by Methanex<sup>16</sup>. It follows that this amended claim, if the amendment were allowed by the Tribunal, is hopeless and bound to fail on its merits. On this ground alone, the Tribunal would exercise its discretion against Methanex under Article 20 of the UNCITRAL Rules.
28. Third, the Tribunal notes that Methanex's claim invoking the amended § 2262.6(c) as a measure was made very late, after the conclusion of the first week of the main hearing in June 2004 and more than a year after the amendment was promulgated in California. Not only was this period of delay unexplained by Methanex; but the applica-

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<sup>16</sup> Id., p. 1811: " ... *I may be beating a dead horse... . You [the Tribunal] asked what is the subsequent effect of this latest change for a methanol producer? There is none ...*".

tion came after many of the USA's witnesses had been cross-examined orally by Methanex at the main hearing, including Mr Simeroth who testified generally as to the California Regulations. Further, that claim ran counter to Methanex's Reply of February 2004, which had confirmed that no new claim was being introduced by Methanex and that the amended § 2262.6(c) was simply being deployed as evidence of California's intent to discriminate against methanol producers. In all these circumstances, there is a real risk of material prejudice to the USA; and on this ground also the Tribunal exercises its discretion against Methanex under Article 20 of the UNCITRAL Rules.

29. In conclusion, for all these reasons, (i) the Tribunal rejects Methanex's application to amend its Second Amended Statement of Claim to plead the amended § 2262.6(c) of the California Regulations of May 2003 as a third measure under Article 1101 NAFTA; but (ii), as indicated above, the Tribunal nonetheless allows Methanex to adduce this amended regulation as evidence in support of its case against the two measures already pleaded by Methanex (namely: the 1999 California Executive Order and the earlier 2000 California Regulations), there being no like impediments or unfairness to the USA in this regard.

## **PART II - CHAPTER G METHANEX'S REQUEST FOR ADDITIONAL EVIDENCE FROM THIRD PERSONS**

### **1) Introduction**

1. On 4th October 2002, Methanex served its "First Request for Additional Evidence". The relevant evidence, listed in an Annex to the Request, consisted of two types: (i) witness testimony of certain specified individuals and generic persons likely to have personal knowledge or information relating to issues before the Tribunal, and (ii) documents in the possession of (a) California or certain of its officials, (b) ADM, (c) Regent International and (d) certain other individuals, all in the USA. Methanex submitted that the evidence sought was relevant and material to the dispute; and that it was necessary to the full and fair presentation of Methanex's case to the Tribunal. Methanex's Request was made by reference to (i) the IBA Rules and (ii) 28 U.S.C. § 1782.
2. **(i) The IBA Rules:** So far as concerns obtaining documentary and witness evidence under the IBA Rules, Methanex relied on Articles 3.8 and 4.10 of the IBA Rules (see above, Annex 2 to Chapter II B of this Award). It is to be noted that it is a precondition to an application for Documents under Article 3.8 of the IBA Rules that "the Party cannot

obtain the documents on its own", that it is for the requesting party to identify the documents sought "in sufficient detail", and that the power of the arbitral tribunal is to "take the necessary steps if in its discretion it determines that the documents would be relevant and material". Similar requirements are contained in Article 4.10 of the IBA Rules in relation to Witnesses of Fact.

3. **(ii) § 1782:** Methanex also relied on 28 U.S.C. § 1782. It provides:

*"The district court of the district in which a person resides or is found may order him to give his testimony or statement or to produce a document or other thing for use in a proceeding in a foreign or international tribunal ... The order may be made pursuant to a letter rogatory issued, or request made, by a foreign or international tribunal or upon the application of an interested person and may direct that testimony or statement be given, or the document or other thing produced, before a person appointed by the court."*

This legislation allows Methanex (as "an interested person") to apply to one or more relevant US District Courts in the USA for an order, subject to the Court's jurisdiction and the exercise of its judicial discretion, directing a third person to give testimony or to produce documentation for use in a proceeding before a "foreign or international tribunal".

4. The difficulties over the interpretation of 28 U.S.C. § 1782 have long been well-known to legal scholars and practitioners in the field of transnational arbitration<sup>1</sup>. It appears that an international commercial arbitration tribunal with its seat outside the USA is not an "international tribunal" within the meaning of the statute, still less such an arbitration tribunal sitting in the USA; and whether this Tribunal falls to one or other side of the line is perhaps a difficult question. The wording of this legislation does not require that an application by an interested person (such as Methanex in the instant case) have the approval of a tribunal. Nonetheless, whilst Methanex maintained that its application to the US District Court(s) would not need any supportive order from the Tribunal, it nonetheless wished to avoid any

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<sup>1</sup> See e.g. Hans Smit, "Assistance Rendered by the United States in Proceedings before International Tribunals" (1962) 62 *Colum. L Rev.* 1264; and "International Litigation Under the United States Code" (1965) 65 *Col L Rev.* 1015. More recently, see Hans Smit "The Supreme Court Rules on the Proper Interpretation of Section 1782: Its Potential Significance for International Arbitration" (2003) 14 *Am Rev. Int. Arb.* 295.

dispute as to whether it was first required to obtain such an order by obtaining the same from this Tribunal<sup>2</sup>.

5. Methanex's submission that it needed no supportive order was, in the Tribunal's view, supported by the wording of the legislation. Further, following the main hearing, it appears to be justified by the judgment of the US Supreme Court of 21st June 2004 in *Intel Corp. v. Advanced Micro Devices, Inc*<sup>3</sup>. The Supreme Court there decided (inter alia) that an application may be made at any time by an interested person, including a time when there is no tribunal to give its consent to the application; and that a US District Court has jurisdiction to make an order even where the tribunal opposed the application. This case was not cited by Methanex or the USA at the main hearing (understandably); and the Tribunal takes note of the judgment without here relying upon it for the Tribunal's decision.
6. In its letters of 21st October and 12th November 2002, the Tribunal indicated that it was minded to address Methanex's Request upon receipt and study of Methanex's fresh pleading and evidential materials (served respectively on 5th November 2002 and 31st January 2003) and after consulting with the Disputing Parties. By letter of 17th January 2003, the Tribunal stated that it would be appropriate to deal with the Request at the forthcoming procedural meeting, later fixed for 31st March 2003. It also noted: "... that, procedurally, Methanex could make any application to the relevant US district court(s) under 28 U.S.C. § 1782 without awaiting that Spring Meeting (or indeed any fresh pleading or other materials from the USA)".
7. By letter of 23rd January 2003, the USA requested that the Tribunal correct this statement. The USA submitted that, pursuant to Articles 3.8 and 4.10 of the IBA Rules, Methanex had to await a decision of the

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<sup>2</sup> See footnote 1, at p. 3 of Methanex's First Request for Additional Evidence: "Although courts have held that it may not be necessary for a litigant to obtain the permission of the Tribunal before seeking an order in [a] district court ... Methanex wishes to avoid any dispute as to whether it was first required to obtain a Tribunal order."

<sup>3</sup> *Intel Corp v Advanced Micro Devices*, 542 U.S. 241 (2004), holding that US District Courts have a discretion under 28 U.S.C. § 1782(a) to order discovery to a private party for use in an anti-trust investigation by the EU Commission to which that party had filed a complaint. The EU Commission was treated as a "foreign tribunal"; and the Supreme Court rejected the Commission's argument (as amicus) that such an order should only be made at the request of the Commission and not at the behest of a private complainant only.

Tribunal before making any application. It also maintained that, while the issue had not been extensively litigated, recourse under 28 U.S.C. § 1782 was only permissible where a tribunal had first decided that the request or evidence was appropriate. By letter of 30th January 2003, Methanex took issue with both these points. Methanex's position was expressly that it could act without resort to the Tribunal. It submitted that the IBA Rules recognise that each party is entitled to gather evidence "on its own", adding: "... Methanex can indeed acquire the documents on its own under § 1782 without resorting to the Tribunal for assistance. While the Tribunal's aid would be welcome, such aid is not required unless and until Methanex fails in its efforts to obtain the evidence itself".

8. The Tribunal did not accede to the USA's request that the Tribunal "correct" its statement in its letter of 17th January 2003. The Tribunal remained minded to accept Methanex's position on this point, whilst recognising that it was not a point which the Tribunal itself had any power to determine. Methanex expressly referred to this fact in its letter of 17th March 2003: "... the USA argued [in its letter of 23rd January 2003] that Methanex must await a decision by the Tribunal before taking any affirmative steps with United States domestic courts, and it requested that the Tribunal rescind its acknowledgement of Methanex's procedural rights. The Tribunal has not done so nor does Methanex believe it would be appropriate to do so."
9. Also in its letter of 17th March 2003, Methanex provided for the Tribunal's information a draft application for evidence that it wished to file with the District Court for the Central District of California. Methanex stated that it had limited its first proposed request to testimony and documents from Mr Richard Vind and Regent International on the grounds that both were heavily involved in lobbying efforts in California and both would undoubtedly have probative evidence bearing on the issue of California's malign "intent". Methanex concluded its letter by requesting that the Tribunal resolve the issue at the procedural meeting on 31st March 2003, continuing "or, if it has no objection, we are prepared to file the application immediately". Significantly, Methanex did not then disclose to the Tribunal (or the USA) that Methanex had already procured much of this original documentation from Mr Vind and Regent International without their knowledge or consent in 1997-1998 and 2000-2001. This fact only

became apparent to the Tribunal at the main hearing in June 2004, as considered below in Chapter II I of this Award.

10. By letter of 20th March 2003, the Tribunal noted that the immediate decision required of it was "whether to authorise in any way Methanex's intended filing of the draft application to the District Court for the Central District of California" before the procedural meeting on 31st March 2003. The Tribunal stated that it would prefer not to make any decision prior to hearing the Disputing Parties further at the procedural meeting later that same month. In the absence of any objection stated by the Tribunal, Methanex remained at liberty to make its application to this and any other US District Courts as the Tribunal had earlier stated.
11. On 26th March 2003, in its Response to the USA's Supplemental Statement of Defense on Intent, Methanex referred to Articles 3 to 5 of the IBA Rules, stating that these provisions not only permitted a party to obtain relevant evidence, but also required the Tribunal to take steps to ensure that the party has the opportunity of doing so. This submission re-stated its application of 4th October 2002, based upon Articles 3.8 and 4.10 of the IBA Rules.

## **2) The Procedural Meeting of 31st March 2003**

12. The Disputing Parties made detailed submissions on Methanex's Request at the procedural meeting of 31st March 2003<sup>4</sup>. Methanex submitted that it would be very unusual for a party not to be allowed to use available court procedures that it needed in order to prove its case and that, in terms of time-tabling, the court proceedings in relation to 28 U.S.C. § 1782 could be completed in three to four months, with a full hearing on jurisdiction and the merits still possible in January 2004<sup>5</sup>. Methanex contended that use of the 28 U.S.C. § 1782 process was the most expeditious and comprehensive means of obtaining the evidence<sup>6</sup>. As to the subject-matter of the application under 28 U.S.C. § 1782, Methanex stated that this would be documents and individual witnesses from the Government of California, Mr Vind and possibly some other (then unspecified) individuals. However, no draft applications were supplied by Methanex detailing

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<sup>4</sup> Representations were made by Mr Dugan on behalf of Methanex, and by Mr Clodfelter, Mr Legum and Ms Menaker on behalf of the USA (submissions in respect of 28 U.S.C. § 1782 on behalf of the USA were made principally by Mr Legum).

<sup>5</sup> Transcript of 31st March 2003, pp. 28 and 33.

<sup>6</sup> *Id.*, p. 36-38.

the scope of the requested discovery from California or the specific type of documentation required of Mr Vind and his company<sup>7</sup>. The Tribunal confirmed that it would like to see such drafts; but these were not forthcoming from Methanex<sup>8</sup>.

13. The USA maintained that Methanex's application was "both a waste of time and a fool's errand" because Methanex already had access to the bulk of the documents that it sought, while two of the persons identified by Methanex had voluntarily agreed to appear as factual witnesses for the USA (Mr Vind and Mr Listenberger). Mr Vind had also indicated to the USA that he would voluntarily produce "any documents that he has concerning the August 4th, 1998 meeting"<sup>9</sup>. The USA submitted that for Methanex to resort to court proceedings under these circumstances would be inappropriate. As for Methanex's requests directed at California, the USA submitted that as one of the most transparent governments in the world, the documentation responsive to Methanex's request was available publicly on the internet. The USA also contended that there was a basic question as to whether 28 U.S.C. § 1782 applied at all to an international arbitral tribunal<sup>10</sup>, and that Methanex's time estimates for the 28 U.S.C. § 1782 process were in any event far too short. It also submitted that Methanex had engaged in "gamesmanship" and had reversed its position so far as the application of the IBA Rules was concerned<sup>11</sup>.
14. In response, Methanex stated that it was not looking for public record evidence, and that it had examined the public record very carefully<sup>12</sup>. The documents offered by the USA in respect of Mr Vind were said to be inadequate; and it was anyway necessary that Mr Vind be under a legal compulsion to provide documents<sup>13</sup>. The date of this observation is significant: by this time (i.e. March 2003), Methanex had already

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<sup>7</sup> Id., pp. 34, 42 and 98.

<sup>8</sup> Id., p. 43.

<sup>9</sup> Id., pp. 57-58.

<sup>10</sup> Similarly, that there were also issues as to whether the USA could be a person subject to discovery under 28 U.S.C. § 1782 and as to whether the relief sought would violate the Eleventh Amendment. Transcript of 31st March 2003, pp. 62-64.

<sup>11</sup> Id., pp. 65-67. In this respect, cf. Methanex's 4th October 2002 Request and its letter of 30th January 2003.

<sup>12</sup> Transcript of 31st March 2003, p. 95. Its position was that the evidence from the public record was nonetheless sufficient to sustain a judgment that California had acted with the intent of protecting ethanol producers and disadvantaging their competitors.

<sup>13</sup> Id., pp. 96-102.

acquired surreptitiously a mass of original documentation from Mr Vind and his company (Regent International) in 1997-1998 and in 2000-2001, and it was also certain that any Court application by Methanex would be contested by Mr Vind and also by the USA (which was calling Mr Vind as a factual witness). The Court's reaction to the disclosure of such surreptitious acquisition can perhaps be imagined. At the time, however, such acquisition was not disclosed by Methanex to the Tribunal, as described below.

15. Methanex also took issue with the USA's various points on the application of 28 U.S.C. § 1782 and, with respect to the IBA Rules, stated that its position had always been that it did not believe that the Tribunal's blessing was necessary in order to invoke 28 U.S.C. § 1782<sup>14</sup>. Counsel for Methanex stated: "In the best of all possible worlds, we would prefer a Tribunal order, but if the Tribunal, for whatever reason, is unwilling to issue it, we believe that under the statute we are entitled to go to the District Court as an interested party and seek to convince the District Court to grant us this additional evidence. In other words, while we would welcome a Tribunal order, we don't believe it is necessary for us to succeed at the District Court level, and I don't believe that position has changed."
16. In reply, the USA submitted that it had heard for the first time that Methanex was not looking for documents on the public record, and that it had also learnt that Methanex had not decided what documents it wished to receive from Mr Vind, Regent International or ADM. It was therefore exceedingly difficult to arrive at any kind of decision as to whether the requirements of the IBA Rules were met<sup>15</sup>.
17. At the conclusion of the procedural meeting of 31st March 2003, as regards 28 U.S.C. § 1782, the Tribunal was not minded to grant to Methanex the consent it sought for its proposed applications to the US District Courts. The Tribunal was concerned at the timeliness of Methanex's applications and their effect on the timing of these arbitration proceedings<sup>16</sup>. It also took into account the expressed intentions of the USA to adduce written and oral testimony from Mr Vind, Regent International and ADM; and it indicated that it would keep the matter under active consideration<sup>17</sup>. From Methanex's submis-

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<sup>14</sup> *Id.*, pp. 108-109.

<sup>15</sup> *Id.*, p. 127.

<sup>16</sup> The dates in *Intel Corp v Advanced Micro Devices*, 542 U.S. 241 (2004) are instructive; the dates of the three judgments are: (i) 7th January 2002: District Court for the Northern District of California; (ii) 6th June 2002: Court of Appeals for the Ninth Circuit; and (iii) 21st June 2004: US Supreme Court.

<sup>17</sup> Transcript of 31st March 2003, pp. 154-155.

sions at this procedural meeting, the Tribunal did not understand that Methanex was pursuing its request under the IBA Rules; but if it had, that application would have been dismissed by the Tribunal for Methanex's non-compliance with Articles 3.8 and 4.10 of the IBA Rules.

18. In December 2003, after the procedural meeting in March 2003, the USA with its Amended Statement of Defense adduced three witness statements from individuals attending the dinner of 4th August 1998 (and related events): Mr Vind, Mr Weinstein and Mr Listenberger of ADM. Each of these witness statements recorded the maker's willingness to appear for cross-examination at the main hearing. Subject to fulfilling those promises, it was by then clear to the Tribunal, if not also to Methanex, that an account of the meeting over dinner with Mr Davis would be available to the Tribunal at the main hearing in June 2004, to be subject to cross-examination by Counsel for Methanex.

### **3) Methanex's Re-submission of its Request for Additional Evidence**

19. By letter of 28th January 2004, Methanex re-submitted "its long-standing request that the Tribunal permit Methanex to gather additional evidence in the United States without delay". It contended that the Tribunal had delayed Methanex's exercise of its procedural rights to conduct fact finding under 28 U.S.C. § 1782 and that the Tribunal had still to decide the issue. Methanex again referred to Articles 3.8 and 4.10 of the IBA Rules, and requested a decision under the IBA Rules. It also cited the recent decision of the US Supreme Court in *McConnell v. Federal Election Commission* (10th December 2003)<sup>18</sup>. Methanex contended that this case supported its claims that the evidence sought was material and relevant. The case was put forward as authority that there was a close alignment of interests between large political contributions and actual or apparent indebtedness on the part of federal officeholders in the United States, whereas Methanex had argued in its pleadings that a similar alignment of interests was the moving force behind California's MTBE ban. Methanex concluded its letter by stating that US law allowed and encouraged the type of evidence gathering sought; and that the IBA Rules required the Tribunal to commence the process.

20. By letter of 12th February 2004, the USA contended that Methanex's

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<sup>18</sup> 540 U.S. 93, 124 S. Ct. 619 (2003).

Request for Additional Evidence had already been rejected by the Tribunal. By letter of 20th February 2004, the Tribunal asked Methanex to clarify the scope of its application by drafting the specific terms of the order now sought from the Tribunal. It had not previously done so. Methanex provided such a draft order on 8th March 2004. In the accompanying letter, Methanex stated that the Tribunal had not rejected its Request for Additional Evidence, having stated at the procedural meeting of 31st March 2003 that it was going to deliberate further on the matter.

21. By letter of 16th March 2004 to the Disputing Parties, the Tribunal decided as follows:

*"The Tribunal has considered Mr Dugan's letter dated 8th March 2004, enclosing the 'proposed order' to be made by the Tribunal. This draft order has clarified one point in that it had appeared from Mr Dugan's letter of 28th January 2004 (at p. 7) that Methanex was seeking an order for 'additional evidence from the United States'. This is now clearly not the case; but it is appropriate to raise three further matters:*

*(1) Methanex's position, as understood by the Tribunal, has been that an order from the Tribunal is not necessary to any application made by Methanex to a court of competent jurisdiction under 28 USC § 1782 directed at third persons (e.g. see transcript for 31.03.2003, pp. 108-109). In these circumstances, it remains unclear to the Tribunal why it is necessary for the Tribunal to make any order in the form sought by Methanex. Whilst the Tribunal does not encourage (nor discourage) an application under 28 USC § 1782, it remains open to Methanex to make any application as, when and where it sees fit, as indicated by the Tribunal (inter alia) in its letter of 17th January 2003 to the Disputing Parties.*

*(2) Insofar as Methanex is seeking an order from the Tribunal pursuant to Articles 3.8 and 4.10 of the IBA Rules of Evidence, it remains unclear to the Tribunal that Methanex has yet satisfied all the conditions necessary for the application of these provisions. In particular, Methanex did not at the procedural meeting of 31st March 2003 establish that it could not obtain relevant documentation on its own and/or that relevant witnesses would not appear voluntarily before the Tribunal. The position appears not to be materially different today. Indeed,*

*the Tribunal notes that (i) it was informed by Mr Legum's letter dated 22nd September 2003 that Methanex has obtained several thousands of pages of documentation pursuant to the California Public Records Act since March 2003, and (ii) with its Amended Statement of Defense dated 5th December 2003 the USA has adduced witness statements from certain of the relevant factual witnesses identified by Methanex in March 2003. From their witness statements, these witnesses appear to speak directly to the events of 4th August 1998 on which (inter alia) Methanex has relied; and, given that these witnesses are to be called by the USA at the hearing next June (if requested by Methanex or the Tribunal), it will of course be possible for Methanex to cross-examine them on their written testimony.*

*(3) The Tribunal does not here rule out granting an application under Articles 3.8 and/or 4.10 of the IBA Rules at or even after the June hearing. By then, it may transpire that there are indeed relevant and material gaps in the evidence before the Tribunal, in particular, for example, if certain of the USA's named witnesses relating to the events of 4th August 1998 were to decline voluntarily to attend the June hearing for cross-examination. At this stage, however, this is mere supposition; and it cannot now provide the basis of a decision by the Tribunal in the form currently requested by Methanex."*

Again, the overall position had not changed for Methanex: whilst the Tribunal had not blessed Methanex's applications under 28 U.S.C. § 1782, it had not opposed such applications (even assuming, as a legal matter, that such a hypothetical opposition would have had any effect on Methanex's rights under the Statute); Methanex remained at liberty to make any such applications at any time; and Methanex had not met to the Tribunal's satisfaction the requirements under Articles 3.8 and 4.10 of the IBA Rules. Methanex did not respond to the Tribunal's observations before making its applications under 28 U.S.C. § 1782, as next described.

#### **4) Methanex's Applications to the District Courts in California and its Withdrawal of Such Applications**

22. By letter of 7th April 2004, Methanex advised the Tribunal that it had filed applications pursuant to 28 U.S.C. § 1782 before the US District Courts in California (a copy of the applications, which were dated 2nd April 2004, was provided to the ICSID Secretariat). The evidence sought in the applications was very broad, including all documents evidencing, concerning or relating to California's decision to allow the

use of ethanol, and all documents evidencing, concerning or relating to the relationship between the former Governor Davis and the ethanol industry. In its letter to the Tribunal, Methanex stated that it would be almost impossible to obtain the evidence before the main hearing in June 2004. Methanex also stated that it was disappointed with the timing and content of the Tribunal's decision on obtaining additional evidence.

23. On 20th April 2004, the members of the Tribunal, the Administrative Secretary of the Tribunal, and the USA were served with notice of orders made by the District Courts of the Central and Eastern Districts of California providing the date for filing any opposition to Methanex's applications under 28 U.S.C. § 1782. The USA filed objections to Methanex's applications; and, on 12th and 14th May 2004, Methanex then served Notices of Withdrawal in respect of all its applications. In each Notice, Methanex's reasons for the withdrawal were given as follows:

*"Methanex filed the Application to obtain relevant evidence prior to the hearing on the merits in the underlying arbitration. The hearing is set to commence on June 7, 2004, and the Tribunal only recently suggested that Methanex proceed with the Application. (See Letter from V.V. Veeder, President of the Methanex Tribunal, dated March 16, 2004, attached as Exhibit 1 to Methanex's Application for Assistance.) Given the objection filed by the United States of America, it is clear that Methanex will be unable to schedule the necessary depositions and obtain the relevant additional evidence prior to the hearing. Accordingly, Methanex withdraws the Application without prejudice, and reserves the right to refile at a later date."*

It is apparent from the procedural chronology from October 2002 onwards, as set out above, that Methanex's reasons in the Notice of Withdrawal mis-stated the Tribunal's position.

## **5) Further Submissions at the Main Hearing**

24. In its closing oral submissions at the main hearing in June 2004, Methanex contended that, subsequent to the procedural hearing of 31st March 2003, it had not been clear that Methanex was free to go forward with its application under 28 U.S.C. § 1782. The USA had objected to Methanex's contention that it was open to Methanex

to make its application without the blessing of the Tribunal, and that issue had not been decided by the Tribunal, as Methanex had wished<sup>19</sup>. Further, Methanex contended that it would have been premature for a US court to take any position with respect to an application under 28 U.S.C. § 1782 until the Tribunal had issued a decision on the USA's objection, which the Tribunal had indicated that it would be doing shortly. According to Methanex, this explained Methanex's failure to pursue its application before April 2004<sup>20</sup>. Methanex did not develop any submissions on the requirements of Articles 3.8 and 4.10 of the IBA Rules or seek to respond to the USA's arguments in this respect<sup>21</sup>.

## 6) The Tribunal's Decision

25. At the June 2004 hearing, Methanex did not pursue an application to the Tribunal under Articles 3.8 and/or 4.10 of the IBA Rules for the Tribunal to take such legally available steps to obtain documents and/or testimony on the basis that there were relevant and material gaps in the evidence before the Tribunal. That possibility was open to Methanex, as the Tribunal had made express in its letter of 16th March 2004. Instead, Methanex invited the Tribunal only to draw adverse inferences on the basis that the USA had blocked discovery of documents and the giving of testimony<sup>22</sup>. That invitation is considered elsewhere in this Award and rejected by the Tribunal on the facts of this case. For present purposes, it follows from Methanex's decision not to make any further application in respect of its Request for Additional Evidence that there is no cause for any further decision by the Tribunal under Articles 3.8 and 4.10 of the IBA Rules.
26. As regards 28 U.S.C. § 1782, the Tribunal does not consider that its position requires any change. As the Tribunal made known to Methanex repeatedly, Methanex was at all times free to make any application to any US District Court. While recognising that a tribunal's consent is not required for an application under § 1782, this Tribunal did and does not wish to consent to Methanex's application. In any event, the fate of an application under § 1782 falls to be decided by the relevant US court and not by an international tribunal, as Methanex accepted at the procedural meeting of 31st March 2003<sup>23</sup>. The Tribunal cannot itself grant any order under § 1782,

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<sup>19</sup> Mr Dugan for Methanex, Transcript Day 8, pp. 1846-1848, 1850-1851.

<sup>20</sup> *Id.*, p. 1851.

<sup>21</sup> This was not withstanding a specific request from the Tribunal, Transcript Day 8, p. 1846.

<sup>22</sup> Mr Dugan for Methanex, Transcript Day 8, p. 1841.

<sup>23</sup> Transcript of 31st March 2003, p. 40.

even it were minded to so. In any event, having now heard the testimony of Messrs Vind, Weinstein and Listenberger and considered de bene esse the "Vind Documents" procured by Methanex in the context of all the evidence adduced in these arbitration proceedings, the Tribunal does not consider that any useful purpose could possibly be served by Methanex's application.

27. In all these circumstances, the Tribunal dismisses Methanex's Request for Additional Evidence from Third Persons.

## **PART II - CHAPTER H METHANEX'S REQUEST FOR DOCUMENTARY DISCLOSURE BY THE USA: THE "TRAVAUX" FOR ARTICLES 1101, 1102, 1105 AND 2101 NAFTA**

### **1) Introduction**

1. By letter of 10th May 2004, Methanex requested that the Tribunal respond to its request to obtain relevant evidence from the USA with respect to the NAFTA negotiating history, stating that the request was made "almost three years ago". Methanex stated that the evidence would shed significant light on the intent of the NAFTA Parties "in particular regarding the interpretation of Articles 1101, 1102 and 2101". Methanex then set out a list (said to be non-exhaustive) of the reasons why the evidence would be both relevant and material to issues before the Tribunal - by reference to a series of questions on the intentions of the NAFTA Parties with respect to Articles 1101, 1102 and 2101 NAFTA. In its closing oral argument at the June 2004 hearing, Methanex stated that it was now also seeking the negotiating history for Article 1105 NAFTA<sup>1</sup>.
2. On 16th July 2004, the FTC announced the public release of the negotiating history of Chapter 11, i.e. the draft negotiating texts produced between 1991 and 1993 by the NAFTA investment negotiating group, made up of representatives from each NAFTA Party<sup>2</sup>. The release of

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<sup>1</sup> Mr Dugan for Methanex, Transcript Day 8, pp. 1826-1827, 1831.

<sup>2</sup> The FTC's statement of 16th July 2004 noted: "*We are committed to transparency in trade negotiations. The negotiating texts of the NAFTA are documents of historical value and we recognize the level of public interest in them. We asked our officials to compile the NAFTA negotiating texts, bearing in mind the time necessary to complete this. We began the process with Chapter 11 and are pleased to announce that Chapter 11 texts will be available through our websites*". The negotiating history is available at [http://www.dfait-maeci.gc.ca/tna-nac/dispatch/trilateral\\_neg-en.asp](http://www.dfait-maeci.gc.ca/tna-nac/dispatch/trilateral_neg-en.asp).

these documents, insofar as they overlap with the documents sought by Methanex, came too late to be of assistance to Methanex at the main hearing; and it has since made no application to the Tribunal in regard to the release of these documents. Such release does not affect the Tribunal's consideration of Methanex's application here at issue.

3. The nature and timing of Methanex's application requires the Tribunal to set out at length the procedural history of Methanex's several applications made earlier in these arbitration proceedings. It would be a misunderstanding to treat these different applications as one single request made, in Methanex's phrase, "almost three years ago". The Tribunal also notes that, pursuant to Article 3.6 of the IBA Rules, the power to order the production of documents only arises where: "the Arbitral Tribunal determines that (i) the issues that the requesting Party wishes to prove are relevant and material to the outcome of the case, and (ii) none of the reasons for objection set forth in Article 9.2 apply". The reasons for objection contained at Article 9.2 include "(a) lack of sufficient relevance or materiality". (The full text of Article 3 of the IBA Rules is set out above, in Annex 2 to Chapter II B of this Award).

## **2) Methanex's Earlier Applications in Respect of the Negotiating History of NAFTA**

4. By letter of 24th September 2001, Methanex made (inter alia) the following request for documentary disclosure: "Methanex believes that all relevant evidence bearing on the intent of Article 1105 should be before this Tribunal. Accordingly, Methanex requests that the Tribunal direct the United States to produce the following as soon as possible: ... 1. All documents in the possession of the United States relating to the negotiating history of Chapter Eleven of NAFTA". This request was, on its face, predicated on the existence of a dispute between Methanex and the USA as to the interpretation of Article 1105 NAFTA; and in support of the request Methanex contended that the USA had put the "historical context" of Article 1105 directly at issue before the Tribunal.
5. At paragraph 80 of the Partial Award, the Tribunal decided: "In the light of the decisions made in this Award, we do not think it necessary here to make any order on Methanex's application for documentary production ... expanded by Methanex's letter of 24th September 2001. Such documentation was not relevant to the decisions in this Award;

and if relevant to the future conduct of these arbitration proceedings, a like application can be renewed by Methanex against the USA". There was then no renewed application by Methanex in relation to Article 1105 NAFTA.

6. Instead, as already noted, on 28th August 2002, Methanex made a Request for Interpretation of the First Partial Award, and also raised certain Further Matters. One of the "Further Matters" was a "renewal" (sic) of Methanex's request for an order compelling the USA to produce any potentially relevant parts of NAFTA's negotiating history, made exclusively by reference to the meaning of Article 1101 NAFTA. In its closing oral argument at the June 2004 hearing, Methanex confirmed that prior to August 2002, it had made no request for the negotiating history concerning Article 1101 NAFTA<sup>3</sup>.
7. By letter of 25th September 2002, the Tribunal invited Methanex to clarify two matters, namely: (i) whether it was correct to describe the current application as a re-submission of the earlier application given that the requests were apparently different, and (ii) the relevance of the documents requested given the Tribunal's decisions in the First Partial Award on the meaning of Article 1101. The Tribunal also stated that it was not minded to decide the application before a procedural meeting with the Disputing Parties.
8. Methanex responded by letter of 30th September 2002. It contended that its earlier letter of 24th September 2001 contained a request for the entirety of the negotiating history of NAFTA Chapter 11; and that this request was being renewed. As to relevance, it stated as follows: "As set forth in our August 28 letter, the Tribunal determined that the Article 1101 term "relating to" requires a "legally significant connection" and in this case requires a showing of appropriate discriminatory intent. The negotiating history of NAFTA Chapter 11 is very likely to shed relevant light upon the issue of discriminatory intent, since this is a key NAFTA principle".
9. For reasons not disclosed in these arbitration proceedings, Methanex decided not to pursue its application at the procedural meeting of 31st March 2003, as was expressly confirmed by Methanex in its closing oral argument at the main hearing in June 2004<sup>4</sup>. As described

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<sup>3</sup> Mr Dugan for Methanex, Transcript Day 8, pp. 1825, 1829.

<sup>4</sup> *Id.*, p. 1830: "as to what should have been raised in 2003, Methanex, in retrospect, probably should have raised it, but it was a matter of in litigation you pick and choose where you make your requests and where you fight your fights. And Methanex decided not to."

above, this procedural meeting was fixed by order of 12th February 2003 with a view to defining the nature and timing of the next stages of these arbitration proceedings. In accordance with that order, on 26th March 2003 Methanex submitted its written submissions on such procedural issues. It there made no mention of any application in respect of NAFTA's negotiating history. There the matter rested at and after the meeting of 31st March 2003; or so it appeared at the time to the Tribunal. More than twelve months later, by its letter of 7th April 2004, Methanex complained that the Tribunal had yet to issue an order with respect to its request; and, by further letter of 10th May 2004, it requested that the Tribunal respond to its request to obtain relevant evidence from the USA with respect to the NAFTA negotiating history in the terms already noted above.

### **3) The USA's Response**

10. By letter of 3rd June 2004, the USA responded to the effect that Methanex's application was untimely and had failed to establish the materiality of the documentation sought. It therefore submitted that the application should be rejected. With respect to timeliness, the USA contended that the application in respect of the negotiating history for Articles 1102 and 2101 was being made for the first time on 10th May 2004. The application in respect of Article 1101 was not in conformity with the Partial Award; it had not been pursued at the procedural hearing on 31st March 2003; nor had it been demonstrated that the negotiating history of Article 1101 was relevant subsequent to the making of the Partial Award. The USA submitted that the request of 10th May 2004 was correctly viewed as a new request by Methanex, made on the eve of the main hearing that had been fixed for almost one year; and it was to be rejected by the Tribunal on these grounds alone.
11. As to materiality, the USA maintained that the documents sought were of questionable use due to their fragmentary nature, resulting from the absence of any verbatim transcript or agreed minute of the NAFTA parties' negotiations, combined with the speed at which the negotiations for NAFTA took place; and that Methanex had failed to demonstrate that the documents would be relevant for the purpose sought in these proceedings. In this last respect, the USA maintained that the requirements of Article 32 of the Vienna Convention on the

Law of Treaties had not even arguably been met by Methanex: there had been no showing that the requested documents would not confirm the ordinary meanings of the NAFTA provisions; nor had there been an attempt to show that interpreting these provisions according to their ordinary meaning would leave the meaning ambiguous or obscure or lead to a result which was manifestly absurd or unreasonable.

#### **4) The Disputing Parties' Submissions at the Main Hearing of June 2004**

12. In its closing oral submissions at the main hearing, Methanex submitted that the negotiating history of NAFTA had been produced by the USA in other NAFTA cases; and it reiterated its submissions that the history would shed light on the various issues of interpretation at issue in these arbitration proceedings. The USA's failure to provide the negotiating history should lead the Tribunal to draw adverse inferences against the USA<sup>5</sup>. Methanex was asked by the Tribunal to develop its argument on the need for travaux by reference to the Vienna Convention on the Law of Treaties, and its attention was also drawn to the order of 28th May 2004 in the NAFTA arbitration: *Canfor Corporation v. USA*<sup>6</sup>.
13. In the course of its further submissions at the main hearing, Methanex stated that it was seeking the negotiating history in respect of Articles 1101, 1102, 1105 and 2101 NAFTA. The request in respect of Article 1105 was being added by way of an amendment to its existing application<sup>7</sup>. As already noted, Methanex confirmed that prior to the Partial Award there had been no request for the negotiating history concerning Article 1101 NAFTA, and that the request made in August 2002 had not been pursued at the March 2003 procedural meeting for Methanex's own reasons<sup>8</sup>. Methanex also accepted that the time for making a request in respect of Article 1101 was before the Partial Award<sup>9</sup>. As to materiality, Methanex submitted that the negotiating history for Article 1101 NAFTA would very likely shed light on the meaning of "relating to", and that the negotiating history for Article 1105 NAFTA could well shed light on that term too<sup>10</sup>.

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<sup>5</sup> Id., Transcript Day 8, p. 1821.

<sup>6</sup> Transcript Day 8, p. 1822; *Canfor Corporation v. The USA*, Procedural Order No. 5 of 28th May 2004 (This Canfor order is available on the internet: see [www.naftalaw.org](http://www.naftalaw.org)).

<sup>7</sup> Mr Dugan for Methanex, Transcript Day 8, p. 1831.

<sup>8</sup> Id., Transcript Day 8, pp. 1829-1830.

<sup>9</sup> Id., Transcript Day 8, p. 1825.

<sup>10</sup> Id., Transcript Day 8, p. 1826.

Methanex stated that it was hard to believe that some expression of the potential scope of the "fair and equitable treatment" was not raised during the course of the negotiation (for Article 1105); and it suggested that the negotiating history might show that the FTC's Interpretation of 31st July 2001 had substantively reduced the scope of Article 1105<sup>11</sup>. No oral submissions were developed by Methanex at the main hearing in respect of Articles 1102 and 2101.

14. So far as concerned the *Canfor* order, Methanex explained that it had been relying on this as authority for saying that the USA had formerly agreed to disclose the negotiating history of NAFTA, although it accepted that this was perhaps overstating the position<sup>12</sup>. Methanex also explained in response to a question from the Tribunal that, in seeking the negotiating history, Methanex was seeking the discovery that the USA would be liable to produce in a US court. This would include letters between the Parties, negotiating texts, minutes of meetings, and memoranda prepared for the negotiations; but it would extend to memoranda not shared between the NAFTA Parties<sup>13</sup>. In other words, Methanex was seeking from this Tribunal an order for productions cast in terms much broader than the order made by the *Canfor* tribunal.
15. The USA did not develop its submissions orally at the main hearing, stating that it was content to rely on its submissions as contained in its letter of 3rd June 2004.

## 5) The Tribunal's Decision

16. For two principal reasons, as explained below, the Tribunal rejects Methanex's application for disclosure by the USA of the negotiating history of Articles 1101, 1102, 1105 and 2101 NAFTA. First, the application was not made in a timely manner by Methanex; and second, it was not shown to the Tribunal's satisfaction that recourse to supplementary means was appropriate pursuant to Article 32 of the Vienna Convention and therefore meeting the requirements of Articles 3.6 and 9.2(a) of the IBA Rules.
17. *(i) Unreasonable Delay:* As appears from the history of Methanex's application, the only relevant application before May 2004 was made in respect of the negotiating history of Article 1101 NAFTA. However,

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<sup>11</sup> Id., Transcript Day 8, pp. 1835, 1836-1837.

<sup>12</sup> Id., Transcript Day 8, p. 1823. The USA was ordered to disclose the texts. See *Canfor Corporation v. The USA*, Procedural Order No. 5 of 28th May 2004, para. 8.

<sup>13</sup> Mr Dugan for Methanex, Transcript Day 8, pp. 1838-1840.

this was an application that (i) was made at an inappropriate time (28th August 2002); it should have been made prior to the Partial Award (7th August 2002) because it concerned the meaning of a provision that was the principal subject of that Partial Award, and (ii) it was not pursued at the procedural meeting in March 2003, as it could have been. The application in respect of Article 1105 had been decided in the Partial Award of 7th August 2002 and was not renewed by Methanex thereafter until the main hearing in June 2004. No application had ever been made by Methanex in respect of either Article 1102 or Article 2101 before May 2004.

18. It follows that Methanex's letter of 10th May 2004 to the effect that an application for the negotiating history of NAFTA had been outstanding "for three years" misstates the procedural chronology. It also follows that, on 10th May 2004, i.e. less than one month prior to the main hearing (which had been fixed almost a year earlier, on 30th June 2003) and eighteen months after the date of Methanex's Second Amended Statement of Claim, the Tribunal was presented with an application by Methanex that was to a large extent entirely new; and so far as concerns the application in respect of Article 1105, this application was not made until the penultimate day of the main hearing in June 2004. In the Tribunal's view, all this was far too little, far too late; and as a matter of procedural fairness and equality, and quite apart from the substantive grounds for rejecting the request, the Tribunal is not minded to allow such a delayed application at such a late stage of these lengthy proceedings.
19. (ii) *Vienna Convention*: Methanex made little attempt either in its letter of 10th May 2004 or in oral submissions at the main hearing to explain why a satisfactory interpretation of Articles 1101, 1102, 1105 and 2101 could not be achieved by application of the method prescribed by Article 31 of the Vienna Convention; or why recourse to supplementary means was appropriate pursuant to Article 32 of the Vienna Convention. It is of course possible with a provision of any treaty to formulate a series of questions seeking to elucidate why a particular text was chosen; and it is similarly possible to say in any given case that travaux préparatoires could shed light on the intention of the drafting parties. Whilst the Tribunal acknowledges that Methanex does not have sight of the travaux and may be in difficulty in specifying precisely how the travaux would assist, there should be no difficulty for Methanex to assert in respect of each provision why interpretation in accordance with Article 31 of the Vienna Convention leads to a result that is ambiguous or obscure, or that is manifestly absurd or unreasonable, or that its interpretation in

accordance with Article 31 would be confirmed by the travaux under Article 32, all of which are the prescribed contingencies for recourse to travaux. Methanex did not do so.

20. In Part IV of this Award below, the Tribunal considers seriatim the meaning of the relevant provisions of NAFTA. As will be shown, this exercise did not establish any basis for recourse to the supplementary means of interpretation in the form of the travaux under Article 32 of the Vienna Convention. In these circumstances, there is no inequality of arms as between the Disputing Parties in this arbitration under Article 31 and the relevant provisions of NAFTA<sup>14</sup>. The point of Article 31 is that both Disputing Parties are equally obliged to construe the ordinary meaning of the text. The Tribunal cannot therefore decide from Methanex's submissions that the disclosure sought by Methanex is relevant and material to the issues that Methanex seeks to prove, as required by Article 3.6 and 9.2(a) of the IBA Rules.
21. This factor suffices to dispose of Methanex's application in respect of Articles 1102 and 2101 NAFTA. As regards Articles 1101 and 1105, it is also necessary to consider the impact of existing interpretations, which Methanex's case largely failed to do.
22. *Article 1101*: With respect to Article 1101, the existing interpretation is contained in the Partial Award. So far as the Disputing Parties are concerned, the Partial Award is final and binding for the reasons set out above, in Chapter II E of this Award. For the reasons there explained and in the Tribunal's letter of 25th September 2002, there is no ambiguity in the present case concerning the decision at paragraph 147 of the Partial Award, that the phrase "relating to" in Article 1101(1) NAFTA signifies something more than the mere effect of a measure on an investor or an investment and that it requires a legally significant connection between them. In these circumstances, in the Tribunal's view, there can be no grounds for recourse to the negotiating history in respect of Article 1101. As a theoretical matter, it may be that, prior to the Partial Award, there could have been grounds for such recourse; but, for whatever reason, Methanex did not at that stage seek the negotiating history of Article 1101. That was its choice at that time. It cannot re-make that choice differently now, long after the Partial Award.
23. *Article 1105 NAFTA*: With respect to Article 1105, the existing inter-

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<sup>14</sup> The position in this arbitration may be contrasted with the parties' position in *Canfor v. The USA*. This Tribunal does not know the circumstances under Article 32 which may have moved the *Canfor* tribunal to decide as it did, but would in any event not subscribe to the international legal reasons given by the *Canfor* tribunal for its Order No. 5, at para. 22 (see reference above).

pretation is contained in the FTC's Interpretation of 31st July 2001. Leaving to one side the impact of Article 1131(2) NAFTA, the FTC's interpretation must also be considered in the light of Article 31(3)(a) of the Vienna Convention as it constitutes a subsequent agreement between the NAFTA Parties on the interpretation of Article 1105 NAFTA (without here deciding Methanex's claim that the interpretation of 31st July 2001 is in truth an amendment, not an interpretation). It follows that any interpretation of Article 1105 should look to the ordinary meaning of the provision in accordance with Article 31(1) of the Vienna Convention, and also take into account the interpretation of 31st July 2001 pursuant to Article 31(3)(a) of the Vienna Convention. Indeed, according to *Oppenheim's*, an authentic interpretation by treaty parties overrides the ordinary principles of interpretation:

*"The parties to a treaty often foresee many of the difficulties of interpretation likely to arise in its application, and in the treaty itself may define certain of the terms used. Or they may in some other way and before, during, or after the conclusion of the treaty, agree upon the interpretation of a term, either informally (and executing the treaty accordingly) or by a more formal procedure, as by an interpretative declaration or protocol or a supplementary treaty. Such authentic interpretations given by the parties override general rules of interpretation."*<sup>15</sup>

Moreover, there has been a series of decisions by NAFTA tribunals on the meaning of Article 1105; and Methanex has indeed relied on the most recent such decision (in the *Waste Management case*<sup>16</sup>).

24. The issue of the interpretation of Article 1105 is considered by the Tribunal below, in Part IV of this Award. For present purposes the point is that, for its application to succeed, it was for Methanex to show that notwithstanding the existence of various possible interpretations of Article 1105, including a subsequent agreement by the NAFTA Parties as to interpretation, it remained appropriate for this Tribunal, in this case, to have recourse to supplementary means of interpretation. That requires the meaning of Article 1105 to be demonstrably ambiguous or obscure, or the result of interpretation pursuant to Article 31 to be manifestly absurd or unreasonable, or its interpretation in accordance with Article 31 to be confirmed by the travaux. Where in the course of time there has been a series of

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<sup>15</sup> *Oppenheim's International Law*, 9th ed., Volume 1, p. 630.

<sup>16</sup> *Waste Management Inc v. United Mexican States*, Award of 30th April 2004, 43 ILM 967 (discussed further in Part IV below).

decisions on a given provision by international tribunals seised with the task of interpretation; and there has also been an agreement by treaty parties on interpretation, the likelihood of supplementary means of interpretation contemplated by Article 32 of the Vienna Convention being relevant and material must inevitably decline. Methanex did not satisfactorily address these difficulties; and it failed in particular to demonstrate to the Tribunal how reference to the travaux could nonetheless be appropriate in this case.

25. Further, such difficulties were all the more acute given that the scope of document production that Methanex sought from the USA was exceptionally broad. As noted, Methanex sought negotiating texts, minutes of meetings and memoranda prepared for the NAFTA negotiations, whether shared or not between the NAFTA Parties. It was thus for Methanex to demonstrate not only that it was appropriate to depart from the text of the NAFTA provisions and to conduct an investigation ab initio of the supposed intentions of the NAFTA Parties<sup>17</sup>, but also that such intentions could reliably be established from documents which had never been seen or discussed between the three NAFTA Parties<sup>18</sup>. It failed to do so.
26. In conclusion, for all these reasons, the Tribunal rejects Methanex's Request for Documentary Disclosure by the USA of 10th May 2004, as modified and developed by Methanex at the main hearing in June 2004.

## **PART II - CHAPTER I**

### **THE USA'S APPLICATION FOR THE EXCLUSION OF CERTAIN OF METHANEX'S EVIDENCE**

#### **1) Introduction**

1. By letter dated 23rd April 2004 (second letter) to the Tribunal, the USA submitted a proposal for an exchange of written submissions

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<sup>17</sup> See the Commentary of the International Law Commission referred to above, in Chapter II B.

<sup>18</sup> In the *Canfor* case, the NAFTA tribunal decided that internal memoranda of one NAFTA Party do not reflect the common negotiating intention of the NAFTA Parties in drafting, adopting or rejecting a particular provision: see *Canfor Corporation v. The USA*, Procedural Order No. 5 of 28th May 2004, para. 19. The NAFTA tribunal case did not therefore order disclosure of such memoranda, although it did order the disclosure of communications, explanation notes, position papers or memoranda that were shared amongst the NAFTA Parties: see *id.*, paras. 20-21. For the reasons stated above, this Tribunal does not share the view expressed by the *Canfor* tribunal.

on the admissibility of certain of the evidential materials submitted by Methanex. In the light of objections raised to this application by Methanex's letter of 4th May 2004, including the absence of any identification by the USA of what evidence it considered objectionable, the Tribunal invited the USA to serve by 18th May 2004 written submissions dealing with its objection to the admissibility of evidential materials already adduced by Methanex. By Motion dated 18th May 2004, the USA then applied for the exclusion of certain categories of evidence submitted by Methanex, by reference to Article 25(6) of the UNCITRAL Rules, which provides that: "The arbitral tribunal shall determine the admissibility, relevance, materiality and weight of the evidence offered".

2. There were four categories to which the USA objected as evidence in these proceedings. First, the USA submitted that several documents submitted into evidence by Methanex were illegally copied from the private files of Mr Vind and his company, Regent International: Exhibits 52-61, 64, 66, 151-153, 155-156, 159-160, 162, 165, 202, 216-219, 222-223, 226 and 258-259 to the Second Amended Statement of Claim (referred to as the "Vind Documents"). The USA submitted that the admission of illegally obtained evidence by Methanex was inconsistent with the principle of good faith inherent in any arbitration agreement. As to the second and third categories, the USA contended that several of the witness statements and expert reports served by Methanex failed to comply with the directives set out at paragraphs 164 and 165 of the Partial Award and Articles 4 and 5 of the IBA Rules (e.g. as to present and past relationships with the Disputing Party, source of information, etc). With respect to witness statements, the USA's complaint concerned the declaration of Mr Puglisi dated 28th March 2003, a letter of Mr Hastings dated 14th January 2004, and the second and third affidavits of Mr Macdonald dated respectively 5th November 2002 and 19th February 2004. With respect to expert reports, the USA's complaint concerned the two reports of Professor Williams and the two reports of Professor Rausser. Fourth, the USA contended that Methanex had submitted evidential materials with its Reply of 23rd April 2004 to the submissions of amici, whereas all of Methanex's documentary evidence was to have been submitted by 31st January 2003 under the Tribunal's procedural orders.
3. The Tribunal need not here recite at any length its decisions regarding the USA's second to fourth complaints. Having heard the Disputing Parties by telephone conference-call on 24th May 2004, the Tribunal

decided these issues largely in favour of Methanex, as set out in its order by letter dated 1st June 2004. In summary, the Tribunal ruled that the expert reports of Professor Williams and Professor Rausser could remain in evidence, subject to relevance, materiality and weight. The Tribunal also ruled that the witness evidence of Mr Puglisi and Mr Macdonald could remain in evidence; and that their subsequent statements of 31st May 2004 should be admitted, subject to relevance, materiality and weight; and it noted Methanex's confirmation that Mr Hastings had not submitted witness evidence. Lastly, as regards Methanex's response to the amici, the Tribunal ruled in favour of Methanex.

4. The Tribunal returns to the first complaint made by the USA, in regard to the Vind Documents. It had been preceded by Mr Vind's witness statement dated 21st November 2003, adduced with the USA's Amended Statement of Defense of 5th December 2003. Mr Vind there testified that the Vind Documents were copies of documents contained in the files of his company, Regent International, including personal notes, private correspondence, materials expressly subject to legal professional privilege and a private address-book. Mr Vind was at the time the CEO of Regent International, with offices at Brea, California. (For ease of reference, the Tribunal does not distinguish between Mr Vind and his company). Mr Vind stated that he realised that someone had broken into his offices three or four years ago (i.e. in 1999-2000). He suspected that certain persons unknown to him had induced the office-building's cleaning company to grant them access to his company's offices, or that the persons who broke in were aware that security was lax over the weekend. He suspected that persons aligned with MTBE interests were behind the break-in to his offices. He said that he reported the break-in and the illegal copying of documents to the FBI and to the Attorney General of California.
5. It was not possible for the Tribunal to resolve this matter during the telephone conference-call with the Disputing Parties on 24th May 2004. By the Tribunal's order of 1st June 2004, the Tribunal ruled only that the Vind Documents should remain in evidence for the time being *de bene esse*, subject to further submissions by the Disputing Parties and further order from the Tribunal at the main hearing, which was to start the following week. At that main hearing, the Vind Documents were to become a controversial issue in the proceedings, requiring in camera sessions at Methanex's request and four new witnesses as to the manner of Methanex's acquisition of the Vind Documents.
6. The Tribunal eventually decided this issue against Methanex at the main hearing, by excluding the Vind Documents from the evidence;

and it is appropriate for the Tribunal to repeat that order in this Award (with reasons), together with an account of the successive explanations offered by Methanex.

## **2) Methanex's Initial Response**

7. Returning to the procedural chronology in regard to the Vind Documents, on 31st May 2004 Methanex submitted its own Motion Concerning Evidentiary Matters, supported by declarations from Mr Macdonald and Mr Puglisi. This application included a response to the USA's Motion of 18th May 2004. Methanex maintained that the Vind Documents had been gathered legally; and Methanex submitted a written declaration of Mr Puglisi dated 31st May 2004 in support of that contention. Mr Puglisi is a private detective, whose company had once been engaged by Methanex's legal advisers (but not Counsel or former Counsel engaged by Methanex in these arbitration proceedings). This firm of legal advisers had its office in Washington DC; and Methanex always declined to identify it by name in these arbitration proceedings. For ease of reference, it is here referred to as "the unnamed DC law firm".

8. In that declaration, Mr Puglisi described the origin of the Vind Documents as follows:

*"The Vind Documents were found discarded on public property behind Regent International's offices at 910 E Birch Street in Brea, California, 92821. I supervised a licensed California private investigator who collected the discarded materials. The documents were forwarded to me via express mail, overnight delivery in a sealed box. I made copies of those documents and forwarded these copies to counsel for Methanex during the course of my investigation. A subset of these materials are the Vind Documents".*

As events unfolded at the main hearing, it soon became apparent that the first sentence was wrong; and that the remainder was materially incomplete.

## **3) Methanex's Embargo Request**

9. In the course of the second day of the main hearing (8th June 2004), in sessions held in camera at Methanex's request, Methanex stated that it had now found various of the originals of the Vind Documents (as requested by the Tribunal); and it submitted exhibits to support its contention that the Vind Documents had been obtained lawfully

by Methanex: Exhibit X1, being copies of Federal Express and other envelopes showing when so-called "original" documents were received by Mr Puglisi; Exhibit X2, being a list of the dates of the envelopes in Exhibit X1; Exhibit X3, being a receipt recording the recent handover of so-called original documents by Mr Puglisi to Methanex's Counsel in these proceedings; Exhibit X4, being a list showing what so-called originals had and had not been located by Methanex; and Exhibit X5, being an index of so-called original documents, attaching at Tabs 1-31 copies of the so-called originals and showing (i) the Methanex exhibit number, (ii) the Joint Submission of Evidence reference, (iii) the provenance, i.e. Mr Puglisi or an un-named lawyer, (iv) whether the so-called original had or had not been located and (v) in certain cases, the date when the document had been received by Mr Puglisi.

10. Methanex also requested an embargo with respect to communications from the USA to Mr Vind so far as concerned the disclosure of original documentation, the further exhibits, the contents of the discussions held in camera and comments recorded on the transcript in the course of the open hearings prior to Mr Vind's testimony. On 8th June 2004, the Tribunal granted a temporary embargo in order to preserve the status quo until Mr Vind testified under cross-examination. (Mr Vind was due to testify, and did testify, on 10th June 2004). On 9th June 2004, after hearing the Disputing Parties, the Tribunal made a further order with respect to the embargo request by Methanex, in these terms:

*"In regard to the USA's motion to exclude the remaining Regent International documents, the Tribunal is being requested by Methanex to impose an embargo on certain documentary and evidentiary materials prior to Mr. Vind's testimony tomorrow on 10th June 2004, which request has been opposed by the USA. The Tribunal considers that it has the power to impose the embargo, but in the exercise of its discretion and except in two respects as explained below, it declines to impose the embargo. The reasons for this order will be given at a later date.*

*First, before Mr Vind's testimony tomorrow, nothing shall be revealed by the USA to Mr Vind of any discussions taking place in these sessions held in camera over the last three days.*

*Second, whilst both Methanex and the USA shall be entitled to adduce into evidence this afternoon the new exhibits X1 to X4, if any such exhibit is not adduced in evidence this*

*afternoon with the two Methanex witnesses, it will not be revealed by the USA prior to Mr Vind's testimony tomorrow to Mr Vind. Mr Vind can be shown the new bundle marked X5, the bundle we were shown this morning, before he commences his testimony tomorrow, except for the new documents in Tab 24 and Tab 31, which the United States agreed not to show or discuss with him prior to his testimony.*

*In addition, Mr Vind, if he requests, can be shown the so-called originals of the relevant Regent International documents before he commences his evidence tomorrow. It also follows that the two Methanex witnesses who will give evidence this afternoon will testify in public, subject to the Tribunal's existing order of 28th May 2004 on sequestration, which will mean that Mr Vind will be excluded from the hearing room during their testimony."*

11. The Tribunal's reasons for this order were two-fold. First, it desired as a general principle that the main hearing should be heard openly, without unnecessary resort to hearings in camera and a secret transcript. Second, as requested by Methanex, it was minded for the time being to protect Methanex's right to cross-examine Mr Vind as to his credibility, without prior and unnecessary disclosure of Methanex's growing difficulties in explaining the lawful source for the Vind Documents in its possession. As events unfolded, that right became illusory; and eventually Mr Vind's sense of outrage was, in the Tribunal's view, fully justified.

#### **4) The Testimony of Mr Puglisi and Ms Morisset**

12. The Tribunal initially heard evidence from two witnesses for Methanex on the methods used by its agents at different times to obtain the Vind Documents: Mr Puglisi and Ms Morisset.
13. **Mr Puglisi:** Prior to the hearing (on 28th March 2003 and 31st May 2004), Mr Puglisi had submitted two declarations. Mr Puglisi's testimony deals with the first period of document collection from July 1997 to August 1998, before Methanex commenced these arbitration proceedings against the USA.
14. In his oral evidence, Mr Puglisi confirmed the truth of his two written declarations<sup>1</sup>. He testified that he had been retained in 1997 by law-

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<sup>1</sup> Transcript Day 3, p. 619.

yers representing Methanex (i.e. the un-named DC law firm) to obtain information on the funding of certain lobbying organisations which, he said, were sending out negative publicity on Methanex products. He testified that he had identified that Mr Vind (of Regent International) and ADM were sponsoring these organisations; and that subsequently his company investigated Mr Vind to see if there was evidence of an active and concerted effort directed against Methanex. In this context, documents including certain of the Vind Documents were obtained from a dumpster by a self-employed private investigator, Mr Terry Dunne, who sent the documents by courier to Mr Puglisi. On receipt, the documents were labelled on the back, the label showing the target of collection (Regent International), a case identification number, the address that the given document was recovered from (910 E Birch Street, Brea, California), date of receipt, and a serial number<sup>2</sup>. He confirmed from the labelling and copies of the courier packages (and a list of dates thereof) that he had received in the period of July 1997 to August 1998 the originals of Exhibits 52-60, 64, 66, 151, 153, 155, 159-160, and 165 to the Second Amended Statement of Claim. Mr Puglisi testified that it was the practice of his firm to operate within the law, and that the documents had been lawfully obtained by Methanex<sup>3</sup>.

15. According to Mr Puglisi, he was told by Mr Dunne that the documents were collected from the communal dumpster for the building in which the Regent International offices were located, and that this dumpster was in a "public" area adjacent to the building parking lot. Mr Puglisi testified that, based on what he had been told by Mr Dunne, there was a parking lot behind the building and that the dumpster was located in that parking lot<sup>4</sup>. He also said that he had a recollection of seeing a photograph that Mr Dunne might have taken or a handwritten diagram made by him<sup>5</sup>. This showed that the parking lot was not gated; that there was no security guard; and that there was no restriction on who could enter the lot. Mr Puglisi further stated in re-examination that the public had total access to the parking lot and to the dumpster; and that there was no chainlink fence around it<sup>6</sup>.
16. Mr Puglisi testified that his assignment to Mr Dunne was to collect whatever he could find in the dumpster that related to Regent International. As to the original for Exhibit 151, Mr Puglisi accepted in cross-examination that there was no label on the back of this

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<sup>2</sup> Id., pp. 595-603.

<sup>3</sup> Id., pp. 604-609.

<sup>4</sup> Id., pp. 637-638.

<sup>5</sup> Id., pp. 641, 678.

<sup>6</sup> Id., p. 677.

document (whereas he said that in the ordinary course of events there should have been); but he stated that he could recall receiving this document specifically, or an identical document, as it was of noted interest at the time. This document was the draft itinerary for the meeting at dinner of 4th August 1998 between (inter alios) Mr Davis, Mr Vind and ADM. Mr Puglisi also accepted that the original document tendered by Methanex for Exhibit 151 had a fax trailer at the bottom of the document, whereas inexplicably the actual Exhibit 151 did not<sup>7</sup>. Both versions of the document record a production date "7/30/98", presumably by ADM.

17. This draft itinerary, Exhibit 151 (whichever version), is the document to which the Tribunal referred in the Partial Award, at paragraph 60 (page 22). Albeit then described by Methanex as an "agenda" and not yet produced by Methanex to the Tribunal or the USA, the document formed an important part of Methanex's submissions at the jurisdictional hearing in July 2001, regarding its recent discovery of the "secret" meeting of 4th August 1998 between Mr Davis and ADM (see especially Day 3, at pages 480-486 of the transcript). Mr Puglisi's records show that he received this document on 9th July 1998; and one version bears a fax transmission date of "Aug 4 '98". Accordingly the Tribunal infers that this draft itinerary was in Methanex's possession by August 1998 and that, as Mr Puglisi confirmed, its significance was then noted by Methanex, with knowledge of the intended meeting, its date, place and participants, including Mr Vind of Regent International.
18. Mr Puglisi had no recollection of receiving the originals of Exhibits 217-219, 222-223, 226 and 258-259 to the Second Amended Statement of Claim. As to the apparent discrepancy between this evidence and his second declaration, which on its face was made with respect to all of the Vind Documents, Mr Puglisi stated that the declaration was based on the documentation supplied to him by Methanex. He testified: "Basically, the lawyers representing Methanex presented to me that a subset of the documents that we had collected had been entered into this hearing. I took on faith that what they told me was accurate. I did not go back and cross-reference the footnotes with the documents that were presented to me"<sup>8</sup>. This was, in the Tribunal's view, a serious error.
19. **Ms Morisset:** Ms Morisset, a French law graduate, was working as a para-legal for the un-named DC firm and studying law at the

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<sup>7</sup> Id., pp. 646-652.

<sup>8</sup> Id., p. 664.

Catholic University in Washington DC. She was called as a witness by Methanex to describe the second period of document-collection by Methanex's agents from August 2000 to February 2001, after Methanex had commenced these arbitration proceedings against the USA. According to Ms Morisset's testimony, she had joined the un-named DC law firm in about September 2000; and within the law firm she had worked on this assignment between October 2000 and January 2001.

20. A declaration by Ms Morisset was served by Methanex on the third day of the main hearing, on 9th June 2004. In this declaration, Ms Morisset stated her understanding that, during the period from August 2000 to February 2001, the un-named DC law firm had retained a private investigator, Mr Jim Stirwalt, to collect and forward documents discarded by Regent International at its offices in Brea. A total of 88 packages had been received; and these had been recorded on receipt by Ms Morisset by means of a Bates stamp being applied to copies of the original documents. Ms Morisset also stated her understanding that the documents were collected on public property; and that the collection was terminated when Regent International relocated its offices to different premises in February 2001.
21. In her oral evidence to the Tribunal, Ms Morisset stated that she had understood from conversations with partners of the un-named DC law firm (which she did not identify) that Mr Stirwalt was investigating Regent International and Mr Vind in connection with how the ethanol industry was coming out against MTBE<sup>9</sup>. She had learnt that the documents being obtained by Mr Stirwalt had been discarded by their owners; and she had asked one of the partners whether obtaining discarded documents was legal. As she recalled, she had been shown an extract of the California Code to this effect (which she did not identify)<sup>10</sup>. It was her understanding that the documents were obtained from a "public" place, namely a dumpster behind the offices of Regent International in Brea, and that Mr Stirwalt was instructed by her law firm not to trespass onto any private property to obtain documents and to stay within the law<sup>11</sup>. Ms Morisset's testimony was that the originals of Exhibits 217-219, 222-223, 226 and 258-259 to the Second Amended Statement of Claim were documents for which she had kept custody as part of her employment with the law firm<sup>12</sup>.

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<sup>9</sup> *Id.*, pp. 682-684.

<sup>10</sup> *Id.*, p. 685.

<sup>11</sup> *Id.*, pp. 686-689.

<sup>12</sup> *Id.*, pp. 693-707. Methanex relied on two signed receipts, subsequently numbered exhibits X6-X7, as evidence that the originals had been handed over to Methanex's counsel on 8th June 2004.

22. In cross-examination by Counsel for the USA, Ms Morisset confirmed that she had received documents from Mr Stirwalt, made a copy of what she had received, and applied a Bates stamp. She noticed very early on that the documents were discarded documentation as she saw coffee and other stains on the documents, some of which were torn. It was this that had led to her question to the partners of the unnamed DC law firm as to whether obtaining discarded documents was legal<sup>13</sup>. As she recalled, the conversation about the legality of what Mr Stirwalt was doing took place in the fall of 2000. She did not know about discussions before that date, although she had been told by her law firm that Mr Stirwalt had been instructed to operate with legal means only<sup>14</sup>. Ms Morisset's understanding was that Mr Stirwalt terminated his investigation because he had been requested to do so: the offices of Regent International had moved and the documents were no longer accessible to the public because they were behind a wooden fence with a "No Trespassing" sign<sup>15</sup>.
23. As to Methanex's Exhibit 258, a print out from Mr Vind's electronic diary, Ms Morisset testified that the so-called original of this document was "one of the cleaner ones", without any tell-tale signs of being discarded as trash. She also confirmed that there were holes consistent with the document having been stapled, the staple now being missing: "... the way I processed the documents was in a way to make sure they stayed as - that I respected their integrity as much as possible. So, I was hired as a legal assistant because I'm very detail oriented, and one of the things that I did is to make sure that if I had an original, that was stapled, I would actually go back with the staple, look at where the holes were, and staple it again. So, either this came to me stapled and I removed the staple and I forgot to re-staple it, which I think is unlikely, or it came to me in this fashion, and I just left that way"<sup>16</sup>. From all the evidence adduced at the main hearing, it remains unclear to the Tribunal whether Exhibit 258 was procured by Methanex as a discarded document falling into the same category as other Vind Documents received by Ms Morisset.

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<sup>13</sup> Transcript Day 3, p. 713.

<sup>14</sup> *Id.*, pp. 715-717.

<sup>15</sup> *Id.*, pp. 718-719.

<sup>16</sup> *Id.*, pp. 722-724.

## 5) Mr Vind's Testimony

24. Shortly before the oral testimony of Mr Vind, the USA sought to introduce photographs that were said to show that the Vind Documents were not taken from a dumpster in a parking lot; that there was no parking lot behind Mr Vind's offices; and that the dumpster was located behind closed doors in a private part of the office-building itself. Methanex objected to the tendering of these photographs on the basis that they had not been authenticated. The Tribunal decided to look at the photographs for information, taking into account that Mr Vind would be able to testify to their authenticity later that same day<sup>17</sup>. (A selection from these photographs of the site, comprising Exhibit X8, appears below in Annex 3 to this Chapter).
25. Mr Vind subsequently testified that he had taken these photographs on 6th June 2004, that they showed the office-building in Brea that housed his company's offices prior to its move to different offices in about January 2001. His evidence was that the photographs showed that the dumpster was not located on public property, but rather in the building behind closed doors; and that he had every expectation that anything he threw out would go to the licensed waste disposal contractor and be disposed of in a proper manner, and would not be pilfered by third persons, including Methanex's agents<sup>18</sup>.
26. Mr Vind confirmed that there was no parking lot directly adjacent to the Regent International offices, and no dumpster adjacent to those offices. He said that the trash was kept inside the office-building, behind doors. He explained that this was in part because the office-building was opposite a hotel, which would not allow trash to be kept out in the open<sup>19</sup>. He explained that cleaners would come to the Regent International offices (on the second floor of the building), take the trash from the trash receptacles in the office, tie the trash in bags, and take these to the closed trash area which was part of the common area for tenants in the office building. Right outside the closed trash area was a space for the trash truck to reverse and unload the dumpster, which was a publicly accessible space. He believed the practice was to roll the dumpster out from the private trash area and then the trash truck would pick it up and empty

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<sup>17</sup> The photographs were subsequently admitted into evidence by the Tribunal and numbered Exhibits X8-X10. The USA also tendered two satellite photographs and a map of the area of the Regent International offices, which were numbered Exhibits X11-X12 and X13 respectively.

<sup>18</sup> Transcript Day 4, pp. 1011-1012.

<sup>19</sup> *Id.*, pp. 943-945.

its contents into the truck. Mr Vind also stated that the trash area behind the doors was intended to be locked, although he thought in practice the cleaning contractors being as lax as they were did not keep the doors locked at all times<sup>20</sup>.

27. Mr Vind also testified that when he was informed by the US State Department that items from his personal correspondence were being relied on by Methanex as evidence in these arbitration proceedings, he became very concerned as to where the documents had come from. Documents had been taken from his files - not merely copied - and original documents were no longer to be found in his files. Mr Vind had complained to the building landlord on numerous occasions with respect to the cleaning company leaving the door of the office-building open whilst they were cleaning at the weekend; and he stated that it would have been easy for anyone to walk into the offices at nighttime or over the weekend when the cleaners were there, and to take whatever they wanted. Mr Vind testified that he had complained of this incident to the Attorney General for California (Mr Lockyer). Mr Vind also said that he had contacted his lawyer (Mr Richard Crane) and requested him to contact the FBI because the Attorney General had raised the possibility that this was a federal crime<sup>21</sup>. Mr Vind accepted that it was not correct to say that he (Mr Vind) had reported the break in to the FBI. His evidence was that he was convinced that someone had illegally entered his office to obtain the documents, although he had no personal knowledge of such a break in. He had not filed a report with the local police<sup>22</sup>. By late 2003, the relevant events were, of course, at least thirty months old.
28. As to the different types of documents that made up the Vind Documents, Mr Vind stated that it would be illogical for him to throw away correspondence that was only three or four years old<sup>23</sup>. Drafts of documents would likely be put into the trash. His telephone message books would be put into the trash after about a year or so (a copy of a message book is Methanex's Exhibit 259). He testified that he only printed out one copy of his electronic diary (a copy of which appears at Methanex's Exhibit 258), which he kept on his desk. He did not recall a date when that copy went missing, nor a time when he discarded it<sup>24</sup>.

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<sup>20</sup> *Id.*, pp. 1018-1019.

<sup>21</sup> *Id.*, pp. 998-1002.

<sup>22</sup> *Id.*, p. 1003.

<sup>23</sup> *Id.*, p. 1008.

<sup>24</sup> *Id.*, pp. 1008-1011.

29. Mr Vind was a truthful witness; and as regards matters falling within his own knowledge, the Tribunal accepted his testimony.

### **6) The Photograph Adduced By Methanex**

30. In the course of its submissions on the Vind Documents, Methanex introduced a photograph to the effect that there came a time when Methanex's document collection operation stopped because Regent International moved to different premises where the dumpster was protected by a "No Trespassing" sign<sup>25</sup>. This photograph showed a dumpster located outside a different building, behind two doors, one of which had a sign "Posted, No Trespassing, Keep Out". Methanex submitted that the photograph was significant in terms of demonstrating its good faith in that Methanex had ceased the collection of evidence when it had considered that it was no longer legal. The photograph was dated 11th October 2000; and it was subsequently explained further in the evidence of Mr McAnish: he had learnt in October 2000 from reading the Vind Documents that Mr Vind's company was intending to move in early 2001 to its new offices nearby, at Sherwood Professional Center, 1075 Yorba Place; and he then took the photograph at these new premises.
31. There are several possible explanations for Methanex's conduct in suspending its activities at the new offices of Regent International (i.e. after 12th February 2001). However, even accepting Methanex's explanation for its good faith in regard to the new offices (which the Tribunal is prepared to assume for present purposes), it does not necessarily establish Methanex's good faith in regard to its activities at Mr Vind's old offices.

### **7) The Testimony of Mr Stirwalt and Mr McAnish**

32. Subsequent to the oral testimony of Mr Vind, Methanex indicated that its submissions were now made on the assumption that the documents were not in fact obtained from a dumpster located outside Mr Vind's offices on a parking lot, but rather that the private investigators obtained the documents from the dumpster within the office-building as described by Mr Vind, on the assumption also that the doors to the closed trash area were not locked and/or were open. Methanex was asked by the Tribunal if it was pursuing an application to adduce evidence from the private investigators themselves,

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<sup>25</sup> The photograph was numbered Exhibit X14.

but Methanex said that it was not doing so. The Tribunal then expressed its concern as to the unsatisfactory state of the evidence on precisely how the two individuals, Mr Stirwalt and Mr Dunne, retrieved the documentation from the dumpster behind the doors at the office building, or otherwise. It asked Methanex whether it was making any application to the Tribunal to produce these two witnesses. Methanex stated that it was; and it now also stated (for the first time) that its relevant collection-agents were *not* Mr Stirwalt and Mr Dunne, but Mr McAnish working for Mr Stirwalt and Mr Dunne.

33. By letter of 12th June 2004, the Tribunal was informed that Methanex would be submitting evidence from Mr McAnish and Mr Stirwalt; but that it had been unable to locate Mr Dunne. Declarations of Mr McAnish and Mr Stirwalt (both dated 12th June 2004) were subsequently served by Methanex on 13th June 2004. On 14th June 2004, the Tribunal was informed by letter from Methanex that it had located Mr Dunne but that: "Mr Dunne does not want to be involved in this proceeding. Accordingly, he declined to produce a witness statement or to testify". Mr Dunne was not a witness in these proceedings, although he was made personally aware of the relevance of his testimony to this arbitration.
34. Accordingly, in Mr Dunne's absence, Methanex adduced no direct testimony in regard to document-collection during the first period of its activities from July 1997 to August 1998. Being limited to the second period of document-collection from August 2000 to February 2001, the evidence Mr McAnish and Mr Stirwalt went only to the method of collection of eight of the Vind Documents, namely Exhibits 217-219, 222-223, 226 and 258-259 to the Second Amended Statement of Claim.
35. **Mr Stirwalt:** In his declaration dated 12th June 2004, Mr Stirwalt stated that he was a licensed private investigator in California and Arizona; and that, in August 2000, he had been engaged by Control Risks Group of McLean, Virginia, on behalf of the un-named DC law firm whose client was Methanex. His instructions were to investigate Mr Vind and Regent International and to ascertain whether documents discarded by Mr Vind and Regent International could be obtained legally. Mr Stirwalt stated that he had referred the work to Mr Patrick McAnish, also a licensed private investigator in California, whom he had known for ten years. The assignment had terminated in early 2001 when Regent International moved office locations; and it had been concluded that discarded documents were no longer legally available for collection.

36. In oral testimony, Mr Stirwalt stated that he had discussed issues concerning the legality of obtaining the discarded documents on an almost daily basis with the unnamed DC law firm; and that it had been both his opinion and the opinion of the law firm that the document collection was lawful<sup>26</sup>. He confirmed, however, that he had never visited the site at 910 E Birch Street in Brea; and that he had not consulted with any legal experts on the law of California. He stated that Mr McAnish had told him on a daily basis that he was retrieving documents from the dumpster<sup>27</sup>. He also stated that he did not know Mr Puglisi. Mr Dunne had telephoned him on the previous day (14th June 2004); and they had discussed their testimony requested for these proceedings and also briefly the particulars relating to the collection of the documents<sup>28</sup>.
37. **Mr McAnish:** In his declaration dated 12th June 2004, Mr McAnish stated that he had been contacted by Mr Stirwalt to undertake a long-term surveillance and recovery of discarded material from the common dumpsters located at 910 Birch Street, Brea. Mr McAnish stated that, every weekday morning at about 6.00 a.m., he visited the building and accessed the dumpsters from the public walkway in front of the doors to the dumpster area. He stated that the doors were never locked and, at times, were open or ajar. He said that he brought home garbage bags containing Regent International documentation; and having sorted the documentation at his home, he sent what appeared to be relevant documentation initially to Control Risks Group and then, from September 2000, direct to the unnamed DC law firm. From his review of the documents, he ascertained that Regent International would be moving in early 2001. In October 2000, he visited the new location (Sherwood Professional Center, 1075 Yorba Place); and he took the photograph showing the access the dumpster there. He determined that the dumpster was located in an area where a no-trespassing sign had been posted; and it was concluded that it would not be possible legally to obtain documents from this new site. He stated that he never retrieved documents from the new location, and that the last retrieval from 910 E Birch Street was on or around 12th February 2001. Mr McAnish attached to his declaration eight photographs of 910 E Birch Street that he said he had taken on 12th June 2004.

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<sup>26</sup> Transcript Day 7, p. 1606.

<sup>27</sup> Id., p. 1613.

<sup>28</sup> Id., pp. 1614-1616.

38. In oral testimony, Mr McAnish said that at the time of his investigations there had been six tenants in the 910 E Birch Street building, including a fitness club located in the basement, of which he had become a member, and whose facilities he had used on half a dozen occasions<sup>29</sup>. Mr McAnish testified that he visited the site every weekday from August 2000 to February 2001, i.e. on more than 100 occasions. During this period, he entered the trash area behind the doors (situated inside the office-building) and opened every trash-bag in the dumpsters until he found the bags with documentation from Mr Vind and his company. He said that sometimes the doors to the trash area were open. The Tribunal infers that on other times the doors were closed.
39. He would then remove the bag (or occasionally bags) of Regent International trash<sup>30</sup>. The other trash-bags contained documentation and trash from other tenants of the office-building, which included a medical practice. Mr McAnish did not remove these bags. He would take the bags containing Regent International's trash to his car parked nearby; and given that (as it appeared to him) Mr Vind's company was disposing of its documentation in preparation for its removal to new premises, these trash-bags could be heavy: at least one weighed about 20 lbs.
40. Generally this would all be done in ten or so minutes, between the hours of 6.00 and 7.00 in the morning<sup>31</sup>. This timing, he explained, was convenient because he thereby avoided the traffic jams on the roads later in the day between Long Beach (where he lived) and Brea (about 25 miles away); and it was not chosen (he said) because the site was then relatively deserted (as indeed it was). During much of this period's winter months, the Tribunal notes that the site would also be in darkness. Mr McAnish would then return home to review the contents of the bag, and would send relevant documents by courier, initially to Control Risks Group in McLean, Virginia and subsequently to the un-named DC law firm. He said that he did not recall the name of the law firm<sup>32</sup>. In response to a question from the Tribunal, he said that he had sent over one hundred courier packages to the law firm. He then gave evidence that he did not believe that he used the name of the law firm on the courier package, but

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<sup>29</sup> *Id.*, p. 1624.

<sup>30</sup> *Id.*, pp. 1634-1635.

<sup>31</sup> *Id.*, p. 1643.

<sup>32</sup> *Id.*, pp. 1644-1645.

sent the packages to a specific individual at the law firm's address<sup>33</sup>. That individual remained un-named by Mr McAnish and Methanex.

41. Mr McAnish testified that on a couple of occasions he had observed the dumpsters being emptied by truck. He said that collections were made weekly. He confirmed that the trash collection personnel opened the doors of the trash area, if they were not already open, rolled out the dumpsters and emptied them into the truck. He confirmed that he never saw the dumpsters being left out for any long period of time<sup>34</sup>.
42. Mr McAnish testified that he spoke to Mr Stirwalt maybe once a week, but that was just in relation to the number of hours he was spending on this assignment. He said that initially he (probably) had a conversation with Mr Stirwalt as to where the dumpsters were located; and that they had several conversations at the start of the assignment regarding where to send the documents. He could recall no other conversations with Mr Stirwalt as to the methods used for the collection of documents<sup>35</sup>. He had also had a conversation with Mr Stirwalt early in the assignment when he had been told that the un-named DC law firm's opinion was that what he was doing was legal. He had obtained a copy of the Brea City Ordinance (see further below) at Mr Stirwalt's instruction and had passed this onto Mr Stirwalt. He had only briefly looked at the contents of the Ordinance, which he understood had been requested by the un-named DC law firm<sup>36</sup>. Mr McAnish said that he had taken out a gym membership at the fitness club on Mr Stirwalt's instruction "to provide a legitimacy for my being there"<sup>37</sup>. He had been reimbursed for this by Mr Stirwalt. (Mr McAnish' evidence was that he was being paid by Mr Stirwalt<sup>38</sup>.)

## 8) The Further Submissions of the Disputing Parties

43. ***Methanex's Submissions:*** Methanex relied on the overall evidence to establish its bona fides in regard to the collection of the Vind Documents. So far as concerned the methods of collection, Methanex conceded that the recollection of Mr Puglisi had been faulty; and that it was willing to withdraw his evidence in that respect.

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<sup>33</sup> Id., pp. 1669-1670.

<sup>34</sup> Id., pp. 1648-1649.

<sup>35</sup> Id., pp. 1651-1654.

<sup>36</sup> Id., pp. 1664-1666.

<sup>37</sup> Id., p. 1655.

<sup>38</sup> Id., p. 1650.

44. In its submissions on the law, Methanex's position was that the actions of Regent International and Mr Vind constituted an abandonment of all rights in the Vind Documents. The test was the accessibility of the documents to members of the public, as appeared from the decision of the US Supreme Court in *California v. Greenwood* [486 US 35, 108 SCL 1625]. It submitted that the Vind Documents were accessible to all tenants in the office-building, which removed any expectation of privacy, and further accessible in that the doors to the trash area were unlocked. There was no trespassing involved in taking the Vind Documents as there was no "No Trespassing" sign: the documents were in a commercial building in a common area, open to the public, and there was an implied license to open the doors to the public area. In this respect, Methanex relied on three cases: the decision of the Court of Appeal of Louisiana in *Navratil v. Smart* [400 So.2d 268], the decision of the Missouri Court of Appeals in *St. Louis County v. Stone* [776 S.W.2d 885], and the decision of the Court of Appeals in Arizona in *Maricopa County, Juvenile Action No. J-75755* [21 Ariz.App. 542, 521 P.2d 641].
45. So far as concerned the Brea City Ordinance relied on by the USA (see further below), Methanex submitted that it was far from clear that this Ordinance was concerned with privacy or the protection of property: the aim of the Ordinance was the protection of public health. It also submitted that the Ordinance was invalid as it was inconsistent with the common law. In this respect, it relied on a considerable number of authorities, in particular the decision of the California Court of Appeal, Third District, in *V.I. Wexner v. Anderson Union High School District Board of Trustees et al* [258 Cal. Rptr. 26] and the decision of the Supreme Court of California in *The People v. Ayala* [24 Cal.4th 243, 6 P.3d 193, 99 Cal. Rptr.2d 532]. Relying on the decision of the Supreme Court of California in *Cheong v. Antablin* [16 Cal.4th 1063, 946 P.2d 817, 68 Cal.Rptr.2d 859], Methanex submitted that there were policy reasons why the Ordinance was not valid in that it might otherwise impact on, for example, the law of torts in California. Methanex also relied on *Magda v. C.L. Benson* [536 F.2d 111] in support of the proposition that the Brea Ordinance could not render illegal a search by an FBI agent.
46. Methanex also submitted that, even if the Vind Documents had been obtained unlawfully, it would nonetheless be appropriate for the Tribunal to allow them into evidence in these arbitration proceedings. In support of this last submission, Methanex maintained that

the Vind Documents were admittedly authentic; the Vind Documents had probative value; and they went to the heart of the case in that they showed (for example) contact between Governor Gray Davis and Mr Vind's office. Methanex also submitted that it was necessary to balance the competing interests of the Disputing Parties. The USA had a huge budget; there was a mismatch of resources; and the USA had thwarted Methanex's other evidence gathering activities, including its attempts to obtain relevant evidence from third persons. At the same time, Methanex had done everything it could to remain within the law, as was shown by the photograph taken by Mr McAnish that supported Ms Morisset's evidence.

47. Methanex also submitted that in civil cases a court could still admit illegally obtained evidence if it was relevant and probative. In this respect, it relied on the decision of the Superior Court of New Haven, Connecticut, in *Xiukun Lin v. National Railroad Passenger Corp.* [2004 WL 113495], and two other cases: the decision of the Supreme Court of Louisiana in *Pullin v. Louisiana State Racing Commission* [484 So.2d 105], and the decision of the Court of Appeals in Maryland in *Sheetz v. Baltimore* [315 Md. 208, 553 A.2d 1281]. As to the relevance of the documents in the present case, Methanex took the Tribunal (by way of example) to three documents: Exhibits 56, 226 and 259 to the Second Amended Statement of Claim<sup>39</sup>.
48. **The USA's Submissions:** The USA submitted that Methanex's version of the facts relating to the method of document collection changed repeatedly; and it pointed to several major inconsistencies in Methanex's evidence. The USA made its legal submissions primarily by reference to Chapter 8.28 of the Brea Municipal Code, "Solid waste collection and salvage of recyclable materials". It relied in particular on paragraph 8.28.130(D), which provides:

*"No person, other than the owner thereof, the owner's agents or employees, or an officer or employee of the City or a permittee's agents or employees authorized for such purposes, shall tamper or meddle with any solid waste, green waste, or recyclable material receptacle or the contents thereof, or remove the contents thereof, or remove any receptacle from the location where the same shall have been placed for collection."*

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<sup>39</sup> *Id.*, pp. 1704-1722.

This criminal offence attracts serious penalties. The USA submitted that, pursuant to this Ordinance, it was illegal to remove documents that had been placed in the trash in the City of Brea without the owner's permission, save in the case of a trash collector or someone authorised to remove the trash by the owner or the City. This was the case even if the trash was located outside an office-building, whether in a parking lot or at the street curb. It also applied when the trash was collected from inside the closed trash area of an office-building.

49. Further, the purpose of the Ordinance was broader than mere sanitation; and in any event the general purpose was not decisive of the issue (relying on *State v. Boland* [800 P.2d 1112]). The USA also cited *Stephen Slesinger Inc. v. The Walt Disney Co.* [2004 WL 612818] as a recent example of the California Superior Court relying on and applying an ordinance (of the City of Burbank) similar to the Brea Ordinance. Hence it submitted, in the instant case, the means of obtaining the Vind Documents was unlawful.
50. So far as concerned Methanex's argument that the Brea Ordinance was somehow invalid under California law, it was not for this Tribunal to rule on whether the Ordinance was somehow unconstitutional or inconsistent with the law of California. In any event, the Ordinance was presumptively valid on its face; and Methanex had been unable to point to any case showing that the Ordinance was unconstitutional or inconsistent with California law. There had been no showing that the Ordinance covered an area of legislation expressly or impliedly reserved to the State. In addition, the authorities relied on by Methanex concerned the Fourth Amendment of the US Constitution or similar provisions in state constitutions, and were not relevant. The Fourth Amendment protected citizens against unlawful searches and seizures by the Government, and was intended to protect against the police overreaching and doing unlawful searches and seizures. The Brea Ordinance on its face did not cover the activities of the police. Questions as to reasonable expectation of privacy therefore did not arise. In this respect, the USA relied on *Katz v. United States* [389 US 347].
51. So far as concerned the impact of a trespass, the USA again relied on the *Slesinger* case. It also maintained that the cases relied on by Methanex - the *Ananda* case, the *Navratil* case and the *St Louis* case - all pointed to the existence of a trespass in the current case. The *Slesinger* case was also cited in support of the proposition that US civil courts have exercised a discretion to exclude illegally obtained material (it being accepted that the exclusionary rule developed in

the Fourth Amendment cases did not apply in civil cases).

52. As to Methanex's contentions that the Vind Documents should be allowed into evidence by the Tribunal even if illegally obtained by Methanex, the USA drew attention to the significant changes in Methanex's version of events; and it submitted that allowing the evidence would be contrary to the principle of equality of arms, in that the USA had proceeded on the assumption that no illegal means would be used to gather evidence. It was submitted that the USA had in no sense thwarted Methanex's collection of evidence: Methanex had made its applications to the California courts under 28 U.S.C. § 1782; the USA (as was its right) had opposed those applications; and Methanex had then withdrawn its applications before there could be any judicial decision. There was, in any event, no evidence that Mr Vind himself had ever been asked to provide testimony or to furnish documentary evidence by Methanex. The USA also made the point that Mr Vind could hardly supply original documents that were already in Methanex's own possession. The USA submitted that documents "illegally fished out of another man's trash" have no place in an international arbitration under a treaty such as NAFTA; and that it would act as a malign incentive if any NAFTA tribunal were to condone the collection and submission of evidence procured by illegal means.

### **9) The Tribunal's Decision and Reasons**

53. On 15th June 2004, having read the Vind Documents *de bene esse*, heard the relevant witnesses and considered the submissions of the Disputing Parties, the Tribunal decided to uphold the USA's challenge to the admissibility of the Vind Documents and ordered that they would form no part of the evidential record in the arbitration proceedings<sup>40</sup>. The reasons for the Tribunal's order are set out below.
54. In the Tribunal's view, the Disputing Parties each owed in this arbitration a general legal duty to the other and to the Tribunal to conduct themselves in good faith during these arbitration proceedings and to respect the equality of arms between them, the principles of "equal treatment" and procedural fairness being also required by Article 15(1) of the UNCITRAL Rules. As a general principle, therefore, just as it would be wrong for the USA *ex hypothesi* to misuse its intelligence assets to spy on Methanex (and its witnesses) and to introduce into evidence the resulting materials into this arbitration,

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<sup>40</sup> *Id.*, pp. 1729 and 1767-1768.

so too would it be wrong for Methanex to introduce evidential materials obtained by Methanex unlawfully.

55. The first issue here is whether Methanex obtained the Vind Documents unlawfully by deliberately trespassing onto private property and rummaging through dumpsters inside the office-building for other persons' documentation. Whilst certain of Methanex's agents may have held an honest belief that no criminal violation was committed under the City of Brea's Ordinance, given the legal advice allegedly proffered by the un-named DC law firm, the evidence demonstrates at least a reckless indifference by Methanex as to whether civil trespass was committed by its collection-agents in procuring the Vind Documents from Mr Vind's office-building in Brea. Once the USA demonstrated *prima facie* that the evidence which Methanex was proffering had been secured unlawfully, if not criminally, the burden of proof with respect to its admissibility shifted to Methanex, yet Methanex elected not to call the relevant partners of the unnamed law firm, whose testimony might have clarified the issue. The Tribunal is unable to see why these partners could not have testified before it. On the materials before the Tribunal, the evidence shows beyond any reasonable doubt that Methanex unlawfully committed multiple acts of trespass over many months in surreptitiously procuring the Vind Documents. Such unlawful conduct is not mitigated by the fact that the doors to the trash-area were not always closed but sometimes ajar: the entry into this area behind the doors remained unlawful; and Methanex made no attempt to distinguish between documents obtained when the doors were ajar and when they were closed.
56. The second issue is materiality. The Tribunal considered the content of the Vind Documents carefully, assisted by the submissions from Methanex's Counsel as to their relevance to its case. By the time of the main hearing in June 2004, the Vind Documents were of only marginal evidential significance in support of Methanex's case. There was other direct oral and documentary evidence relating to the meeting of 4th August 1998 between Mr Davis and ADM and other contacts between Mr Vind and Mr Davis; and the Vind Documents, as explained by Methanex's Counsel at the main hearing, could not have influenced the result of this case. Insofar as Methanex was seeking to discredit Mr Vind as a factual witness by using the Vind Documents during his cross-examination at the main hearing, it need only be said that, in all the circumstances, no such attempt could ever have succeeded in the manner originally intended by Methanex.

57. The third issue is the exercise of the Tribunal's general discretion under Article 25(6) of the UNCITRAL Rules to determine, in all the circumstances of this case, the admissibility of the evidence offered by Methanex. As already explained above, the Vind Documents comprise two different categories: (i) those documents collected by Methanex during the first period from July 1997 to August 1998 before these arbitration proceedings commenced; and (ii) those documents collected by Methanex during the second period from August 2000 to February 2001 after these arbitration proceedings were commenced in December 1999.
58. As regards the first category (eventually comprising Exhibits 52-60, 64, 66, 151, 153, 155, 159, 160 & 165) collected before these proceedings began, Methanex adduced no satisfactory evidence as to the lawfulness of the means it employed to obtain these documents from Mr Vind and his company. The relevant person, Mr Dunne, was not called by Methanex as a witness; and although Mr Dunne was made aware of these proceedings and could have testified (by video-link, if not in person), Methanex provided no satisfactory explanation for his absence as a material witness. As already noted above, no partner from the un-named DC law firm was called by Methanex. Moreover, Methanex's changing, incomplete and inconsistent explanations for its conduct left grave suspicions as to precisely what its agent or agents did to obtain these documents during this first period. In all the circumstances, the Tribunal decided that this documentation was procured by Methanex unlawfully; and that it would be wrong to allow Methanex to introduce this documentation into these proceedings in violation of a general duty of good faith imposed by the UNCITRAL Rules and, indeed, incumbent on all who participate in international arbitration, without which it cannot operate.
59. As regards the second category eventually comprising eight documents (Exhibits 217-219, 222-223, 226, 258 & 259), collected by Methanex during these arbitration proceedings, Methanex's conduct is wholly inappropriate, to say the least. There is no doubt on the evidence adduced by Methanex that this documentation was obtained by successive and multiple acts of trespass committed by Methanex over five and a half months in order to obtain an unfair advantage over the USA as a Disputing Party to these pending arbitration proceedings. The dates are illuminating: in August 2000, when this unlawful collection began, Methanex had made no application to the Tribunal for additional evidence from third persons; but when Methanex made its application, particularly at the procedural meet-

ing on 31st March 2003, Methanex was already in possession of certain of the original documents which it purportedly sought from others. In these circumstances, the Tribunal likewise decided that it would be wrong to allow Methanex to introduce this documentation into these proceedings in violation of its general duty of good faith and, moreover, that Methanex's conduct, committed during these arbitration proceedings, offended basic principles of justice and fairness required of all parties in every international arbitration.

60. Regrettably, the matter does not end there. It became apparent to the Tribunal from Methanex's evidence at the main hearing in June 2004 that Methanex was well aware of the meeting of 4th August 1998 between Mr Davis and ADM and its possible significance, long before these arbitration proceedings were commenced in December 1999. Accordingly, the Tribunal can no longer accept the premise that Methanex sought to amend its claim, eventually in the form of the Second Amended Statement of Claim, because of its own recent discovery of information "in the fall of 2000": see Methanex's explanation set out in the Preface above. At this late stage of these arbitration proceedings, the Tribunal cannot unmake the procedural order it made allowing Methanex to amend its claim, which was based materially on Methanex's explanation. Nonetheless the Tribunal can here record its disappointment that its procedural order was not then made with knowledge of the full facts and circumstances known at that time to Methanex itself. For the purpose of this Award, however, this further factor has played no part in the Tribunal's decisions or reasoning.

### **ANNEX 3 TO PART II CHAPTER I SELECTION OF SITE PHOTOGRAPHS EXHIBIT X8**

The upper photograph, taken from the street, shows Mr Vind's office-building on the right at 910 E Birch Street in Brea, California 92821. It also shows the steps leading from the street onto the property, arriving short of the two doors behind which the dumpsters were stored, i.e. the trash in the dumpsters was located inside the building and not in a public space.

The middle photograph shows the entrance to Mr Vind's office-building and (to its right) the doors behind which the dumpsters were stored. Mr Vind's office was on the second floor of the building.

The lower photograph shows the doors behind which the dumpsters were stored, in a closed position; and (to their right) the top of the steps leading down to the street.

## **PART III - CHAPTER A THE UNIVERSITY OF CALIFORNIA REPORT AND THE SCIENTIFIC EVIDENCE**

### **1) Introduction**

1. As recited above in Chapter II D, California Senate Bill 521, enacting the MTBE Public Health and Environment Protection Act of 1997 and signed into law on 8th October 1997, directed the University of California to conduct research on the effects of MTBE. To address the questions posed by the California Bill, the University of California conducted a competitive peer-reviewed request for proposals ("RFP"), with a total of six research projects being selected for funding. These six projects covered essentially the entire range of the eleven research topics specified by the California Bill and in the RFP. A grant of US \$500,000 was awarded by California to the investigators to assist in carrying out their work, which was in effect leveraged up by virtue of their existing work and facilities funded by governmental authorities<sup>1</sup>.
2. As regards impacts on human health and the environment, six of the California Bill's research topics bear mention here:

*Topic One:* An assessment of the risks and benefits to human health and the environment of MTBE and its combustion byproducts found in air, water and soil, and a comparison of those risks and benefits to ETBE, TAME and ethanol that could be used in lieu of MTBE in gasoline;

*Topic Two:* An assessment of available research and data on the impact of MTBE on human health and the environment in each state where MTBE has been used in gasoline at levels of 10% or greater, by volume, within the last five years;

*Topic Three:* An assessment of the risks to human health and the environment associated with MTBE leaking from underground and aboveground storage tanks, from surface watercraft and other sources of MTBE pollution in surface water bodies;

*Topic Four:* An analysis of current levels of MTBE in the state's drinking water, reservoirs, lakes and streams;

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<sup>1</sup> Professor Graham E. Fogg, Transcript Day 5, pp. 1232; 1235-1236.

*Topic Five:* An evaluation of the costs and effectiveness of treatment technologies available to remove MTBE from surface waters, ground-water and drinking water; and

*Topic Ten:* An evaluation of the scientific peer-reviewed research and literature on the human health and environmental effects of MTBE, as well as any original research necessary to provide the information specified in Topics 1 to 9 inclusive<sup>2</sup>.

In addition to the mandated research topics in the California Bill, the University of California investigators specifically sought to develop a set of policy options for the California legislature based on scientific principles and a cost-benefit analysis.

## 2) The University of California Report

3. In November 1998, only days after Governor Davis's election, UC and the UC Toxic Substances Research & Teaching Program released the five volume, 600-page Report "Health & Environmental Assessment of MTBE" (the "UC Report"). The UC Report comprised 17 separate papers compiled by more than 60 researchers with a separate volume providing a summary of the whole, together with the resulting recommendations. A number of the UC Report's principal findings and key recommendations are set out below. In the interests of precision, this section summarises or closely paraphrases the relevant passages of the UC Report (likewise, in section 5 below, the evidence of the Disputing Parties' scientific witnesses is summarised or closely paraphrased).
4. **Reformulated Gasoline ("RFG"):** Beginning in the late 1980s, studies were undertaken to identify ways in which gasoline could be reformulated to help achieve certain air quality goals<sup>3</sup>. Based on studies with older vehicles, it was determined that adding oxygenated organic compounds, such as alcohols and ethers to conventional gasoline, resulted in a reduction in the emissions of carbon monoxide and other products of incomplete combustion. Subsequent studies identified several ways in which gasoline could be reformulated. Compared to conventional gasoline, RFG has reduced vapour pressure (to lower evapora-

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<sup>2</sup> Arturo Keller et al., Executive Summary, Recommendations, Summary, in UC Report Vol. I: Summary & Recommendations, at pp. 9-10 (4 JS tab 36) (hereinafter Keller et al., UC Report Vol. 1).

<sup>3</sup> *Ibid.*

tive emissions), reduced sulphur content (to prevent poisoning of catalytic converters) and reduced aromatic and benzene content (to decrease evaporative and exhaust emissions of these compounds)<sup>4</sup>. Reformulated fuel may or may not include oxygenated compounds; the term "reformulated gasoline" does not of itself imply the presence of oxygenates<sup>5</sup>.

5. **Two Primary Types of RFGs:** Federal RFG and California Phase II RFG ("CaRFG2") constitute the two primary types of reformulated gasoline. Federal RFG requires a minimum oxygen content of 2.0% by weight, but does not specify what type of oxygenate must be used. CaRFG2 specifies an oxygen content of 1.8 to 2.2% by weight, also with no mandate for any particular oxygenate<sup>6</sup>. Oxygenate compounds used in RFG can contaminate water sources and also result in air emissions specific to these additives<sup>7</sup>.
6. **California Phase II Reformulated Gasoline:** The use of CaRFG2 since June 1996 has resulted in reductions in the emissions of various air pollutants including benzene, a known human carcinogen<sup>8</sup>. These reductions in pollutant emissions have resulted in human and environmental health benefits.
7. **MTBE:** Although gasoline refiners have used a variety of oxygenates - MTBE, other ethers and ethanol - to meet the RFG and CaRFG2 oxygen content requirements in California, most have chosen to use MTBE<sup>9</sup>. It was the "oxygenate of choice" in California<sup>10</sup>.
8. **Modern Vehicles:** Improvements in the emission control technology used in newer cars have significantly reduced emissions of air pollutants<sup>11</sup>. As a result, MTBE and other oxygenates "have no significant effect on exhaust emissions from advanced technology vehicles"<sup>12</sup>. Also, "there is no statistically significant difference in the emissions reduction of benzene as between oxygenated [whether by MTBE or ethanol] and non-oxygenated RFGs that meet all other CaRFG2 standards. Thus, there is no significant additional air quality benefit to the use of oxygenates such as MTBE in reformulated gasoline relative to alternative CaRFG2 non-oxygenated formulations"<sup>13</sup>.

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<sup>4</sup> *Ibid.*

<sup>5</sup> Keller et al., UC Report Vol. 1, at 11 (4 JS tab 36).

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*, pp. 16-18.

<sup>8</sup> *Id.*, pp. 15, 18.

<sup>9</sup> *Id.*, p. 15.

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*, p. 11.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

9. **Water Contamination:** There are significant risks and costs associated with water contamination due to the use of MTBE. MTBE is highly soluble in water and will transfer readily to groundwater from gasoline leaking from underground storage tanks ("USTs"), pipelines and other components of the gasoline distribution system. In addition, the use of gasoline containing MTBE in motor boats, particularly those using older two-stroke engines, results in the contamination of surface water reservoirs<sup>14</sup>.
10. **California's Water Resources:** It is clear that California water resources are being placed at risk by the use of MTBE in gasoline. MTBE has been detected in several water supply systems, which have shut down the contaminated sources, resorting to alternative supplies or treatment. Since both groundwater wells and surface water reservoirs have been contaminated, alternative water supplies may not be an option for many water utilities. If MTBE continues to be used at current levels and more sources become contaminated, the potential for regional degradation of water resources, especially groundwater basins will increase<sup>15</sup>. Severity of water shortages during drought years will be exacerbated. California's water resources are placed at risk by the use of MTBE.
11. **MTBE Health Risks:** For the general population, the risk of exposure to MTBE through ingestion of MTBE-contaminated water is currently low. MTBE exposure through inhalation is also likely to be below health-threatening levels, except for occupational workers such as gasoline station attendants and auto-mechanics. However, there are important data gaps in our understanding of the acute and chronic toxicity of MTBE<sup>16</sup>. Little or no research is currently being conducted that directly addresses these issues. Whilst MTBE risks to human health may be low, they are uncertain.
12. **Treatment Costs:** The cost of treatment of MTBE-contaminated drinking water sources in California has the potential to be enormous. In addition, the costs of remediating UST and pipeline leaks and spills could be in the order of tens to hundreds of millions of US dollars per year<sup>17</sup>. There are other significant costs to the economy, which may be in the tens of millions of US dollars per year, in terms

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<sup>14</sup> *Id.*, pp. 11-12.

<sup>15</sup> *Id.*, p. 12.

<sup>16</sup> *Id.*

<sup>17</sup> *Id.*

of monitoring of surface water sources for MTBE and in potential losses in recreational income to surface water reservoirs that ban or restrict the use of gasoline-powered boats. The treatment costs of MTBE-contaminated drinking water is potentially enormous.

13. **Cost Benefit Analysis:** An economic analysis of the benefits and costs associated with the three formulations of CaRFG2 gasoline (non-oxygenated, ethanol oxygenated and MTBE-oxygenated) indicates that non-oxygenated gasoline achieves air quality benefits at the least cost, followed by CaRFG2 with ethanol. The water treatment costs associated with CaRFG2 with MTBE makes this choice the most expensive gasoline formulation. When all costs are considered, net annual costs are estimated to be in the order of US \$1-3 billion, due primarily to the costs of treating contaminated water supplies, higher fuel prices and lower fuel efficiencies<sup>18</sup>.
14. **Economics:** From a purely economic perspective, the UC Report concludes it would be best to effect a transition to non-oxygenated CaRFG2, but this is not thought to be a viable option as a fuel oxygenate content is mandated by federal law<sup>19</sup>. However, because of the lessons learned from the MTBE story - that the addition of any chemical compound to the environment in quantities that constitute a significant fraction of the total content of gasoline may have unexpected environmental consequences - the UC Report recommends "a full environmental assessment of any alternative to MTBE in CaRFG2, including the components of CaRFG2 itself, before any changes are made in California state law."<sup>20</sup>
15. **Phase-Out of MTBE:** Although many communities in California were seeking to ban the use of MTBE in gasoline, the UC researchers consider that an immediate ban would result in a significant disruption in gasoline production and drive up the price of gasoline paid by consumers<sup>21</sup>. Accordingly, rather than any immediate ban on MTBE, these researchers recommend that consideration be given to phasing out MTBE over a period of several years and that "refiners be given flexibility to achieve CARB's air quality objectives by modifying the caps in the CaRFG2 specifications [so] as to allow wide-scale production of non-oxygenated RFG. Using CARB's Predictive Model as a

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<sup>18</sup> Id.

<sup>19</sup> Id.

<sup>20</sup> Id., pp. 12-13.

<sup>21</sup> Id.

guideline, refiners [would be able to] find the most cost-effective formulation for each region and season, without assuming the liability and risks that MTBE poses to California's water supplies"<sup>22</sup>.

16. **The Transition Phase:** A number of policy recommendations are suggested with a view to reducing the costs of using MTBE while protecting water supplies, should an MTBE phase-out be required. Two bear particular mention here. The first was a recommendation that California seek a waiver of the federal requirement that RFG sold in California have an oxygen content. This would allow the sale of nonoxygenated CaRFG2 in all areas<sup>23</sup>. The second was a recommendation for the assessment of the environmental impact of using other oxygenates such as ethanol. However, because of the potential adverse health effects associated with the incomplete combustion products of ethanol, the UC Report concludes that further study of the combustion products and their potential health effects was required before it could be recommended that ethanol be substituted for MTBE on a large scale. If ethanol was found to provide a net energy savings and have minimal environmental impact, then an increase in the availability of ethanol as a potential oxygenate was recommended<sup>24</sup>.

### **3) Public Hearings on the University of California Report**

17. Public hearings on the UC Report were held on 19th February 1999 in Diamond Bar, California, and on 23rd and 24th February 1999 in Sacramento, California. At these hearings, the authors of the UC Report presented their findings<sup>25</sup>; and government officials and members of the public (including MTBE and methanol producers) had an opportunity to ask questions and present oral testimony.
18. Those testifying, amongst others, included persons affected by MTBE water contamination, as well as individuals associated with the chemical and oil industries. The testimony received at these public hearings indicated broad-based support for the finding by the University of California that MTBE usage in gasoline constituted a serious threat to California's drinking water and that a ban on the use of MTBE in California RFG was warranted. Of the 109 persons who testified, 69 were in favour of banning, 23 were against and 17

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<sup>22</sup> *Id.*, p. 13.

<sup>23</sup> *Id.*

<sup>24</sup> *Id.*, p. 14.

<sup>25</sup> Transcript of UC Report Hearing at Diamond Bar, at pp. 18-87, 19th February 1999 (15 JS tab 22 at 581); Transcript of UC Report Hearing at Sacramento, at pp. 2-81, 23rd February 1999 (15 JS tab 22 at 782).

testified on other issues<sup>26</sup>.

19. California federal agencies were given an opportunity to review and comment on the UC Report. In late December 1998 the US Geological Survey congratulated the University of California faculty on the Report, noting that it contained an impressive amount of information and research that would prove useful in addressing the use of MTBE and other oxygenate additives to gasoline<sup>27</sup>. The US Department of Health and Human Services ("DHHS") commented at the same time.<sup>28</sup> Thereafter, on 22nd February 1999 CARB provided its comments to the California Environmental Protection Agency ("Cal EPA")<sup>29</sup>. Like the US Geological Survey, both the DHHS and CARB were generally supportive of the UC Report<sup>30</sup>.

#### 4) The California Regulatory Chronology

20. California's legislative interest in MTBE and ethanol did not start with the California Bill in October 1997. As related in Chapter III B below, California introduced legislative incentives for the use of ethanol in 1983, prior to the commonplace use of MTBE in California; and with such use from 1990 onwards, there were a number of legislative and regulatory proposals considered by California in regard to MTBE prior to both the California Bill and the election of Governor Gray Davis.
21. **The 1999 Executive Order:** On 25th March 1999, approximately four months after the publication of the UC Report and one month after the public hearings, Governor Davis issued the 1999 Executive Order. The basis for the order was stated as follows: "The findings and recommendations of the U.C. report, public testimony and regulatory agencies are that, while MTBE has provided California with clean air benefits, because of leaking underground fuel storage tanks MTBE poses an environmental threat to groundwater and drinking water"<sup>31</sup>.

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<sup>26</sup> Transcript of UC Report Hearing at Sacramento, 23rd February 1999 (15 JS Tab 22 at 913-1017).

<sup>27</sup> US Geological Survey, Comments on Health and Environmental Assessment of MTBE, p. 2 (18 JS 148).

<sup>28</sup> US Dep't of Health & Human Servs., Comments on Health and Environmental Assessment of MTBE (24th December 1998) (18 JS 145).

<sup>29</sup> US Dep't of Health & Human Servs., Comments on Health and Environmental Assessment of MTBE (18 JS 145).

<sup>30</sup> Cal. Air Resources Bd., Comments on Health and Environmental Assessment of MTBE, (16 JS 25).

<sup>31</sup> 1999 Executive Order, preamble (1 JS Tab 1 (c)).

22. In accordance with those findings and recommendations, by the 1999 Executive Order, Governor Davis certified that "on balance there is significant risk to the environment from using MTBE in gasoline in California".<sup>32</sup> The 1999 Executive Order also tasked the California Energy Commission ("CEC") in consultation with CARB, with developing "a timetable by July 1, 1999 for the removal of MTBE from gasoline at the earliest possible date, but not later than December 31, 2002"<sup>33</sup>.
23. The 1999 Executive Order next directed CARB to request an immediate waiver of the federal reformulated gasoline oxygenate requirement from the Administrator of the US EPA<sup>34</sup> (a step recommended in the UC Report). Such a waiver, if granted, would have permitted California to use RFG that achieved air quality requirements without any oxygenate.
24. The 1999 Executive Order also directed several California agencies to prepare reports on the environmental and health affects of using ethanol as an oxygenate<sup>35</sup> (again, a step recommended in the UC Report). These reports were to be peer-reviewed and presented to the Environmental Policy Council for its consideration by 31st December 1999<sup>36</sup>.
25. In the certification made by Governor Davis at the time of the 1999 Executive Order<sup>37</sup>, Governor Davis noted that he had ordered the study of ethanol having "learn[ed] a lesson from [California's] experience with MTBE and [recognising the necessity of] carefully assess [ing] the environmental impacts of other oxygenates such as ethanol before committing to its wide-spread use in California's gasoline supply".
26. ***The 1999 Requested Waiver:*** On 12th April 1999, Governor Davis wrote to US EPA Administrator Carol Browner requesting a waiver of the oxygenate requirement in the federal RFG program<sup>38</sup>. Governor

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<sup>32</sup> *Id.*

<sup>33</sup> 1999 Executive Order, para. 4 (1 JS Tab 1 (c)).

<sup>34</sup> *Id.*, para. 2.

<sup>35</sup> *Id.*, para. 10.

<sup>36</sup> 1999 Executive Order, para. 10 (1 JS Tab 1 (c)).

<sup>37</sup> Certification of Human Health or Environmental Risks of Using Gasoline Containing MTBE in California (16 JS Tab 35 at 1289).

<sup>38</sup> Letter From Governor Davis to Carol M. Browner, Administrator, US Environmental Protection Agency, 12th April 1999 (16 JS tab 65).

Davis made the point that many California refineries had the capability of producing significant amounts of gasoline that provide all of the required emission reductions without using MTBE or any other oxygenate. He further noted that California's RFG regulations accomplish the needed emission reductions without requiring a minimal level of oxygen. Governor Davis pressed California's case for a waiver with a second letter to Administrator Browner on 15th December 1999<sup>39</sup> and a letter to President George W. Bush on 22nd May 2001<sup>40</sup>.

27. The US EPA denied California's request for the requested waiver on 12th June 2001. In response, on 13th August 2001, Governor Davis announced he was challenging the denial in the federal court<sup>41</sup>. On 17th June 2003, the United States Federal Court of Appeals for the Ninth Circuit issued a decision holding that the US EPA had abused its discretion by denying California's waiver request without having evaluated the effect of an oxygenate waiver on California's efforts to comply with particulate-matter standards<sup>42</sup>.
28. Based on the Ninth Circuit's decision, Governor Davis stated his hope that "the EPA will (now) take a hard look at this court decision, realize they were wrong and give California what it needs: the ability to make gasoline with or without oxygenates as conditions warrant"<sup>43</sup>. Approximately two weeks later, on 6th August 2003, Governor Davis wrote to Acting EPA Administrator, Marianne Horinko, reiterating California's request for a waiver in the light of the court's decision<sup>44</sup>.
29. **California Senate Bill 989:** On 8th October 1999, Governor Davis signed into law California Senate Bill 989. The Bill was intended to place into statute the Executive Order D-5-99 issued by Governor Davis on 26th March 1999 and to enact several other provisions of law designed to protect groundwater and drinking water from MTBE contamination<sup>45</sup>. The Bill had been proposed by the Association of

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<sup>39</sup> 16 JS Tab 66 at 1581.

<sup>40</sup> 16 JS Tab 67 at 1583.

<sup>41</sup> Press Release, Office of the Governor of Cal., Governor Davis Sues US EPA over Gasoline Additive, 13th August 2001 (17 JS tab 117).

<sup>42</sup> *Davis v. EPA*, 336 F.3d 965, 969 (9th Cir. 2003) (16 JS Tab 41 at 1331).

<sup>43</sup> Press Release, Office of Governor Davis, Statement Regarding Federal Court's MTBE Ruling, 17th July 2003 (17 JS tab 116).

<sup>44</sup> Letter From Governor Davis to Marianne Lamont Horinko, Acting Administrator, US Environmental Protection Agency, 6th August 2003 (16 JS Tab 68 at 1585).

<sup>45</sup> SB 989, Senate Bill - History - 18 JS Tab 128 at 2512.

California Water Agencies, an association of 400 plus public agencies and mutual water companies responsible for most of the water delivered to California's farmers, businesses and cities<sup>46</sup>.

30. ***The 1999 Cal EPA Ethanol Report:*** In December 1999 Cal EPA issued its report, entitled "Health and Environmental Assessment of the Use of Ethanol as a Fuel Oxygenate" which had been prepared as required by Governor Davis' Executive Order (the "1999 Cal EPA Report")<sup>47</sup>. This report was co-written by several agencies within the Cal EPA, including CARB, the State Water Resources Control Board ("SWRCB") and the Office of Environmental Health Hazard Assessment ("OEHHA"). The purpose of the report was to address Topic 10 of the Executive Order which had directed that CARB and SWRCB: "shall conduct an environmental fate and transport analysis of the health risks of ethanol in air, surface water, and groundwater ..." and that OEHHA "shall prepare an analysis of the health risks of ethanol in gasoline, and any resulting secondary transformation products".
31. As a result of the 1999 CalEPA Ethanol Report, the California Environment Policy Commission found that, although further research was warranted, the impacts associated with the use of ethanol would be significantly less and more manageable than those associated with continued use of MTBE<sup>48</sup>. As regards the potential health risk of ethanol in gasoline, the report concluded, inter alia, that "there are no substantive differences in the public health impacts of the different non MTBE fuel formulations [it] considered". In particular, "although replacement of MTBE by either ethanol or non-oxygenated fuel is expected to have some benefits in terms of water contamination, these cannot be quantified at present. From our analysis, these substitutions have no substantial effects on public health impacts of air pollution"<sup>49</sup>. As regards the air quality impacts of the use of ethanol in California Reformulated Gasoline, Cal EPA's Air Resources Board concluded that "so long as CaRFG3 regulations addressed the potential for ethanol to increase evaporable emissions and cause more rail and truck traffic, the substitution of ethanol and alkytes for MTBE in California's fuel supply

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<sup>46</sup> Association of Cal. Water Agencies, More About ACWA, at [http://www.acwanet.com/aboutacwa/more\\_about\\_acwa.asp](http://www.acwanet.com/aboutacwa/more_about_acwa.asp).

<sup>47</sup> 8 JS 180 through to 9 JS 184.

<sup>48</sup> Summ-1 (25 JS Tab 15).

<sup>49</sup> Volume 1, pp. 1-22 (25 JS Tab 6).

will not have any significant air quality impacts"<sup>50</sup>. And while the authors did not consider ethanol to be a carcinogen by inhalation, they concluded "even if one accepts that ethanol should be regarded as a human carcinogen by the inhalation route ... the risks predicted on this basis from ethanol are negligible"<sup>51</sup>.

32. **The 2000 CaRFG3 Regulations:** On 16th June 2000, following a public hearing on 9th December 1999, CARB adopted the California Reformulated Gasoline Phase III Standards ("CaRFG3") which included a prohibition on the use of MTBE in gasoline beginning 31st December 2002<sup>52</sup>. CARB also required sulphur and benzene levels in California gasoline to be reduced<sup>53</sup>. These regulations became effective on 2nd September 2000.
33. In its resolution granting approval to adopt the regulations, CARB found that:

*"MTBE is highly soluble in water and will transfer to ground-water faster, farther and more easily than other gasoline constituents such as benzene when gasoline leaks from underground storage tanks and pipelines; even upgraded storage tanks are not leak-proof and future leaks from a small percentage of the thousands of gasoline storage tanks in the state will continue in the future; MTBE has been detected in the public drinking water supplies in South Lake Tahoe, Santa Monica, Los Angeles, San Francisco, Santa Clara, and other locations;*

*Along with toxicological concerns, low levels of MTBE in drinking water can be tasted and smelled by susceptible individuals with a taste characterised as solvent-like, bitter, and objectionable; the people of California will not accept drinking water in which they can taste MTBE;*

*Accordingly, the threat posed by MTBE to California's potential drinking water supplies, and the high estimated costs for the continuing costs of cleaning up MTBE groundwater*

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<sup>50</sup> Volume 3, Air Quality Impact of the Use of Ethanol in California Reformulated Gasoline, p. 3 (13A JS Tab 8).

<sup>51</sup> Volume 5, Response to Comments, p. B-32 (25 JS Tab 6).

<sup>52</sup> Cal. Code Regs. Tit. 13, § 2262.6(a) (2000) (14 JS tab 10, 18).

<sup>53</sup> Id., § 2262.3(a).

*contamination make it necessary to prohibit the use of MTBE in California gasoline being supplied from production and import facilities on or after December 31, 2002 - the appropriate deadline identified by the CEC ...".<sup>54</sup>*

The CaRFG3 regulations went beyond merely banning MTBE. They also provided that only ethanol could be used as an oxygenate in California gasoline at §2262.6(c)(i).

34. **The 2002 Executive Order:** On 14th March 2002 Governor Davis issued Executive Order D-52-02, which directed CARB to take action to postpone the ban on the use of MTBE in gasoline by one year (the "Postponement Order")<sup>55</sup>. The Postponement Order notes in its preamble that the Governor so acted in response to the Federal Government's denial of California's request for a waiver of the federal oxygenate requirement<sup>56</sup>. The Postponement Order also notes that the current production, transportation and distribution of ethanol is insufficient to allow California to meet federal requirements and to eliminate the use of MTBE on 1st January 2003. The Governor concluded that "[a]s a result [of the denial of California's waiver request], if use of MTBE is prohibited January 1, 2003, California's motorists will face severe shortages of gasoline, resulting in substantial price increases ..."<sup>57</sup>.
35. By press release of 15th March 2002, Governor Davis issued a public statement in which he noted that he was unwilling to maintain the original effective date of the ban when to do so would harm California's economy and motorists and would benefit the ethanol industry: "I am not going to allow Californians to be held hostage by another out-of-state energy cartel ..."<sup>58</sup>.
36. **The 2002 Draft and 2003 Amended CaRFG3 Regulations:** On 25th October 2002 CARB released for public consideration proposed amendments to the CaRFG3 regulations "to refine the prohibitions of MTBE and specified other oxygenates in California gasoline starting December 31, 2003" (the "Conditional Prohibition"). A hearing date to take comments on the Conditional Prohibition was set for 12th December 2002. As part of the Conditional Prohibition, start-

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<sup>54</sup> Cal. Air Resources Bd., Res. 99-39, at pp. 6-7 (16 JS tab 24).

<sup>55</sup> 2002 Cal. Exec. Order D-52-02 (16 JS tab 46).

<sup>56</sup> Id., preamble.

<sup>57</sup> Id. (emphasis added).

<sup>58</sup> Press Release, Office of Governor Davis, Governor Davis Allows More Time for Ethanol Solution, 15th March 2002 (17 JS tab 115).

ing on 31st December 2003, changes were proposed to §2262.6 (c) (i) and (iv) to change respectively "ether" to "oxygenate" and to include "methanol" in the list of covered oxygenates prohibited in Section 2262.6(c)(1), (2) & (3). On 8th November 2002, one month before the hearing date to consider the Conditional Prohibition, CARB (in response to the Postponement Order) postponed the prohibition of MTBE in California gasoline from 31st December 2002 until 31st December 2003. Finally, as more fully recited in Chapter II F above, CARB adopted the Conditional Prohibition on 1st May 2003.

### 5) The Disputing Parties' Scientific Witnesses [pg 175]

37. ***Methanex's Case:*** In summary, starting with the UC Report, Methanex contends that this constituted a deeply flawed and inadequate foundation for the US measures<sup>59</sup>. Methanex contends that at the time Governor Davis effectively banned MTBE by signing the Executive Order in March 1999, the UC Report was known to be "under funded, incomplete, and simply wrong on many critical points"<sup>60</sup>. Moreover, even aside from inadequate funding, the authors of the UC Report "were not given enough time to do the full comparative analysis with which they [had been] charged."<sup>61</sup> The UC Report was "supposed to evaluate all competing oxygenates, but instead singled out one - MTBE"<sup>62</sup>. The UC Report failed to report any analysis of ethanol or other competing oxygenates such as methanol and TAME. The UC study also bungled the cost-benefit analysis by including "sunk costs that would have to be incurred whether or not MTBE was banned. Worse, although this defect was well known in 1999, the UC researchers refused to change their analysis, and Governor Davis simply ignored all these defects"<sup>63</sup>. Also, the conclusion that the net costs associated with oxygenated gasoline were lower for ethanol than MTBE did not take into consideration federal ethanol subsidies and tax incentives offered by California for in-state ethanol production<sup>64</sup>. The UC Report also miscalculated future leakage rates and clean-up costs; and it had been heavily criticised by the US Government itself.
38. Methanex also argues that, in any event, many of the UC Report's findings militated against a ban of MTBE in favour of ethanol. The UC

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<sup>59</sup> Second Am. Claim, paras. 111-117; Reply, paras. 75-83.

<sup>60</sup> Reply, para. 75.

<sup>61</sup> Second Am. Claim, para. 112.

<sup>62</sup> Reply, para. 76.

<sup>63</sup> Id., para. 78.

<sup>64</sup> Id.

Report made clear that: the impact of MTBE on human health could not be "substantiated"; toxicity to fish and other aquatic organisms was very low; and its use in gasoline did not increase the likelihood or prevalence of leaks from USTs or negatively affect the performance or longevity of motor vehicles. The UC Report also found that replacing MTBE with ethanol might not change the need to treat water supplies contaminated with oxygenates and therefore would not alleviate all the perceived problems of MTBE; that ambient concentrations of acetaldehyde and formaldehyde, both air toxics and known carcinogens, were expected to increase if ethanol was substituted for MTBE as the oxygenate of choice; that it was crucial that ethanol or any other substitutes for MTBE be further evaluated before they were widely used; and that to replace MTBE with an untested substitute would only compound the current problem.

39. **The USA's Case:** In response, the USA contended that the UC Report reflected "substantial scholarship".<sup>65</sup> On the USA's case, the UC Report constituted a thorough, objective, multi-disciplined and academically sound scientific foundation for the measures thereafter adopted by California<sup>66</sup>. Its principal conclusions and recommendations suggested really only one outcome. The UC Report considered there to be significant risks and costs associated with water contamination due to the use of MTBE and that the danger of surface and groundwater contamination would increase if the use of MTBE were to continue at then-current levels. It concluded that the cost of treatment of MTBE-contaminated drinking water sources in California could be enormous. Finally, to remedy the serious problems facing California's water supply, it recommended that legislative consideration be given to phasing out MTBE in gasoline over several years.
40. Although the California Bill had expressed a desire that the UC Report also compare the impacts and benefits of MTBE to those for ETBE, TAME and ethanol, the fact that the UC Report did not provide a detailed comparison with other potential oxygenate additives in no way undermined its firm support for the action that Governor Davis took in his 1999 Executive Order. Data from many sources confirm that MTBE posed a higher risk to groundwater than other gasoline constituents. Also, the inclusion of sunk costs in the cost-benefit analysis in no way calls into question the adequacy of the UC Report as a whole. Moreover, because this error was noted in the public comments on the UC Report, the facts available to the

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<sup>65</sup> Am. Defense, para. 54.

<sup>66</sup> Am. Defense, paras. 53-54.

Governor on which to base his decision were known to be correct at the time. Finally, research results issued more or less contemporaneously with the UC Report confirm that it was no pretextual exercise. By July 1999 the US EPA's Blue Ribbon Panel on Oxygenates in Gasoline, a federal initiative, had issued similar conclusions and recommendations, as had the Northeast States for Co-ordinated Air Use Management.

41. **Expert Scientific Testimony:** The Disputing Parties tendered a series of expert reports on the scientific issues relating to MTBE. These focussed primarily on the strengths and weaknesses of the UC Report and a number of its constituent parts. In most cases, reply expert reports were also filed by the Disputing Parties. In these reports, as requested by the Tribunal, the experts commented on each other's analyses and opinions. The resulting expert testimony contained in these many reports is extremely important in this arbitration, going to the heart of the question of whether the US measures, as alleged by Methanex, constitute a "sham environmental protection in order to cater to local political interests or in order to protect a domestic industry"<sup>67</sup>.
42. For the purpose of this Award, we summarise below the principal points and conclusions of the experts in this area. In order not to lengthen what is necessarily a long document, we refrain from noting every point made, especially in the reply reports. We intend no discourtesy in this regard to the experts; and we have nonetheless considered all of their expert evidence, as well as the oral testimony given by the USA's experts at the main hearing under cross-examination by Methanex (Methanex's experts did not testify orally at the main hearing because the USA did not require their attendance for cross-examination).
43. **Methanex's Expert Witnesses:** Methanex introduced in evidence nine expert reports concerning the UC Report. Three were prepared by Exponent (in one case working with Applied Engineering Science or "AES") - the first dated November 2002, the second and third dated January 2003; two by Professor Gordon Rausser - dated 31st January 2003 and 19th February 2004; two by Professor C. Herb Ward - dated 31st January 2003 and 19th February 2004; and two by Dr Pamela Williams - the first undated, and the second dated 19th February 2004. We summarise the effect of the testimony of these witnesses below.

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<sup>67</sup> Reply, para. 147; Transcript Day 1, pp. 246-247 (Mr Dugan for Methanex).

44. **The Exponent Reports:** Exponent (together with AES) was retained initially to evaluate the current status of UST/LUSTs in California and the relationship of recent UST regulations to the frequency of tank system releases and MTBE detections in California's groundwater sources of drinking water<sup>68</sup>. Their work also looked at the relationship between the use of watercraft with two-stroke engines on surface water in California and the detection of MTBE in these sources of drinking water. Exponent's November 2002 Report concluded that the weight of the evidence indicates that there has been vastly improved management of USTs (and regulatory compliance) in California since 1998; and that the number of new LUST's identified has decreased with time and is now small. Consequently, the frequency with which MTBE is detected in drinking water sources in California during this time period is also low, generally less than 1% in groundwater sources, with a noticeable decrease in percent detects in surface water since 1998, following the restrictions on the use of watercraft with two-stroke engines. Since 1996, the detected concentrations of MTBE in sample drinking water sources in California generally have been less than the State's primary (health-based) Maximum Contaminate Level ("MCL") of 13 parts per billion (ppb) and secondary (aestheticbased) MCL of five ppb. It is also clear that MTBE is detected less often and at lower concentrations than several other organic chemicals found in California's drinking water sources<sup>69</sup>.
45. This expert report also notes that more recent studies conducted in California confirm that the salient issue in limiting gasoline contamination of drinking water is not a ban on MTBE, but rather improvements in the enforcement of UST standards and other regulations aimed at preventing petroleum releases<sup>70</sup>. It points to numerous studies which have been undertaken in the European Union with respect to USTs, LUSTs and MTBE, all of which have concluded that prevention of tank systems leaks, rather than a ban on MTBE as a gasoline oxygenate, is the primary method to prevent fuel releases into the environment<sup>71</sup>.
46. Although MTBE has received considerable attention in California, there are currently no statewide monitoring databases that track whether drinking water sources have been closed due to the pres-

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<sup>68</sup> Exponent, Evaluation of UST/LUST Status in California and MTBE in Drinking Water, November 2002, Second Am. Claim, Exhibit E.

<sup>69</sup> *Id.*, p. xiv.

<sup>70</sup> *Id.*

<sup>71</sup> *Id.*

ence of MTBE. Because of these data limitations, it is not possible to provide an exact estimate of how many drinking water sources in California have been closed due to MTBE; but this number is likely to be small; and closure decisions may have little to do with the presence of measured concentrations of MTBE at these sources. Finally, Exponent concludes that "if the trends observed above become more definitive over time, it will be even more apparent that banning MTBE's use in gasoline is not necessary to protect groundwater and surface-water resources when adequate regulations are implemented and enforced"<sup>72</sup>.

47. In Exponent's "First Report of January 2003", Exponent presents an evaluation of the UC Report, focussing on several sections that Exponent concludes limit the UC Report's ability to support its own conclusions and, more importantly, to support Governor Davis' 1999 decision effectively to ban MTBE<sup>73</sup>. Exponent identifies five primary limitations to the UC Report.
48. First, the UC Report does not provide an adequate assessment of the potential risks or benefits to human health or the environment associated with any alternatives to the use of MTBE in gasoline. In particular, the Report tends to underestimate the potential benefits of MTBE and to over-simplify (or ignore) potential hazards associated with ethanol and non-oxygenated fuels. Therefore, any statements that the potential risks are lower and/or the potential benefits are higher for alternatives to MTBE cannot be supported. As a result, the UC Report's recommendation and the Governor's subsequent order to phase out MTBE were premature and not justified<sup>74</sup>.
49. Second, the UC Report's list of recommendations is too limited in scope, having excluded simpler and more obvious solutions to addressing potential impacts of MTBE (and other gasoline constituents) on drinking water resources. For example, even though the Report acknowledged that MTBE detections in groundwater were a direct result of leaking underground gasoline storage tanks, it did not offer any recommendations to address the leaking tank problem such as enforcement of existing laws. By limiting their discussion and recommendations to a single option (i.e. phase out of MTBE), the UC authors failed to provide the Governor with adequate data upon

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<sup>72</sup> Id.

<sup>73</sup> Exponent, Evaluation of the University of California Report Titled "Health & Environmental Assessment of MTBE", January 2003 (12 JS tab C).

<sup>74</sup> Id., p. 3.

which to base an informed decision<sup>75</sup>.

50. Third, the UC Report provided an inaccurate assessment of the then-current and potential future impacts of MTBE on drinking water resources in California. Specifically, it over-simplified the data available at the time, down played the bias in the data with respect to characterising current conditions, and inappropriately extrapolated the data to estimate future conditions state wide. In reality, the available monitoring data (then and now) show that MTBE has not had a widespread or worsening impact on public drinking water sources in California. Therefore, the Report's conclusion that there were "significant risks" associated with water contamination due to the use of MTBE, and the Governor's subsequent reliance on this conclusion, was not based on a reasonable interpretation of the available data<sup>76</sup>.
51. Fourth, the Report did not provide an adequate assessment of the potential human health risks associated with MTBE in gasoline. In particular, although it presented over 200 pages of toxicology data and estimated broad ranges of human exposures to MTBE, the UC Report did not characterise what these findings meant - in terms of actual risks to human health. Therefore, any statements or inferences that MTBE exposures in California pose a public health risk cannot be supported by the data presented<sup>77</sup>.
52. Fifth, its other shortcomings notwithstanding, the UC Report's Summary and Recommendations contains numerous negative conclusions that are not substantiated by the supporting documentation. These statements have the effect of implying at the outset that the use of MTBE in gasoline has resulted in a dire situation that requires immediate action, rather than careful consideration and further study of the issues raised in the Report (Volume I, page 17).
53. In Exponent's "Second Report of January 2003", Exponent goes beyond the UC Report and presents an evaluation of the 1999 Cal EPA Report (entitled "Health and Environmental Assessment of the Use of Ethanol as a Fuel Oxygenate"; see above)<sup>78</sup>. Exponent saw four fundamental limitations in the 1999 Cal EPA Report.

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<sup>75</sup> *Id.*, p. 7.

<sup>76</sup> *Id.*, pp. 9 and 11.

<sup>77</sup> *Id.*, p. 14.

<sup>78</sup> Exponent, Evaluation of the Cal-EPA Report Titled "Health & Environmental Assessment of the Use of Ethanol as a Fuel Oxygenate", January 2003 (12 JS tab D).

54. First, the 1999 Cal EPA Report provided an inadequate characterisation of the potential impacts of the use of ethanol-fuel blends. Specifically, Cal EPA likely underestimated emissions of key air pollutants and failed to consider the increased potential for public exposure to benzene and other gasoline constituents in drinking water. The authors of the report, by their own admission, acknowledged that it suffers from several major data gaps and uncertainties. Because of these errors and omissions, the 1999 Cal EPA Report likely underestimated the potential public health risks associated with ethanol in gasoline. Thus, the California Environmental Policy Council did not have an adequate data set upon which to make an informed decision about the environmental and health impacts of ethanolfuel blends<sup>79</sup>.
55. Second, the Executive Summary of the 1999 Cal EPA Report grossly misrepresented its own characterisation of the extent of benzene drinking water contamination from the wide-scale use of ethanol in California gasoline. Specifically, the Executive Summary cites a "20% peak relative increase in public drinking water wells impacted by benzene" from the substitution of MTBE with ethanol-fuel blends (pages 1-14). In reality, the authors of the 1999 Cal EPA Report predicted that benzene was twice as likely (i.e. > 100% increase) to affect a drinking water well from the use of ethanol-fuel blends relative to conventional gasoline. This mischaracterisation is important, because the California Environmental Policy Council's decision to approve the use of ethanol may have been based (in part or entirely) on a review of the Executive Summary<sup>80</sup>.
56. Third, the 1999 Cal EPA Report did not "provide an adequate analysis of the fate and transport of ethanol or other gasoline constituents from the release of ethanolfuel blends. In fact, the authors themselves identified more than 20 key data gaps regarding these issues and several outside reviewers identified another dozen or more data gaps that had not been considered. The California Environmental Policy Council's resolution, that the state-wide use of ethanol-fuel blends would not result in 'significant adverse' impact on public health or the environment, was therefore based on an admittedly incomplete analysis"<sup>81</sup>.

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<sup>79</sup> Id., p. 3.

<sup>80</sup> Id., p. 7.

<sup>81</sup> Id., pp. 7-8.

57. Fourth, the 1999 Cal EPA Report did not consider data - which were available before publication of the final report - that suggested ethanol-fuel blends would have a greater impact on benzene plume lengths under different release scenarios than those they predicted. Subsequent studies have concluded that benzene plume lengths may be substantially greater than those predicted in the 1999 Cal EPA Report<sup>82</sup>.
58. Given these limitations, as well as numerous critical data gaps identified by the authors of the 1999 Cal EPA Report, the California Environmental Policy Council's conclusion, that there will not be "significant adverse" impacts to public health or the environment from the use of ethanol-fuel blends, was premature and not supported by the available data. Furthermore, subsequent reports by Cal EPA and others have either confirmed certain of the original report's negative findings and/or reiterated the fact that numerous data gaps must be filled before any decision can be made regarding the use of ethanol in oxygenated and reformulated gasolines in California<sup>83</sup>.
59. ***The Rausser Reports:*** Professor Rausser is the Robert Gordon Sproule Distinguished Professor at the University of California at Berkeley and a Charles River Associates' Senior Counsel. In his 31st January 2003 report ("Was The Decision to Ban MTBE Supported By The Empirical Evidence?"), Professor Rausser provides an economic review (or cost-benefit analysis) of California's decision to ban MTBE in gasoline. From the standpoint of public policy, Professor Rausser concludes that California's decision to ban MTBE in gasoline was irrational<sup>84</sup>.
60. Based on the best available information on the costs and benefits of MTBE, Professor Rausser contends that the decision to ban MTBE relied on a faulty UC Report that failed to provide a logical basis for action. California provided neither the time nor the funding required for an accurate analysis. The UC Report contained a number of omissions and errors; but even if these had been corrected, the Report would have failed to satisfy professional standards for logical and sound public policy analysis. Also, the Report did not follow the accepted cost-benefit methodology or provide a logical basis for its decision. It did not evaluate all of the consequences of the actual decision, erroneously treating sunk costs as if they could be avoided

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<sup>82</sup> *Id.*, p. 9.

<sup>83</sup> *Id.*, p. ES-2.

<sup>84</sup> Gordon C. Rausser, Was the Decision to Ban MTBE Supported by the Empirical Evidence?, 31st January 2003, p. 5 (12 JS tab F).

by banning MTBE<sup>85</sup>.

61. Based on his own cost-benefit analysis of the decision to ban MTBE, Professor Rausser concludes that, based on the best information at the time of the decision, a proper cost-benefit analysis would have lead a reasonable person to conclude that the likely costs of the ban would have significantly exceeded its benefits. Moreover, new information confirms the potential problems of MTBE substitutes, including the relative health risks of emissions from ethanol and MTBE-based fuels, and the likelihood that ethanol will increase the magnitude of contamination from gasoline leaks compared to MTBE. At the same time, experience and studies have confirmed that cleanup of gasoline leaks containing MTBE is likely to be less costly than assumed, and that substitutes for MTBE are likely to be more costly (that is more costly than a conclusion based on an accurate cost-benefit analysis made at the time of the initial decision to ban MTBE)<sup>86</sup>.
62. California's decision to delay rather than cancel the future ban was also irrational. There was no basis for assuming that matters would improve over time. The fundamental excess of costs over benefits is not a result of transition costs that can be reduced by delayed implementation, but rather due to the long term economic and environmental costs of substitutes for MTBE<sup>87</sup>.
63. In his 19th February 2004 report, Professor Rausser responds to the report of the USA's expert, Professor Whitelaw (see below), and indeed relies on Professor Whitlelaw's cost estimates as a further demonstration that "the ethanol additive is far more costly than a MTBE additive to society"<sup>88</sup>.
64. **The Ward Reports:** Professor Ward is the Foyt Family Chair of Engineering and Professor of Civil and Environmental Engineering, George R. Brown School of Engineering, Rice University. Professor Ward was asked to consider two questions: first, whether the state of knowledge about the transport, fate and remediation of MTBE and ethanol in the period 1998-2000, when the case against MTBE was being developed, supported banning MTBE or mandating the use of ethanol; second, whether the present understanding about the behav-

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<sup>85</sup> *Id.*, p. 5.

<sup>86</sup> *Id.*, p. 6.

<sup>87</sup> *Ibid.*

<sup>88</sup> Report of Gordon Rausser, 19th February 2004, p. 3 (20 JS tab A).

our and remediation of MTBE and ethanol in groundwater confirms what was already known about MTBE and ethanol at the time.

65. Having reviewed the UC Report and its analyses of the relative merits and potential environmental impacts of using MTBE and alternatively ethanol as fuel oxygenates to enhance air quality, Professor Ward states six principal conclusions<sup>89</sup>:

(1) The UC Report which was relied upon by Governor Davis to support the ban of MTBE failed to use all applicable scientific information, which lead to bold and erroneous speculation about the transport and fate of MTBE in aquifers and the predicted occurrence of MTBE in public drinking water supplies.

(2) MTBE is neither ubiquitous nor a dangerous groundwater contaminant and is not an imminent threat to the environment, as claimed by Governor Davis in Executive Order D-5-99. Recent estimates confirm that less than one percent of California's public water sources are contaminated with MTBE - as earlier estimates, available to the drafters of the UC study and to Governor Davis, found - and that the rate of discovery is falling rapidly with new and broader sampling.

(3) While slowly biodegradable in many groundwater systems, which sometimes allow plume lengths to exceed those of benzene, toluene, ethylbenzene and xylene (BTEX), MTBE is biodegradable in aquifers by indigenous bacteria. Commercially available and affordable biological processes are now available for clean-up of groundwater contaminated by MTBE.

(4) In contrast, the long-term impacts of the use of ethanol as a fuel oxygenate continue to be largely unknown and unpredictable, despite considerable investigations since the UC study of the behaviour of ethanol-blended fuels and neat ethanol released into groundwater systems.

(5) There is a significant likelihood, however, that ethanol will increase the transport of benzene and known, non-threshold, carcinogens in aquifers and that the concomitant risks to public water supplies may be unacceptable.

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<sup>89</sup> C. Herb Ward, *Transport, Fate, and Remediation of MTBE and Ethanol Used as Fuel Oxygenates*, 31st January 2003, pp. 2-3 (12 JS tab G).

(6) Present scientific and engineering knowledge and analyses confirm the lack of support for California's decision to ban MTBE, its failure to study adequately other alternatives such as methanol, and its mandate of ethanol as the oxygenate of choice.

66. In his report of 19th February 2004, Professor Ward responds to the first round expert reports of the USA's experts, Professor Fogg and Dr Happel (see further below)<sup>90</sup>. He strongly affirms his previous report, and reiterates his view that the "UC-Study is flawed in its analysis of the role of biodegradation in the fate of MTBE in groundwater"<sup>91</sup>. He also concludes: "The decision to ban MTBE as a fuel oxygenate and mandate ethanol as a replacement cannot be justified on a scientific or technical basis because the environmental consequences of widespread use of ethanol are largely unknown"<sup>92</sup>.
67. **The Williams Reports:** Dr Williams is a Senior Scientist at Exponent, the engineering and health risk consulting firm retained as an expert by Methanex. In her First Report, Dr Williams considers whether the UC Report provided an adequate foundation upon which California could make an informed decision regarding the potential environmental or health risks associated with MTBE or alternative oxygenates. She concludes that the UC Report was far from "comprehensive" and suffered from numerous flaws and data limitations. The UC Report therefore did not provide an adequate foundation upon which to make an informed decision regarding the potential environmental or health risks associated with MTBE or alternative oxygenates. She further contends that it was reasonable to conclude that MTBE's air quality benefits, which include reductions in cancer and non-cancer health risks for many persons, will more than outweigh its potential water quality risks. These risks, which were grossly mischaracterised in the UC Report, are generally based on aesthetics (not health risks) and would likely affect a much smaller number of people than would benefit from improved air quality<sup>93</sup>.
68. In her Rebuttal Report, Dr Williams comments on what she believes to be a number of erroneous claims in the USA's Statement of Defense and opinions expressed by the USA's witnesses, Professor

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<sup>90</sup> C. Herb Ward, Response to Rebuttal of the Methanex Report on Transport, Fate, and Remediation of MTBE and Ethanol Used as Fuel Oxygenates, 19th February 2004, pp. 2-3 (20 JS tab B).

<sup>91</sup> *Id.*, p. 2.

<sup>92</sup> *Id.*

<sup>93</sup> Expert Report of Pamela Williams (undated), p. 2 (12 JS tab B).

Fogg, Dr Happell and Mr Simeroth<sup>94</sup>. Dr Williams concludes that Professor Fogg and Dr Happell employed statistically flawed methodologies to measure MTBE detections (by the use of cumulative detections rather than frequency of detections)<sup>95</sup>. To her mind, no matter how California's water quality monitoring data are analysed, the detention frequency and detected concentrations of MTBE in groundwater sources are fairly low and have changed very little over time<sup>96</sup>. Moreover, she asserts that Professor Fogg's assessment of the lag-time and MTBE plume length is unsupported by the available data. As regards the fate and transport of MTBE compared with other groundwater contaminants, Dr Williams suggests that Professor Fogg inappropriately assumed that the general patterns of PCE, TCE and Nitrate contaminants were accurate predictors of the future trends in MTBE contamination. Further, Professor Fogg and Dr Happell inappropriately discounted the important roles of biodegradation and physical and chemical factors in attenuating MTBE<sup>97</sup>. Finally, Dr Williams concludes that the USA inappropriately characterised the relative cancer risks and air quality impacts associated with MTBE and ethanol fuel blends<sup>98</sup>.

69. In Dr Williams's opinion, the California Environmental Policy Commission's conclusion in 2000 (that the wide-scale use of ethanol in California would not pose a significant environmental or health risk) was premature and not substantiated by the available data. Indeed, its findings were based on the very incomplete and biased evaluation by Cal-EPA and, in some instances, contradicted or mischaracterised the actual findings presented in the 1999 Cal-EPA Report. This latter report did not provide an adequate foundation upon which to make an informed decision regarding the potential environmental or health risks associated with the wide-scale use of ethanol<sup>99</sup>. Based on the historical and currently available scientific data, it is reasonable to conclude that the wide-scale substitution of ethanol for MTBE in gasoline will pose a range of environmental and health hazards, which may ultimately negate or partially offset the benefits associated with ethanol-fuel blends<sup>100</sup>.

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<sup>94</sup> Rebuttal Report by Dr Pamela Williams to Amended Statement of Defense of Respondent and Selected expert Reports in *Methanex v. USA*, 19th February 2004, p.1 (20 JS tab C).

<sup>95</sup> *Id.*, p. 2.

<sup>96</sup> *Id.*, p. 3.

<sup>97</sup> *Id.*, p. 4.

<sup>98</sup> *Id.*, pp. 6-7.

<sup>99</sup> Dr Williams' First Expert Report, p. 3.

<sup>100</sup> *Id.*, p. 4.

70. Dr Williams finally concludes that the potential threats to drinking water sources for gasoline releases can be adequately addressed without banning MTBE, simply by implementing and enforcing existing regulations relating to USTs and twostroke engine watercraft<sup>101</sup>.
71. **USA Expert Witnesses:** The USA tendered Expert Reports from five expert witnesses: Mr Kenneth D. Miller (Report, December 2003); Mr Bruce F. Burke (Report, December 2003; Rejoinder Report, April 2004); Professor Graham E. Fogg (Report, 1st December 2003; Rejoinder Report, April 2004); Dr Anne Happel (Report, December 2003; Rejoinder Report, 23rd April 2004); and Professor Edward Whitelaw (Report, November 2003; Rejoinder Report, 21st April 2004). The testimony of Mr Dean Simeroth, one of the US factual witnesses, also touched on these expert issues (Witness Statement, 3rd December 2003; Second Witness Statement, 21st April 2004). We summarise the effect of these witness's testimony below.
72. **The Miller Report:** Mr Miller, an independent engineering consultant to the petrochemical industry, is an engineering graduate from Princeton University with an extensive background and experience relating to the production, sale and marketing of MTBE. In his Expert Report, Mr Miller calculated the amount of methanol demand for MTBE production in plants operated by gasoline refineries in California between 1998 and 2001. Mr Miller's cross-examination by Methanex at the main hearing in June 2004 (by videolink) was not controversial for present purposes and need not be separately summarised here.
73. **The Burke Reports:** Mr Burke is Vice-President of Petroleum and Chemical Group at Nexant Inc., a firm specializing in the provision of management and technical consultant services to the Global Energy Sector. Most of his two reports, which deal with a comparison of MTBE, methanol and ethanol, their competitive interactions and their suitability as oxygenates in gasoline, is not relevant to the issues arising from the UC Report. However, certain parts of his testimony regarding the marketplace for oxygenates used in gasoline in California is relevant to the decision to ban MTBE.
74. In his First Report, Mr Burke testified that in the United States there are primarily two oxygenates used in motor gasoline, MTBE and ethanol. A third compound, TAME, is also used but in much smaller

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<sup>101</sup> Id., p. 5.

quantities. Outside the US, a fourth oxygenate, ETBE, is used (for example, in Spain and France). Thus, of the thousands of oxygenate compounds, only four are in use commercially in any significant quantity. Of these four, TAME and ETBE are used in very limited quantities<sup>102</sup>. Moreover, in the USA there are no producers of, and no market exists for ETBE<sup>103</sup>.

75. In his Rejoinder Report dated April 2004, Mr Burke addressed (inter alia) whether benzene is an essential component of motor gasoline, and whether it can be eliminated entirely from motor gasoline. Historically, due to its high octane and very low RVP, refiners considered benzene to be an attractive feedstock for gasoline production. Prior to the enactment of restrictions on benzene content in gasoline under the Amendments to the Clean Air Act of 1990, the average benzene content of gasoline was about 1.6% by volume. Reflecting its attractive blending characteristics, refineries continue to use benzene in small volumes (limited to less than 1.0% volume as a blend stock in gasoline. As a basic principle, it is generally considered impossible from a practical standpoint to remove 100% of any molecule from refinery streams. Because benzene is widely dispersed throughout many processing streams in all refineries, the removal of every benzene molecule from gasoline would be cost prohibitive<sup>104</sup>.
76. Mr Burke was cross-examined at the main hearing by Methanex. His testimony related principally to the competitive interactions of methanol and ethanol. He confirmed his previously expressed opinion that no binary choice exists between the use of methanol and ethanol as fuel oxygenates and that methanol does not compete with ethanol for sales in the market for oxygenate additives<sup>105</sup>. Mr Burke illustrated the point with evidence that the use of methanol as a vehicle fuel is not allowed for 89 percent of the vehicle fleet in the US because of its corrosive and damaging qualities, and that the use of methanol as a gasoline fuel oxygenate would void the warranties of essentially the entire US vehicle fleet<sup>106</sup>.

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<sup>102</sup> Expert Report of Bruce F. Burke, December 2003, p. 4, para. 21 (13 JS tab B).

<sup>103</sup> *Id.*, p. 37, para 126.

<sup>104</sup> Rejoinder Expert Report of Bruce F. Burke, April 2004, Rejoinder Report, pp. 10 - 11, paras. 34-37 (24 JS tab A).

<sup>105</sup> Mr Burke, Transcript Day 6, pp. 1414, 1415, 1422 and 1484.

<sup>106</sup> *Id.*, pp. 1430, 1432-1433.

77. **The Fogg Reports:** Dr Fogg is Professor of Hydrogeology at the University of California, Davis and co-author of "Volume IV: Health and Environmental Assessment of MTBE" of the UC Report. Professor Fogg was asked to review and comment on the expert reports filed by Dr Williams, Professor Ward, Exponent and AES. His report presents a detailed, scientific analysis of the nature of the MTBE problem in California (as understood in 1998 and more recently) and its impact on groundwater resources across the state. It also addresses several of the assertions presented by Methanex's experts with respect to these issues<sup>107</sup>. Professor Fogg reached the following conclusions:

(1) The UC Report by a multi-disciplinary team of scientists from the University of California relied on scientific literature and other data available at the time;

(2) California, where most of the population resides in a desert climate, is the single largest user of groundwater in the US, and forty-three percent of all Californians obtain drinking water from groundwater;

(3) Properties of MTBE together with its high volume of use in gasoline combine to make it a very potent contaminant of drinking water sources, especially groundwater;

(4) Clean up of groundwater contamination is difficult, costly and sometimes impossible;

(5) MTBE is highly resistant to biodegradation under natural conditions in groundwater systems;

(6) The essence of the MTBE problem is that present-day impacts, which are significant and worsening, are not an accurate measure of the ultimate impacts of MTBE. This is because of the long lag time (commonly decades to centuries) between introduction of groundwater contaminants and their arrival at drinking water supply wells;

(7) Enormous numbers of drinking water supply wells in California are vulnerable to MTBE contamination because of the collocation of drinking water supply wells and leaking underground fuel tanks (LUFTs);

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<sup>107</sup> Expert Report of Graham E. Fogg, 1st December 2003, pp. 2-3 (13 JS tab D).

(8) Despite limitations of the California database on MTBE in drinking water wells, the data clearly show that the percentage of public supply wells contaminated with MTBE has been steadily increasing with time;

(9) Private wells are not routinely monitored by any government agency and testing for MTBE is done on a voluntary basis, at high costs;

(10) Nationwide water quality surveys have shown MTBE either to be the most commonly detected, or the second most commonly detected volatile organic compound (VOC); and

(11) The recommendation of the UC Report to phase out MTBE over an interval of several years was consistent with others' findings and recommendations, including the EPA Blue Ribbon Panel on Oxygenates in Gasoline and the Northeast States for Co-ordinated Air Use Management<sup>108</sup>.

78. In his Rejoinder Report dated 21st April 2004, Professor Fogg replies to the responses from Professor Ward and Dr Williams to his expert report. One conclusion in particular bears noting: that the Ward/William's denial that MTBE detections in groundwater or public drinking water are "wide spread" or "significant" cannot stand, having regard to his findings that by 1998 MTBE had been detected at more than 4,000 LUFT sites and that more than 50% of these sites were within 0.5 miles of a public drinking well. The arrival of just a fraction of the thousands of MTBE plumes to wells can create a serious drinking water contamination problem for an affected community<sup>109</sup>. It will be recalled that MTBE tastes like turpentine in low levels of water contamination (at 5 ppb), quite apart from the risk to human health at higher levels.

79. Professor Fogg was cross-examined at the main hearing by Methanex. In his testimony, he explained how the sum of US \$500,000 which had been committed for the UC Report was "leveraged" considerably through the use of funding available from the National Institute of Health Sciences<sup>110</sup>. As regards the likelihood of continued MTBE leakages from even the most modern USTs and the comparative risks associated with the leakage of ethanol, benzene and MTBE, Professor Fogg pointed out that (i) ethanol tends to be readily biodegraded, (ii)

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<sup>108</sup> *Id.*, pp. 3-7.

<sup>109</sup> Rejoinder Report of Graham E. Fogg, p. 5 (24 JS tab B).

<sup>110</sup> Professor Fogg, Transcript Day 5, pp. 1232 and 1235-1236.

the natural attenuation of benzene is going to mitigate the problem of its leakage from USTs in 80 to 90 percent of cases, but (iii) there is no evidence that biodegradation, either aerobic or anaerobic, without any engineered intervention at leaking tank sites is sufficient to deal with MTBE leakage<sup>111</sup>. Professor Fogg's oral testimony added to and in no way detracted from his earlier written testimony.

80. **The Happel Reports:** Dr Anne Happel is Managing Director of Eco Interactive Inc., a California company providing software and consulting services for the environmental data management needs of governments and industry. Prior to joining Eco Interactive, Dr Happel was a scientist at Lawrence Livermore National Laboratory ("LLNL"), a US Department of Energy national laboratory operated by the University of California. In 1998 she prepared a Report, "Evaluation of MTBE impacts to California Groundwater Resources", which was reported to the Governor's office in 1998 by the Cal EPA. She also served as a member of the US EPA's 1999 Blue Ribbon Panel of Experts Regarding the Use of Oxygenates Including MTBE in Gasoline<sup>112</sup>.
81. In her Expert Report dated December 2003, as regards groundwater risks associated with MTBE, Dr Happel testified that:
- (1) In 1998 and 1999 there was abundant evidence that when MTBE containing gasoline was released to the subsurface in California, the MTBE could result in more frequent and severe impacts to groundwater than other fuel contaminants (i.e. benzene);
  - (2) Her research in 1996 to 1999 demonstrated significant evidence that MTBE possesses a unique and significant threat to California groundwater resources as compared to other fuel constituents and supports Governor Davis' call for the elimination of MTBE in gasoline in California;
  - (3) She took part in a separate, independent review (by the US EPA Blue Ribbon Panel on Gasoline Oxygenates) of the evidence regarding MTBE from a national perspective. The Panel's recommendations were largely in line with those acted upon by California in deciding to ban MTBE; and

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<sup>111</sup> Id., pp. 1246, 1248 and 1259.

<sup>112</sup> Dr Anne Happel, Analysis of the California UST & LUST Programs and the Impacts of MTBE and Ethanol to California Groundwater resources, December 2003, p. 1 (13 JS tab E).

(4) By reviewing current regulatory databases, portions of the extensive scientific literature, and regulatory programmes, she finds substantial evidence that corroborates pre-2000 findings that the use of MTBE in California gasoline posed significant threats to California groundwater resources. The current state of knowledge further substantiates the previous scientific findings that served, in part, as the basis of California's decision to eliminate MTBE from California gasoline<sup>113</sup>.

82. As regards ground/drinking water risks associated with use of ethanol compared with MTBE, having reviewed field and modelling studies, Dr Happel concludes<sup>114</sup>:

(1) For small volume per day vapour or liquid releases, the use of ethanol oxygenate or MTBE-free gasoline is expected to affect groundwater quality considerably less than gasoline-containing MTBE;

(2) Once significant ethanol and MTBE groundwater plumes are formed, the preferential biodegradation of ethanol in groundwater is expected to increase the length of MTBE-contaminated groundwater plumes;

(3) Large-volume neat ethanol spills undergo a significant bio-attenuation. This is in stark contrast to a large-scale release of MTBE-containing gasoline where dispersion (not biodegradation) and long-term active remediation are the primary factors for stabilizing and eventually attenuating the MTBE plume; and

(4) Current studies show that chronic small-volume per day releases (which are commonly found in California 1998-compliant USTs) of ethanol-containing gasoline are expected to have much less significant impacts on water quality than chronic small-volume per day releases of MTBE-containing gasoline. In addition, current studies show that large-scale releases of denatured fuel ethanol, and gasoline-containing ethanol, are expected to have much lower long-term impacts on water quality than large-scale releases of gasoline-containing MTBE.

83. Dr Happel's Rejoinder Report dated 23rd April 2004 reviews the extensive post-1998 California data presented in her earlier December 2003 expert report. Her principal conclusions, which dealt with both MTBE and benzene risks, are<sup>115</sup>:

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<sup>113</sup> *Id.*, pp. 3-4.

<sup>114</sup> *Id.*, pp. 57-58 and 64-65.

<sup>115</sup> Rejoinder Report of Dr Anne Happel, 23rd April 2004.

(1) Industry testimony, statements and actual field studies of operating USTs show that many operating USTs, meeting California's stringent standards, continue to have leakage and that the continued use of MTBE poses a unique risk to groundwater resources versus other gasoline constituents<sup>116</sup>;

(2) Field studies conducted by California agencies since 1998 fully support the anecdotal reports and testimony presented in California, indicating that compliant UST systems would be largely ineffective in preventing the release of gasolinecontaining MTBE and the subsequent MTBE contamination of ground water. These findings directly contradict Dr Williams' claims that "the potential threats to drinking water sources from gasoline releases could be adequately addressed without banning MTBE simply by implementing and enforcing existing underground gasoline storage tank regulations"<sup>117</sup>;

(3) There are nearly 10,000 sites currently reporting MTBE pollution in groundwater. Based on this data, Dr Happel estimates that 10,000 to 15,000 LUST sites have polluted groundwater throughout California. Her estimated number of MTBE-polluted groundwater sites is greater (approximately two-fold) than the number predicted by Fogg et al in the UC Report based on their examination of earlier more limited data sets. Current LUST data shows MTBE-polluted groundwater at over 50% of the sites at concentrations equal to or greater than 200 ppb (and at over 40% of the sites at concentrations equal to or greater than 1,000 ppb). Thus, the extent and magnitude of MTBE pollution in California's groundwater is indeed significant, widespread and worse than predicted by the UC Report<sup>118</sup>;

(4) In 1998, from a statistical analysis of actual LUST data, and from a review of the then existing literature, there was no convincing evidence that biodegradation of MTBE occurred quickly and/or commonly in the field. Therefore, in her 1998 report, she recommended that groundwater resources be managed "with the assumption that MTBE is both mobile and recalcitrant relative to benzene, until proven otherwise"<sup>119</sup>;

(5) Studies of LUST site sediments show that intrinsic biodegradation

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<sup>116</sup> Id., p. 12.

<sup>117</sup> Id., p. 12; cf. Dr Pamela Williams' Rebuttal Report, p. 12.

<sup>118</sup> Id., p. 16.

<sup>119</sup> Id., p. 30.

of benzene (biodegradation by indigenous microorganisms present in the LUST sediments) is widespread, while intrinsic biodegradation of MTBE is limited. LUST results directly show that engineered remediation technologies that add oxygen to anoxic LUST sites will readily result in biodegradation of benzene by indigenous microorganisms present in the sediments, but will only sometimes result in the aerobic biodegradation of MTBE. The presence of indigenous microorganisms that can aerobically degrade MTBE in polluted sediments is limited. When aerobic biodegradation of MTBE occurs, it is markedly slower than benzene biodegradation and will sometimes result in the accumulation of TBA. It is recommended that LUST sites be screened for aerobic degradation potential before undertaking investments in technology to add oxygen to the sub-surface<sup>120</sup>;

(6) Dr Williams' annual detection frequency approach does not show the actual percentage of public drinking wells that are impacted by MTBE in a given year. Annual detection frequency includes only the subset of public wells reporting data to the DHS database in a given year. Thus, the yearly sampling population is significantly biased, primarily because MTBE-positive wells are "dropped" from the yearly sampling pool and because a significant portion of MTBE-positive wells were sampled in only a single-calendar year. Thus, the use of annual detection frequency to understand the percentage of wells impacted by MTBE in a given year is statistically flawed and a misleading approach to characterizing the impact of MTBE in California's public-drinking water wells in a given year<sup>121</sup>; and

(7) Dr Williams' First Report showed that an analysis of the DHS database as of June 2003 demonstrated that 140 of 10,190 public wells (i.e. 1.37 percent) reporting testing for MTBE detected one or more times; whereas, only 0.63 percent (89 of 14,131) of public wells reporting testing for benzene detected benzene one or more times. During the period from 1999 to 2002, 90 individual public wells reported detecting MTBE, while only seven public wells reported detecting benzene. This analysis demonstrates that the MTBE problem has "worsened" for public drinking water wells as compared to other soluble gasoline constituents such as benzene<sup>122</sup>.

84. Dr Happel was cross-examined at the main hearing by Methanex and proved an impressive witness. She explained her 2003 data, based

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<sup>120</sup> *Id.*, pp. 32-33.

<sup>121</sup> *Id.*, p. 46.

<sup>122</sup> *Id.*

on tests results submitted to the State Water Board, which showed that MTBE has now been detected in groundwater at about 10,000 sites in California (70% of the 14,000 LUSTs tested), confirming her 1998 estimates. These results also show groundwater pollution to be worse than was estimated in the UC Report and illustrate the conservative nature of the assumptions employed by Professor Fogg's group in the UC study<sup>123</sup>. She further testified that recent field studies from the Santa Clara Valley Water District and the State Water Resources Control Board demonstrate that the vast majority of the UST systems that meet the most stringent California regulations are continuing to release gasoline to the subsurface<sup>124</sup>; and she explained (consistently with Professor Fogg's testimony) why, in the absence of very expensive intervention, biodegradation is largely ineffective as a remediation technique for small volume leaks of MTBE<sup>125</sup>.

85. **The Whitelaw Reports:** Professor Whitelaw is Professor of Economics at the University of Oregon and President of ECON Northwest. Professor Whitelaw was requested to evaluate the analysis and conclusions presented in Professor Rausser's report. After first describing and evaluating Professor Rausser's cost benefit analysis of California's decision to ban MTBE, he demonstrates how its results change markedly when corrected for detected errors. He concludes by showing that the post-2000 evidence indicates that the pre-hearing 2000 evidence on which California based its decision was not anomalous<sup>126</sup>.
86. Professor Whitelaw notes that the UC study represented a first-ever attempt to quantify the costs and benefits across all three media (air, water, fuel) that would be impacted directly and indirectly by a possible ban of MTBE. He concludes that, as the *pioneers* in this complex assignment, Dr Keller and Dr Fernandez, who authored this part of the UC Report, competently framed the issues related to a possible MTBE ban and developed a useful construct which was adopted later by others (including Professor Rausser), who have attempted this analysis. Nevertheless, Professor Whitelaw agrees that Dr Keller and Dr Fernandez erred by including so-called sunk costs in their analysis. This error contributed to a partial over-estimate of MTBE's water-quality costs relative to its alternatives. However, the UC

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<sup>123</sup> Dr Happel, Transcript Day 5, pp. 1160-1162.

<sup>124</sup> *Id.*, pp. 1164-1165.

<sup>125</sup> *Id.*, pp. 1180-1185.

<sup>126</sup> Expert Report of Ed Whitelaw, November 2003, p. 9 (13A JS tab K).

Report also omitted a number of other important water-quality costs - e.g. it failed to quantify the impacts of MTBE plumes on property values, commercial and residential development and the intrinsic value of California's groundwater resources. It also ignored the cost of monitoring and enforcing the upgraded UST system and resolving conflicts over future MTBE leaks. These errors of omissions contributed to an under-estimate of MTBE's water-quality costs and offset, in part or in whole, the inappropriately included sunk costs.

87. In the end, because of these offsetting errors, the UC Report arrived at an appropriate conclusion while erring in some of the details of its estimates. In the circumstances, Professor Whitelaw concludes that the weight of economic evidence available at the time supported the decision to ban MTBE<sup>127</sup>.
88. Professor Whitelaw identifies what he considers to be a number of shortcomings in Professor Rausser's work in terms of errors of commission, errors of omission, errors in the treatment of uncertainty and in the failure to produce a transparent analysis. After correcting for Professor Rausser's error of commission, but not his other errors, Dr Whitelaw calculates an expected net cost of the MTBE-ethanol switch of \$268 million annually - or approximately \$1.1 billion lower than Professor Rausser's corresponding estimate in his report<sup>128</sup>.
89. Because analyses of the expected net costs of the MTBE ban are not definitive - i.e. because there are uncertainties around many of the underlying assumptions and omissions of sizeable costs - Dr Whitelaw opines that the California decision to ban MTBE in gasoline would have been justified on economic grounds if one or more of the following conditions were met:
- (1) California concluded that the costs associated with the omitted categories exceeded the expected value of the monetized costs and benefits;
  - (2) California was risk averse;
  - (3) California was less sanguine than Professor Rausser about the integrity of upgraded UST systems; and
  - (4) California was concerned about the distributional affects associated with continued MTBE use.

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<sup>127</sup> Id., pp. 3-5.

<sup>128</sup> Id., p 7.

90. Because MTBE's air-quality benefits in car exhausts are substantially similar to ethanol's, the cost benefit issue turns on the lower costs for MTBE as an oxygenate relative to the higher risks of groundwater contamination from MTBE. In 1999, California's policy makers faced the question of whether the benefit of eliminating - once and for all - the considerable uncertainty surrounding MTBE's future ability to contaminate California's groundwater assets and drinking water supplies was worth the risk of increasing gasoline prices by about three cents per US gallon. In Professor Whitelaw's opinion, when California policy makers answered "yes" to this question, they did so rationally<sup>129</sup>.
91. Information made available since 2000 further supports the rationality of the MTBE ban. Recent evidence suggests that transition to ethanol has been smooth and the impacts on gasoline prices modest. By contrast, new evidence about the upgraded UST, and their apparent inability to prevent MTBE from entering into the subsurface, has confirmed that the risks posed by the use of MTBE are in fact even greater today than they were thought to be in 2000.
92. Professor Whitelaw filed a Rejoinder Report of 21st April 2004, much of which is devoted to a detailed discussion of key areas of ongoing disagreement between his work and that of Professor Rausser. However, regarding the categories of quantifiable costs and benefits that would fall inside the borders of California, Professor Rausser and he share common ground on four points<sup>130</sup>:
- (1) MTBE would continue to degrade California's groundwater assets even after full implementation of upgraded UST regulations. Dr Rausser and he agree that MTBE would be more damaging than ethanol to California's water quality. Both expect water quality costs in excess of \$120 million annually associated with ongoing MTBE leaks. Also both agree that MTBE would be more damaging than ethanol to California's water quality<sup>131</sup>;
- (2) The MTBE ban would result in a modest increase in gasoline prices of approximately 3.16 cents per US gallon<sup>132</sup>;

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<sup>129</sup> Id., pp 8, 9 and 49.

<sup>130</sup> Rejoinder Expert Report of Ed Whitelaw, 21st April 2004, pp. 7-8 (24 JS tab E).

<sup>131</sup> Professor Rausser's Report of 19th February 2004, p. 10.

<sup>132</sup> Id., p. 1d.

(3) Air quality would remain unchanged for most toxics, including benzene<sup>133</sup>; and

(4) Post-2000 information is clearly irrelevant to judging the decision to ban MTBE at the time of the ban<sup>134</sup>.

93. Whitelaw also testified at the main hearing, under cross-examination by Methanex. After a helpful explanation of the objectives of and the correct approach to cost / benefit analysis, much of his cross-examination involved a review and reaffirmation of his conclusions (set out in his written expert reports) as to the frailties of the cost / benefit analysis of California's decision to ban MTBE performed by Professor Rausser. Professor Whitelaw provided a detailed explanation of what he believed to be Professor Rausser's errors both of commission and omission. He told the Tribunal that if any one of the four conditions (described above) were met, California's policymakers' support for the MTBE ban would be considered rational. When the potentially huge water quality costs are looked at against the expected three cent per gallon price increase for gasoline, Professor Whitelaw considered it to be "very understandable that sort of normal folks making this decision would say, whoa, it is an insurance premium we are willing to pay"<sup>135</sup>.

94. **Mr Dean Simeroth:** Mr Simeroth is Chief of the Criteria Pollutants Branch of CARB. The Criteria Pollutants Branch has primary responsibility for the development of regulations to control motor vehicle fuel properties that affect air emissions. Since 1987 Mr Simeroth has supervised the development of 24 new or amended regulations for motor vehicle fuels that have been considered and approved by CARB and has managed the program to evaluate performance of the CaRFG regulations.

95. In his witness statement of 3rd December 2003, Mr Simeroth describes the adoption of California's various reformulated gasoline regulations<sup>136</sup>. He notes that the Phase II CaRFG regulations which were adopted in the early 1990s and which required compliance starting in the spring of 1996 were very effective in reducing harmful emissions from motor vehicles in California. In the later 1990s ambi-

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<sup>133</sup> Id., p. 8.

<sup>134</sup> Id., p. 23.

<sup>135</sup> Professor Whitelaw, Transcript Day 6, p. 1536; see also pp. 1499, 1533-1536.

<sup>136</sup> Witness Statement of Dean C. Simeroth, 3rd December 2003, para. 10 (13A JS tab H).

ent concentrations of CO dropped significantly in California. Although the wintertime oxygenate program brought about some of these reductions, the primary cause was that the older, highest polluting cars were being replaced by new cars that emitted far less CO<sup>137</sup>.

96. Both Federal RFG regulations and California RFG regulations apply in California. This means that unless US EPA waives the federal oxygenate requirement, the 80% of California's gasoline that is subject to the federal RFG requirements must contain at least 2 percent oxygen by weight, as well as comply with the CaRFG requirements. MTBE became the oxygenate of choice for most refiners for meeting the federal RFG oxygen requirements in California<sup>138</sup>. After the Federal RFG and CaRFG2 programs were implemented, concerns grew regarding contamination of groundwater from MTBE from gasoline. Because of these concerns, and as required by the California Senate Bill No 989, the CARB conducted a rule making exercise in 1999-2000 by which it adopted a ban on MTBE in gasoline as part of new phase III CaRFG regulations that were to apply starting on 31st December 2002.
97. The toxic sub-models of the CaRFG2 Predictive Model were based on MTBE blended gasoline. Gasolines which contain MTBE or ethanol modestly increase formaldehyde acetaldehyde, with the formaldehyde increase larger for MTBE and the acetaldehyde increase larger for ethanol. Formaldehyde is a more potent carcinogen than acetaldehyde. Adjustments were factored into the exhaust emission equation for formaldehyde and acetaldehyde in the CaRFG3 predictive model to reflect the assumption that oxygenated gasoline would contain ethanol. Along with prohibiting MTBE, the CaRFG3 regulations also reduced the sulphur and benzene specifications that had been applied under the CaRFG2 regulations.
98. In the CaRFG3 rule making, the CARB staff compared the anticipated air quality impacts of the CaRFG3 standards to the impacts of the CaRFG2 standards<sup>139</sup>. The CARB's data show that emissions of NOx, hydrocarbons and potency-weighted toxics will not increase with the CaRFG3 gasoline as compared to CaRFG2 gasoline<sup>140</sup>. As a result, Dr Williams' conclusions that "the historical and currently available scientific data show that the use of ethanol in gasoline will likely produce some negative air quality impacts", and the findings

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<sup>137</sup> Id., para. 14.

<sup>138</sup> Id., paras. 10-11.

<sup>139</sup> Id., para. 30.

<sup>140</sup> Id.

and data from New Mexico and Brazil that "strongly suggest that the substitution of ethanol for MTBE in gasoline may result in back sliding on the improvements that have been made to air quality", are not accurate or applicable to gasoline in California because all California gasoline containing ethanol will be subject to CaRFG3 standards<sup>141</sup>.

99. In addition, California gasoline produced with ethanol which meets CaRFG3 standards will not result in any greater overall benzene emissions than California gasoline produced with MTBE that meets the CaRFG2 standards<sup>142</sup>. This is because the benzene content standard of 0.8 per cent by volume in the CaRFG3 program is more stringent than the corresponding benzene standard of 1.0 percent by volume in the CaRFG2 regulations<sup>143</sup>. Indeed, it is anticipated that the exhaust benzene emissions from CaRFG3 containing ethanol will be lower than the corresponding CaRFG2 containing MTBE<sup>144</sup>.
100. Mr Simeroth also gave evidence at the main hearing, as requested by Methanex. Under cross-examination by Methanex, he testified that, following the decision to ban MTBE, the Criteria Pollutants Branch undertook an exhaustive review of information available at the time to ensure that, in making its Phase III recommendations, the benefits of the Phase II programme were preserved, as was required by state law. Having been asked to summarise the principal conclusions of his witness statements, he stated that "... the basic reformulated gasoline with ethanol will provide the same benefits as Phase II reformulated gasoline with MTBE, or Phase II reformulated gasoline." Methanex's proposition to Mr Simeroth that the CARB made multiple changes to its Phase II reformulated gasoline regulations in order to "accommodate" the addition of ethanol as an oxygenate, following the ban of MTBE, was rejected effectively. Mr Simeroth explained that the Phase II requirements did not specify MTBE, but allowed any approved oxygenate (including ethanol) to be used. The changes, or accommodations, in Phase III reformulated gasoline were made to ensure an adequate supply of gasoline in the State (using the remaining oxygenate - ethanol) whilst at the same time addressing the needs of gasoline refiners<sup>145</sup>. His oral evidence was entirely consistent with and supportive of his written statements.

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<sup>141</sup> Id., paras. 33-34.

<sup>142</sup> Id., para. 41.

<sup>143</sup> Id.

<sup>144</sup> Id., p. 11, para. 43.

<sup>145</sup> Mr Simeroth, Transcript Day 5, pp. 1270-71, 1279-1281, 1290, 1299-1300.

## 6) The Tribunal's Findings on the Scientific Evidence

101. Having considered all the expert evidence adduced in these proceedings by both Disputing Parties, the Tribunal accepts the UC Report as reflecting a serious objective and scientific approach to a complex problem in California. Whilst it is possible for other scientists and researchers to disagree in good faith with certain of its methodologies, analyses and conclusions, the fact of such disagreement, even if correct, does not warrant this Tribunal in treating the UC Report as part of a political sham by California. In particular, the UC Report was subjected at the time to public hearings, testimony and peer-review; and its emergence as a serious scientific work from such an open and informed debate is the best evidence that it was not the product of a political sham engineered by California, leading subsequently to the two measures impugned by Methanex in these arbitration proceedings. Moreover, in all material respects, the Tribunal is not persuaded that the UC Report was scientifically incorrect: the Tribunal was much impressed by the scientific expert witnesses presented by the USA and tested under cross-examination by Methanex; and the Tribunal accepts without reservation these experts' conclusions.
102. It is convenient here to summarise the principal findings of fact which the Tribunal has made in regard to the scientific issues relating to MTBE:
- (1) The California ban on the oxygenate MTBE began as a policy decision of the California Senate which, as expressed in the California Bill, was contingent on the scientific findings of the UC Report and which was to be implemented by California in the light of its public hearings, testimony and peer review;
  - (2) This policy was motivated by the honest belief, held in good faith and on reasonable scientific grounds, that MTBE contaminated groundwater and was difficult and expensive to clean up;
  - (3) There is no credible evidence that, by commissioning or producing the UC Report, the California Senate or the University of California researchers intended to favour the United States ethanol industry or particular companies within it (including ADM); and
  - (4) There is no credible evidence of any intention on the part of the California Senate or the University of California researchers, by commissioning or producing the UC Report, to injure methanol producers, whether US or foreign companies (including Methanex).

## **PART III - CHAPTER B**

### **MR GRAY DAVIS, ADM, AND THE US SYSTEM OF POLITICAL CONTRIBUTIONS**

#### **1) Introduction**

1. Tribunal will begin with Methanex's factual submissions, which aim to demonstrate that the California ban of MTBE was "intended to harm foreign methanol producers, including Methanex"<sup>1</sup>. Many of these arguments are not based on facts, as such, but on factual inferences and interpretations which Methanex invites the Tribunal to draw from the facts.
2. Methanex has proposed the following methodology:

*"Each of these propositions is supported by the facts that are now of record in this case, and by the reasonable inferences that can be drawn from those facts. In a number of instances, the Tribunal can draw the appropriate inferences from the fundamental unreasonableness or incredibility of the contrary justifications that have been offered to refute them-e.g., California's claim that its MTBE and methanol bans, which created an ethanol monopoly, while continuing to allow benzene and other poisonous chemicals to leak into groundwater, was motivated solely by environmental and not protectionist interests<sup>2</sup>."*

Counsel for Methanex's description of this methodology can be summarised, colloquially, as one of inviting the Tribunal to "connect the dots," i.e., while individual pieces of evidence when viewed in isolation may appear to have no significance, when seen together, they provide the most compelling of possible explanations of events, which will support Methanex's claims<sup>3</sup>.

3. Connecting the dots is hardly a unique methodology; but when it is applied, it is critical, first, that all the relevant dots be assembled; and, second, that each be examined, in its own context, for its own significance, before a possible pattern is essayed. Plainly, a self-serving selection of events and a self-serving interpretation of each of those selected, may produce an account approximating verisimilitude, but it will not reflect what actually happened. Accordingly, the Tribunal will

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<sup>1</sup> Second Am. Claim at Part VI.

<sup>2</sup> Id., para. 144.

<sup>3</sup> E.g., Transcript Day 8, p. 1911 (lines 12-17).

consider the various "dots" which Methanex has adduced - one-by-one and then together with certain key events (essentially additional, noteworthy dots) which Methanex does not adduce - in order to reach a conclusion about the factual assertions which Methanex has made. Some of Methanex's proposed dots emerge as significant; others, as will be seen, do not qualify as such. In the end, the Tribunal finds it impossible plausibly to connect these dots in such a way as to support the claims set forth by Methanex.

## 2) The Six Dots

4. **Dot 1:** Methanex asserts that "California has been trying - without success - to develop an in-state ethanol industry [since 1983]"<sup>4</sup>, with the stated motivations being disposal of biomass waste and generation of economic benefits in rural areas<sup>5</sup>. This effort was supported by in- and out-of-state ethanol producers. A number of statements by California officials are adduced to support the effort to create an in-state ethanol industry<sup>6</sup>. Methanex contends that the leaking gasoline USTs crisis was "a pretext for creating the previously non-existent ethanol market that the ethanol lobby coveted, as well as the in-state ethanol industry that California had been unsuccessfully trying to create"<sup>7</sup>.
5. For a number of reasons, the Tribunal is unable to draw from the materials assembled by Methanex the inference which Methanex proposes. First and foremost because, even if California wished to develop an in-state industry to deal with biomass waste and to encourage rural economic development and even if such an initiative were incompatible with NAFTA, there is neither demonstration nor basis for an inference that this putative policy was connected with a desire to harm methanol or Methanex.
6. For example, Methanex notes that California enacted § 502 of its Food and Agriculture Code in 1983 establishing ethanol incentives<sup>8</sup>. However, this was years before MTBE became a common gasoline additive in compliance with federal law<sup>9</sup>. As a result, Methanex does not

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<sup>4</sup> Second Am. Claim, para. 146.

<sup>5</sup> *Ibid.*

<sup>6</sup> *Id.*, paras. 149-157.

<sup>7</sup> *Id.*, para. 152.

<sup>8</sup> *Id.*, para. 146 (citing Cal. Food & Agric. Code § 502 (1983)).

<sup>9</sup> Widespread use of MTBE did not begin until after the passage of the federal

produce evidence to suggest, and the Tribunal cannot conclude that, the enactment was intended to harm methanol or Methanex. In any event, the ethanol incentives in § 502 were repealed in 1984<sup>10</sup>, i.e., long before the narrative of events relevant to this case had commenced.

7. Methanex also claims that there were some ethanol-related incentives in the late 1980s and early 1990s. However, Methanex offers no evidence that these were meant to harm producers of other oxygenates. Methanex notes that legislation in 1988 would have created an "incentive grant program for production of ethanol and other biofuels"<sup>11</sup>. Again, this was prior to the commonplace use of MTBE. Moreover, the benefits were not limited to ethanol but extended to "other biofuels". In any case, no funding was ever authorised for the program<sup>12</sup>. In 1991, California passed legislation to allow blending of ten percent ethanol in reformulated gasoline, provided that the CARB did not find a resulting increase in ozone forming potential. Methanex points to this as one of the "ethanol initiatives" in California, while noting that it was only in place until 1998<sup>13</sup>. This legislation did *not* relate to or benefit the creation of an in-state ethanol industry. Moreover, CARB regulations passed the same year established a limit on the oxygen percent by weight in gasoline which thus prohibited ethanol from reaching the full ten percent by volume<sup>14</sup>.

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Clean Air Act Amendments of 1990, requiring that the areas of the United States with sub-standard air quality use reformulated gasoline with an increased oxygen content. See John Froines et al., *An Evaluation of the Scientific Peer-Reviewed Research and Literature on the Human Health Effects of MTBE, Its Metabolites, Combustion Products and Substitute Compounds*, in U.C. Report Vol. II: Human Health Effects, p. 2 (4 JS tab 37); see also Arturo Keller et al., *Executive Summary, Recommendations, Summary*, in U.C. Report Vol. I: Summary & Recommendations, p. 15 (4 JS tab 36); Am. Defense, paras. 19-21.

<sup>10</sup> Second Am. Claim, para. 146 (citing Stats. 1984, Ch. 268, § 16.91, effective 30th June, 1984).

<sup>11</sup> Reply at tbl.1.

<sup>12</sup> *Ibid.*

<sup>13</sup> *Ibid.*

<sup>14</sup> Cal. Air Resources Bd., *An Overview of the Use of Oxygenates in Gasoline*, at 1, 9-10 (September 1998) (2 JS tab 3); Letter from Tom Soto, P.S. Enterprises, to Assemblywoman Denise Moreno Ducheny (25th August 1997) (11 JS tab 221).

8. Statements by individual California politicians thereafter declaring the need or desire for ethanol incentives that could conversely harm MTBE and methanol did not reflect California law, but only their own or their constituents' aspirations; even less so did statements by lobbyists or interested citizens reflect California law<sup>15</sup>. For example, Methanex's Second Amended Statement of Claim and Reply do not cite or quote statements of Californian *elected politicians* that are on point. The closest citations offered are to distant hearsay involving State Senator Burton, which is considered below, and a remark by State Senator Hayden to the effect that he prefers a "Midwest" fuel source to a "Middle East" one<sup>16</sup>. Officials at the CARB admitted that they would like to see the development of an in-state industry<sup>17</sup>. However, such statements did not signify that such programs were either enacted by California or were connected to an intent by California to harm methanol. Indeed, in 2002, California state legislation to provide incentives for the in-state production of ethanol and other qualifying liquid fuels was proposed - but it was not enacted<sup>18</sup>.
9. **Dot 2:** Methanex's invitation to the Tribunal to view the leakage of MTBE from USTs as a pretext for favouring the ethanol industry<sup>19</sup> cannot be accepted, as there is ample evidence in the record that leaking USTs and water contamination were perceived as a serious and urgent problem by the California Government, as well as by the California public at large<sup>20</sup>. The fact that the ethanol industry might see a silver lining in this crisis and anticipate economic benefits for

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<sup>15</sup> For sample statements by interested parties, see Cal. Envtl. Policy Council, Public Hearing, Transcript of Proceedings: Meeting To Consider Staff Reports on the Environmental Fate and Transport and Potential Health Effects of Using Ethanol in California Reformulated Gasoline, at 69 (18th January 2000) (comments of Lloyd Forrest, TSS Consultants-a company involved in "risk assessment" for ethanol investors); *Id.*, p. 70 (comments of Necy Sumait, Manager for Arkenol Holdings, an ethanol project).

<sup>16</sup> Second Am. Claim para. 278 (quoting California State Senator Tom Hayden, expressing a preference for a domestic fuel source).

<sup>17</sup> Reply, paras. 95-96. James Boyd, of the California Energy Commission (CEC), also spoke indirectly of interest in promoting an in-state industry, Second Am. Claim, para. 157.

<sup>18</sup> S. 1728 (Cal. 2002); Reply at tbl. 1, para. 100.

<sup>19</sup> Second Am. Claim, para. 152.

<sup>20</sup> A number of events prior to the passage of Senate Bill 521 raised concerns in California. Am. Defense, paras. 42, 45-47. These concerns regarding leaking USTs and water contamination yielded a number of proposed resolutions in 1997 and 1998, which were summarised in the UC Report. Graham E. Fogg et al., Impacts of MTBE on California Groundwater, in UC Report Vol. IV: Ground & Surface Water, App. A, pp. 69-71 (4 JS tab 39A).

itself if MTBE were banned from California reformulated gasoline or that the ethanol industry would support legal measures designed to accomplish this (since such measures would suit its own interests) is not by itself proof that California was engaged in a complex covert action whose objective was to help the ethanol industry and to harm methanol producers by banning MTBE.

10. Furthermore, the chronology and substance of the chain of events which ultimately led to the MTBE ban indicate that concerns surrounding leaking USTs were not a mere pretext. The Preamble to the California Executive Order issued by Governor Davis on 25th March 1999 states that it was premised on the finding that the concerns about MTBE leaking from underground fuel storage tanks were justified and did, in fact, pose a significant threat<sup>21</sup>. As recorded above, this conclusion was reached after considering the "findings and recommendations of the U.C. report, public testimony, and regulatory agencies"<sup>22</sup>.
11. Moreover, these findings and recommendations were not produced by a special interest group or at the behest of a handful of state politicians. Rather, the investigation into the concerns regarding MTBE and leaking USTs was mandated by California Senate Bill 521. The Senate Bill was passed unanimously by the California Legislature in October 1997; and, among other things, directed the University of California to conduct a study of the benefits and risks associated with MTBE<sup>23</sup>. As already noted, Methanex does not now include the

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The Government's and public's perception of a significant threat was later articulated at the public hearings held in February 1999 to discuss the findings of the UC Report. e.g., Testimony of James Giannopoulos, Principal Engineer for SWRCB, Transcript of Proceedings: Public Hearing to Accept Public Testimony on the University of California's Report on the Health and Environmental Assessment of MTBE, at p. 216 (19th February 1999) (15 JS tab 22 at 761).

Furthermore, evidence was presented corroborating the perceived threat, e.g., Fogg et al., *supra*, pp. 6, 25, 45; Graham E. Fogg, Expert Report Prepared for the Office of the Legal Advisor, US State Dep't, pp. 10-11, 38-39 (December 2003) (13 JS tab D); also 65 Fed. Reg. 16094 (24th March 2000) (18 JS tab 146).

<sup>21</sup> 1999 Cal. Executive Order D-5-99, pmb. (stating the basis for the order); e.g., Am. Defense, para. 123.

<sup>22</sup> *Ibid.* The subsequent regulations adopted by the California Air Reserve Board - the California Reformulated Gasoline Phase 3 (CaRFG3) standards - were similarly based upon the finding that MTBE leaking from USTs posed a threat that could not be addressed solely by upgrading the tanks. Cal. Air Reserve Bd., Res. 99-39, at pp. 6-7 (9th December 1999) (16 JS tab 24); Am. Defense, paras. 71-72.

<sup>23</sup> S. 521, 1997-98 Reg. Sess. (Cal. 1997) (enacted). Prior to the passage of Senate Bill 521, the proposed bill was analysed and commented on by the California

Senate Bill 521 among the "challenged measures" in these proceedings<sup>24</sup>. The Senate Bill was passed more than a year before Governor Gray Davis took office<sup>25</sup>; and at a time when ADM, the USA's largest producer of fuel ethanol, was not considered a major campaign donor in California<sup>26</sup>.

12. Further demonstrating the long-standing nature of concerns about the consequences of MTBE, it is worth noting that Senate Bill 521 was not the first time that California considered taking steps to ban or to limit use of MTBE<sup>27</sup>. Moreover, an early version of Senate Bill 521 considered banning MTBE outright<sup>28</sup>. It seems that these early

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EPA and its Air Reserve Board. E.g., Cal. EPA, Office of Env'tl. Health Hazard Assessment, Short Form Analysis of SB 521 (14th April 1997) (11 JS tab 248); Cal. EPA, Office of Env'tl. Health Hazard Assessment, Short Form Analysis of SB 521 (8th May 1997) (11 JS tab 249); Cal. Air Reserve Bd., Bill Analysis of SB 521 (4th April 1997) (11 JS tab 240); Cal. Air Reserve Bd., Bill Analysis of SB 521 (8th May 1997) (11 JS tab 242).

It is not clear to what extent Methanex seeks to argue that Senate Bill 521 itself was a pretext. Methanex argues that the bill underfunded the UC Report and did not allocate sufficient time. Second Am. Claim, para. 112. Witnesses at the main hearing who were engaged in the study did not testify that the study was underfunded. Methanex also claims (though does little to substantiate) a tie from the ethanol lobby to Senator Mountjoy and in turn to his introduction of the Bill. *Ibid.* But Methanex does not make any direct assertion of Senate Bill 521 being a pretext - it is not one of the so-called challenged measures. Methanex notes, for example, that the bill called for an objective, thorough study. *Id.*, paras. 111-112.

<sup>24</sup> Second Am. Claim at Part III.

<sup>25</sup> Governor Davis was elected in November 1998. Senate Bill 521 was signed by his predecessor, Governor Pete Wilson, who Methanex has described as unwilling to "give ethanol a 'marked advantage' over all other oxygenates". Second Am. Claim, para. 126. This supports the conclusion that Governor Wilson's approval of Senate Bill 521, which ultimately led to the removal of MTBE, was not intended to harm methanol or Methanex.

<sup>26</sup> Methanex has quoted the L.A. Times as saying, "ADM wasn't a major campaign donor in California until last year [1998]". Second Am. Claim, para. 217. The role of ADM is discussed further infra "Dot 4". The Tribunal notes that elsewhere Methanex argued that the ethanol lobby began trying to influence California politics as early as 1997. Transcript Day 1, p. 163 (lines 1-19).

<sup>27</sup> Cf. Supp. Aff. of Robert T. Wright, 29th January 2003, para. 6 (12 JS tab A) (indicating that Senate Bill 521 was not the first legislative attempt); cf. also S. 1186, 1995-96 Reg. Sess. (Cal. 1995) (not enacted) (a bill introduced to prohibit use of MTBE as a gasoline additive).

<sup>28</sup> Cal. Air Reserve Bd., Bill Analysis of SB 521 (8th May 1997) (11 JS tab 242) (indicating that the proposed Senate Bill 521 was amended, eliminating an immediate ban).

proposals, which preceded the election of Mr Davis and any interaction he may have had with ADM or the ethanol lobby, arose because of serious concerns among Californians over their groundwater. At the time of these proposals, however, requisite studies to substantiate their concerns had not been performed and so adequate data, as were ultimately mandated and funded by the Senate Bill 521, were not yet available.

13. **Dot 3:** Methanex argues that ADM supported a ban of methanol, that this influenced California's decision-making process, and that this, in turn, is evidence that the ban was discriminatory and intended to favour ethanol generally and ADM particularly<sup>29</sup>. Methanex points to the record of conviction of several ADM officers for price-fixing in another industry in which ADM is engaged; sequential contributions which ADM made to Mr Davis's political campaign; and the meeting over dinner which ADM hosted for then-Lieutenant Governor Davis. These are, as it were, a series of "dots" which Methanex urges the Tribunal to connect and then to link to the content of the Executive Order which Governor Davis issued once in office.
14. It is acknowledged by both Disputing Parties that ADM made contributions to the 1998 gubernatorial campaign of Gray Davis, and that ADM met with Mr Davis at a private dinner. The legal implications of these events will be examined below<sup>30</sup>. The Tribunal turns first to another of Methanex's allegations.
15. It is a matter of record that approximately eight years ago three ADM officials were indicted for fixing the price of lysine, an animal feed supplement. In 1998, they were found guilty and ultimately sent to prison<sup>31</sup>. Methanex contends that these convictions, along with the other events in question, show that political manipulation

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<sup>29</sup> Second Am. Claim at Section VI.E; Transcript Day 1, p. 195 (lines 8-10) ("[M]ethanol, because of ADM's contributions to Davis, was denied the best treatment accorded to ethanol").

<sup>30</sup> *Infra* "Dot 4"; "Dot 5".

<sup>31</sup> *United States v. Andreas*, 216 F.3d 645 (7th Cir. 2000) (affirming convictions for conspiring to violate § 1 of the Sherman Antitrust Act) (21 JS tab 3). In 1996 ADM agreed to plead guilty to price-fixing charges and to pay a fine of one hundred million dollars to the US government. ADM was also one of five companies fined by the European Commission for operating a price-fixing cartel. Second Am. Claim para. 214; Grain Group to Pay \$100m Fines, *Fin. Times* (London), 15th October 1996, at 1 (7 JS tab 105); Press Release, European Commission, Commission Fines ADM, Ajinomoto, Others in Lysine Cartel (7th June 2000) (7 JS tab 95).

was ADM's standard operating procedure. However, ADM is a large, diversified corporation, with numerous divisions. The Tribunal has no legal basis for concluding that one unlawful activity of a corporation which leads to a criminal conviction of some of its officers transforms that entity into a criminal organization for all purposes—either tainting per se all other actions by any division, subsidiary or other vehicle, no matter how separate or remote its activities from those upon which the conviction was based; or creating a presumption of unlawful behaviour in all other areas and thereby shifting the burden of proof. The fact that three ADM officers engaged in criminal activity in another part of the large corporation's business is not proof and, moreover, does not even provide a basis from which to infer that ADM engaged in criminal or illegal activity with respect to the enactment of the MTBE ban from California gasoline.

16. Furthermore, ADM's activities are not tantamount to those of California. It would be extreme to find the Government of California culpable simply because the field or industry is inhabited by some bad private actors.
17. **Dot 4:** In the USA, as in a number of other countries<sup>32</sup>, political campaigns at the federal and state level may accept private financial contributions, subject to the relevant legal strictures. Some other countries prohibit donations from corporations<sup>33</sup>, but no rule of international law was suggested as evidence that the USA and other nations which allow private financial contributions in electoral campaigns are thereby in violation of international law.

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<sup>32</sup> The Tribunal notes, by way of background which is illuminating but not pertinent to this decision, that various countries allow private contributions, including Australia, France, Brazil, India, Greece, Italy, Japan, and Germany. Over the past decade, many countries that allow political giving have placed new restrictions on corporate donations and have required increased disclosure. For example, Japan introduced various limits in the 1990s; Germany and France introduced new campaign finance requirements more recently.

<sup>33</sup> As further background material, the Tribunal notes that there are countries that do not allow corporations to make campaign contributions. France, for example, banned donations from private sector corporations in 1995. Some countries, like Canada and the UK, also place some limits on the amounts that can be spent on campaigns. The laws in the United States are more liberal than most other countries. For such background discussion, see, for example, Karl-Heinz Nassmacher, *Party Funding in Continental Western Europe, in Funding of Political Parties and Election Campaigns* 117-37 (Int'l Inst. For Democracy & Electoral Assistance, Reginald Austin & Maya Tjernstrom eds., 2004).

18. There are three main approaches to regulating campaign contributions in the United States: (i) requiring disclosure; (ii) limiting contribution; and, to a lesser extent, (iii) providing for public financing of campaigns. These generalisations are true of both state and federal election law. There are, however, important differences between federal and state election law. While US law does not permit corporations to support candidates for federal office<sup>34</sup>, it was not contested that states may allow corporations to make contributions to candidates for state-level positions<sup>35</sup>.
19. Because the contributions at issue in this case were those made to Mr Davis, a candidate for state office and later a state elected official, the California state code and regulations are the relevant sources of law. The Tribunal need not delve far into the specific details of California's regulatory regime, other than to note, for the purposes of this case, that Mr Davis's acceptance of contributions from ADM did not violate any relevant election law<sup>36</sup> and Mr Davis met the requirements, discussed below, that such contributions be publicly disclosed in a prescribed form and in a timely fashion. As indicated above, Methanex does not contend otherwise.
20. At the time of Mr Davis's candidacy and gubernatorial election in 1998, California, like a number of other states, did not limit the amount that individuals or corporations could contribute to candidates<sup>37</sup>. However, California required candidates for state offices to report contributions received and expenditures made during cam-

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<sup>34</sup> 2 U.S.C. § 441b(a); *McConnell v. Fed. Election Comm'n*, 124 S.Ct. 619, 694 n.86 (2003) (23 JS tab 36).

<sup>35</sup> It is a matter of background material not pertinent to the decision at-hand that more than half of states currently do allow for such contributions, albeit generally in limited amounts. For such background materials, see Brief of Amici Curiae, States of Iowa et al. at 22, *McConnell v. Fed. Election Comm'n*, 124 S.Ct. 619 (2003) (No. 02-1674 et al.) (citing background materials); Nat'l Conference of State Legislatures, *How States Regulate Money in Elections*, at <http://www.ncsl.org/programs/legman/about/campfin.htm>.

<sup>36</sup> E.g., Second Am. Claim, para. 143.

<sup>37</sup> As of 1996 California state law only limited contributions for special elections. In November 1996, California voters approved Proposition 208 which amended the Political Reform Act of 1974 and established, among other things, limits on campaign contributions. However, Proposition was enjoined by a US District Court in January 1998, *California ProLife Council PAC v. Scully*, 989 F.Supp. 1282 (E.D. Cal. 1998). E.g., Letter from Dick Vind to Marty Andreas (16th July 1998)(mentioning Proposition 208 and the district court's decision) (5 JS tab 58).

paigns<sup>38</sup>. The manner in which this was to be done was established in the 1974 amendments to California's Political Reform Act and codified in the California Code<sup>39</sup>. In addition, the Online Disclosure Act of 1997 required Mr Davis to adhere to the procedures established by the Secretary of State to facilitate public access to the disclosed information via the Internet<sup>40</sup>.

21. In summary, Mr Davis's acceptance of contributions from ADM did not violate California's election laws or regulations. Methanex does not allege, and it does not appear to the Tribunal, that Mr Davis's acceptance of contributions from ADM violated any of California's election laws or regulations. In fact, Methanex made clear that it did not allege that Mr Davis behaved criminally or in violation of the campaign contribution regime then in place<sup>41</sup>. Yet, Methanex maintains that "ADM and the ethanol lobby instigated the California ban"<sup>42</sup> and that the relationship between ADM and Mr Davis constituted "political corruption"<sup>43</sup> as ADM had an "undue influence"<sup>44</sup> on events in California because of its contributions.
22. The USA argues that this is an untenable position or at least one that raises a question as to the conclusions that Methanex would like the Tribunal to draw. According to the USA, if ADM's contributions influenced or affected the outcome of Mr Davis's decision-making, then this would constitute a legal violation; therefore, to establish undue influence, Methanex would, at least, have to be in a position to allege, if not also to demonstrate, that a legal violation took place<sup>45</sup>.

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<sup>38</sup> Cal. Sec'y of State, Political Reform Division, at <http://www.ss.ca.gov/prd/prd.htm> (16 JS tab 34). During the relevant time period for this case, the central disclosure requirements were set forth by California's Political Reform Act of 1974. Cal. Gov. Code § 81000 et seq.

<sup>39</sup> The general statutory instrument for California election law may be found at Cal Gov. Code §84200 et seq.

<sup>40</sup> Cal. Gov. Code § 84600 et seq.; Am. Defense, para. 180, n.33.

<sup>41</sup> E.g., Second Am. Claim, para. 143. In the Partial Award, the Tribunal noted that Methanex had not argued that any violations of US or California campaign contribution or criminal law had taken place. Partial Award para. 70. During the main hearing, Methanex again conceded that it could not establish any "quid pro quo". Transcript Day 1, pp. 135, 180.

<sup>42</sup> Reply at Sub-section II.B.3. Earlier in the Reply, Methanex stated, it was "improper influence-bought by ADM's contributions-that triggered Davis'[s] MTBE ban in the first place". Id.,para. 5.

<sup>43</sup> Transcript Day 1, p. 135 (line 8).

<sup>44</sup> Id., p. 136 (line 15) (internal quotation marks omitted); Reply, para. 69.

<sup>45</sup> Transcript Day 2, p. 409 (lines 1-21); Rejoinder, para. 72 (emphasis added).

23. The Tribunal notes that Methanex's argument is, at times, difficult to pin down - sometimes seeming to represent that the type of impermissible exchange took place which Methanex otherwise disavows. For example, in its Reply, Methanex claims that the "only reasonable inference" from the record is that "*in exchange for* [political contributions], the U.S. ethanol industry became the sole supplier for the California oxygenate market . . ." <sup>46</sup>. The Tribunal observes that California's Penal Code prohibits an official from accepting monies with "any . . . understanding that his vote, opinion, or action . . . shall be influenced thereby" <sup>47</sup>. However, further exploration of California's legal doctrine surrounding undue influence is unnecessary; turning to the question of whether there is a basis from which to infer that there was such undue influence, the Tribunal finds that the simple fact that ADM made political contributions does not, alone, suffice to support Methanex's allegations. While the Tribunal is not, as Methanex puts it, "so naïve that it will *refuse* to believe that even after [Mr] Davis solicited ADM's money, ADM received nothing in return" <sup>48</sup>, the Tribunal similarly will not be so rash as to *assume* this without an evidentiary basis from which to make this inference.
24. Methanex proposes that the US Supreme Court's decision in *McConnell v. Federal Election Commission* <sup>49</sup> provides such a basis <sup>50</sup>. In *McConnell*, the Supreme Court confirmed the constitutionality of the Bipartisan Campaign Reform Act (BCRA) of 2002, which amended the federal campaign contribution regime to address certain manifest abuses <sup>51</sup>. To summarise briefly: aiming both to prevent corruption and to reduce the appearance of impropriety in the federal election system <sup>52</sup>, BCRA bans "soft money" donations to national political parties <sup>53</sup> and places various restrictions on the fundraising activities

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<sup>46</sup> Reply, para. 70; Transcript Day 1, p. 184 (lines 1-5) ("Methanex submits that . . . in California between 1999 and 2000 . . . [t]he United States ethanol industry captured the quid pro quo process and used it for its own ends".).

<sup>47</sup> Cal. Penal Code § 68; Rejoinder, para. 72 .

<sup>48</sup> Reply, para. 3 (emphasis added).

<sup>49</sup> 540 U.S. 93, 124 S.Ct. 619 (2003).

<sup>50</sup> E.g., Reply, paras. 42-44.

<sup>51</sup> *McConnell*, 124 S.Ct. at 626-27 (regarding the constitutionality of Bipartisan Campaign Reform Act of 2002, Pub. L. No. 107-155). The BCRA-codified at 2 U.S.C. § 431 et seq.-amended the Federal Election Campaign Act of 1971, the Communications Act of 1934, and other portions of the United States Code. Id.

<sup>52</sup> *McConnell*, 124 S.Ct. at 628.

<sup>53</sup> 2 U.S.C. § 441i(a); *McConnell* (discussing § 441i and other sections discussed below). Soft money refers simply to political donations that are given in such a way as to avoid legal regulation. Following the BCRA, all donations - including those to political parties for supposedly general "party building" activities - are subject

of federal officeholders<sup>54</sup>, as well as on certain types of advertisements for federal candidates<sup>55</sup>. (The BCRA is focussed on regulating federal political campaigns and the central components of the legislation do not impact state elections<sup>56</sup>.)

25. At the main hearing, Methanex suggested that the Supreme Court's holding in *McConnell* and statements by the Solicitor-General while arguing the case before the Court provide a basis for permissible inference of the corruption of the political contribution regime in California (and indeed, across the United States)<sup>57</sup>. If this were correct, it would greatly simplify Methanex's burden of proof: Methanex's contention would allow the Tribunal to infer that every elected official at the state or federal level, whether in the executive, legislative or judicial branches, who had campaigned and received campaign contributions was per se corrupt.
26. However, Methanex's contention here is, in the opinion of the Tribunal, a misreading of the judgment of the Supreme Court and the intentions of the United States Congress as expressed in the BCRA legislation. In the course of its landmark decision in *McConnell*, the Court took notice of and confirmed congressional statements of the hazards of the pre-existing campaign contribution regime<sup>58</sup>.
27. The US Government, and in turn the Supreme Court, relied upon "a

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to regulation.

<sup>54</sup> E.g., 2 U.S.C. §§ 441i(d); 441i(e).

<sup>55</sup> E.g., 2 U.S.C. § 441b(b)(2).

<sup>56</sup> Only a handful of BCRA's provisions apply to state-level politics. For example, candidates and state or local parties cannot accept "soft money" donations from foreign nationals. 2 U.S.C. § 441e. Also, any campaign activity a state political party engages in on behalf of a federal candidate must be paid for with "hard money" (i.e., money that is raised subject to the legal constraints on political contributions). 2 U.S.C. §§ 431(20)(A), 441i(b).

<sup>57</sup> E.g., Transcript Day 1, p. 131 (lines 1-6) ("Methanex believes that the Supreme Court's findings in that opinion and what was said by the Solicitor General, conclusively validate Methanex's position here."); *id.*, p. 139 (lines 1-4) (describing it as a "permissible inference"). But at least at one point during the main hearing, Methanex seemed to acknowledge that *McConnell* alone could not supply the basis for an inference. Counsel for Methanex noted, "*The issue is whether* this type of political corruption that the Solicitor General and the United States Supreme Court is referring to [in *McConnell*], took place here". Transcript Day 1, p. 135 (lines 7-10) (emphasis added).

<sup>58</sup> E.g., *McConnell*, 124 S.Ct. at 628.

treasure trove of testimony from Members of Congress, individual and corporate donors, and lobbyists, as well as documentary evidence"<sup>59</sup>. The Court found that the record offered sufficient evidence to support Congress' decision to enact the BCRA's various measures - that is, the regulations were justified despite competing constitutional interests. For example, with regard to the Act's ban on soft money contributions, the Court noted that the "record [was] replete with examples . . . of national party committees peddling access to federal candidates and officeholders in exchange for large soft-money donations"<sup>60</sup>. (It is worth noting that the BCRA's factual record was principally based upon a Senate investigation into campaign practices related to the 1996 federal election<sup>61</sup> - thus neither the conclusions drawn by Congress in passing the legislation, nor the Solicitor General in defending it, nor the Supreme Court in upholding it reflects a factual assessment of state election concerns.)

28. In sum, the Tribunal concurs with the summary offered by the United States during the main hearing:

*"The Supreme Court upheld the regulation[s] at issue in the McConnell case, finding that they did not run afoul of U.S. constitutional protections for free speech. Congress did not determine that all campaign contributions were corrupting. It did not outlaw all such campaign contributions. That the possibility or appearance of corruption justified regulation does not and cannot support a finding that by virtue of making or receiving a lawful contribution there is corruption"<sup>62</sup>.*

29. Following the BCRA and the *McConnell* decision upholding all key aspects of the Act, private financial contributions to federal candidates remain lawful under a regulatory regime that requires notice and transparency, and sets limits on who may contribute and how much can be given. Moreover, the legality of contributions to state candidates by domestic corporations is unchanged by either the legislation or the Court's holding in *McConnell*.
30. Given all of this, the introduction of *McConnell* as evidence does not illuminate the facts in this case. The campaign contributions that Mr Davis received from ADM are not, by themselves, evidence that he

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<sup>59</sup> Reply, para. 43 (internal quotation marks omitted) (citing Brief for the Federal Election Commission).

<sup>60</sup> *McConnell*, 124 S.Ct. at 664.

<sup>61</sup> E.g., *id.*, p. 648, 652.

<sup>62</sup> E.g., Transcript Day 2, pp. 410-11 (lines 16-21, 2-3).

was committed, by and in return for such donations, to change the law in California to favour ethanol and to harm MTBE, methanol, or Methanex. Unlike Congress in *McConnell*, Methanex has not alleged the type of record - the "treasure trove of . . . evidence" so to speak - that, if proven, would allow the Tribunal to draw such a conclusion. Rather, Methanex attempts to make its case primarily by analogy and by presenting the timeline of ADM's donations without reference to other critical events<sup>63</sup>. Neither of these attempts is persuasive. After considering ADM's donations within the broader context of political events in California occurring at that time, the Tribunal cannot find Methanex's case proven in this case.

31. The first donation that Methanex highlights is a contribution by ADM to then- Lieutenant Governor Davis's gubernatorial campaign in late May 1998<sup>64</sup>. As noted earlier, this was long after the critical passage of Senate Bill 521, which commissioned the UC Report and effectively laid the groundwork for the ban by requiring that the governor take "appropriate action to protect public health and the environment"<sup>65</sup> "based solely upon the [UC Report]. . . and any testimony presented at the public hearings"<sup>66</sup>.
32. As Methanex points out, ADM also made a number of contributions to Mr Davis between August 1998 (following a meeting between ADM officials, Mr Davis, and others which is discussed at length below)

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<sup>63</sup> In two respects, Methanex argues by analogy - offering evidence that is one or more steps removed from the case before us. First, Methanex suggests that Mr Davis was influenced, on matters unrelated to ethanol, MTBE, or methanol, by financial contributions by other donors. Second Am. Claim, paras. 218-220 (citing journalists' opinion pieces to support these claims). Second, Methanex also points to ADM's practices of making political contributions and lobbying in other parts of the United States. E.g., *id.*, at para. 209 (noting contributions to federal candidates); Reply, para. 55 (describing ADM's characterisation of methanol as foreign).

Methanex also tries to draw an attenuated connection between ADM and Senator Mountjoy, who authored Senate Bill 521. However, Methanex does not provide any information about any financial connection between ADM and Senator Mountjoy, and ultimately simply states that he had been "using the issue [of MTBE] to widen his political base". Second Am. Claim, paras. 210-211. This could be true - Senator Mountjoy had long been involved in the issue and had authored a number of environmentally-related bills - but the Tribunal cannot see how this conjecture assists Methanex's case.

<sup>64</sup> Transcript Day 1, p. 167 (lines 19-20).

<sup>65</sup> S. 521, 1997-98 Reg. Sess. § 3(f) (Cal. 1997) (enacted).

<sup>66</sup> *Id.*, § 3(e).

and September 1999<sup>67</sup>. The second largest single contribution that ADM made to Mr Davis was a \$50,000 donation in September 1999 - roughly 25% of ADM's total donations to his campaign<sup>68</sup> - long after the Executive Order had been issued. In the months following these donations, Governor Davis "pressed the federal government to waive technical provisions of the Clean Air Act to allow California refiners to meet the smog standards with new fuel mixes other than ethanol"<sup>69</sup>. In October 1999, the California legislature passed Senate Bill 989, which "largely codifies into statute [Governor Davis's] Executive Order D-5-99"<sup>70</sup>.

33. Finally, although Methanex argues that ADM's contributions were significant<sup>71</sup>, in total they constituted less than one percent of Mr Davis's 1998 campaign budget<sup>72</sup>. Moreover, it seems that MTBE producers and other petrochemical companies were equally active campaign contributors<sup>73</sup>.

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<sup>67</sup> Second Am. Claim, para. 229; Transcript Day 1, pp. 167-68.

<sup>68</sup> Second Am. Claim, para. 229; Transcript Day 1, p. 168.

<sup>69</sup> Dan Morgan, In Energy Bill, A Daschle Nod to Key Farm States; Ethanol Provision Spurs Lobbying Fight, Wash. Post, 19th February 2002, at A4 (7 JS tab 120); Letter from Gray Davis, Governor of California, to Carol B. Browner, Administrator, U.S. EPA (12th April 1999) (6 JS tab 62); Am. Defense, paras. 64-67.

The Executive Order itself required state agencies to seek a waiver of the federal reformulated gasoline oxygenate requirement; this would allow California to meet air quality standards without using ethanol. 1999 Cal. Executive Order D-5-99 para. 2; Transcript Day 2, pp. 293-94 (lines 18-21, 1-3).

<sup>70</sup> Cal. S. Comm. on Envtl. Quality, Analysis of S. 989, 1999-2000 Reg. Sess., 12th April 1999 (18 JS tab 129); S. 989, 1999-2000 Reg. Sess. (Cal. 1999) (enacted).

<sup>71</sup> E.g., Transcript Day 1, p. 179.

<sup>72</sup> Cal. Sec'y of State, Candidates for Constitutional Offices Complete Financial Activity (1998 Election), [http://www.ss.ca.gov/prd/finance98\\_general\\_final/financial\\_const.htm](http://www.ss.ca.gov/prd/finance98_general_final/financial_const.htm) (16 JS tab 32 at 1275).

<sup>73</sup> Am. Defense, para. 178 (citing relevant contribution documents); Transcript Day 2, at 412 (lines 5-20) ("[T]he record contains evidence showing that Arco contributed approximately the same amount as did ... ADM . . . to Governor Davis's campaign"). As a foreign corporation, Methanex and its US subsidiaries were, by law, prohibited from contributing to Davis's campaign (or to other state or federal elections). Nonetheless, according to at least one source, Methanex Corporation's US subsidiary tried to donate \$10,000 to the Democratic National Committee and \$15,000 to the Republican National Committee. Damon Chappie, Republicans Return Illegal Donation from Canadian Company, Roll Call, 21st October 1996, at 1 (25 JS tab 10 at 2938-39).

34. **Dot 5:** As recited already many times, Methanex places considerable emphasis on the meeting over dinner held on 4th August 1998, which was hosted by ADM in Decatur, Illinois, the seat of its offices, for then-Lieutenant Governor Davis<sup>74</sup>. Methanex submits that the events at the dinner, along with the other bases of inference, confirm that there was an intent to favour ethanol and to injure methanol and Methanex<sup>75</sup>.
35. The participants at the dinner were, in addition to then-Lieutenant Governor Davis, who was accompanied by Messrs Richard Vind and Daniel Weinstein, Martin Andreas, Alan Andreas and Roger Listenberger. Messrs Andreas, Andreas and Listenberger were all officers of ADM at the time. The dinner, which took place at the Decatur Country Club, lasted one and a half to two hours<sup>76</sup>.
36. In the absence of contrary evidence, one would assume that, in the US political context, this sort of encounter would allow a candidate to present himself or herself to potential contributors and contributors to present themselves to the candidate. The candidate would be seeking financial support for his or her election, while the putative contributor would be assessing whether the candidate, once in office, would be accessible to hear its views and concerns on matters of interest to it. The contributor would be looking for what Mr Vind, Chairman and Chief Executive Officer of Regent International (an ethanol supplier)<sup>77</sup> and a witness for the USA who acknowledged that he often had contributed to political campaigns, called "access"<sup>78</sup>.
37. The Disputing Parties agreed, as did Mr Vind, that if the encounter became one of a promise to do something in return for a contribution - a "quid pro quo" - it would be unlawful.<sup>79</sup> Moreover, the Tribunal concludes that if there were proof that the banning of MTBE in California reformulated gasoline, its replacement by ethanol and the impact of all of this on Methanex were extensively discussed at

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<sup>74</sup> E.g., Second Am. Claim, paras. 222-232; Reply at Sub-section II.B.5 ("Gray Davis Meets the U.S. Ethanol Industry").

<sup>75</sup> E.g., Transcript Day 1, p. 237 (lines 8-12) (explaining that Methanex's view is that the Executive Order "flowed" from ADM's contributions and from the August 4th dinner meeting).

<sup>76</sup> Transcript Day 4, p. 847 (line 17) (Mr Roger Listenberger); Second Am. Claim, para. 222 (draft itinerary allotted less than two hours).

<sup>77</sup> Witness Statement of Richard Vind, 21st November 2003, para. 2 (13A JS tab I).

<sup>78</sup> Transcript Day 4, pp. 988 (line 7), 991 (line 4) (Mr Richard Vind).

<sup>79</sup> Id., p. 992 (lines 1-2).

the dinner, *then* (ignoring the narrow restrictions on the Governor imposed by California Senate Bill 521), the timing of the dinner and the contribution of campaign funds could suggest a deal, or a quid pro quo, which would be unlawful and, also, satisfy in this case the intent requirement for Article 1101, as well as for Articles 1102, 1105 and 1110 NAFTA.

38. However, the Tribunal again notes that Methanex concedes that it cannot offer such proof: "[W]e cannot prove . . . anything criminal. We can't prove any quid pro quo. We can't prove any handshake deal"<sup>80</sup>. Thus, the question the Tribunal turns to is whether the evidence adduced can even support, by way of inference, Methanex's view of the dinner - that is, whether there is sufficient circumstantial evidence to justify inferring that the exchange at the dinner was unlawful.
39. To support its contentions, Methanex proffers several pieces of circumstantial evidence: what it claims to be the "secrecy" of the meeting,<sup>81</sup> the presence of ethanol executives from ADM at the meeting<sup>82</sup>, and more general concerns (e.g., statements made in other contexts by ADM executives about methanol and ethanol<sup>83</sup>, and - as already described above - the criminal activity of ADM officers in another industry and place).
40. The Disputing Parties disagree as to whether the dinner was, as Methanex contended, "secret". While the dinner was not advertised, the flight which ADM provided then-Lieutenant Governor Davis and his party on an ADM plane was reported by Mr Davis on the appropriate campaign donation form<sup>84</sup>. Counsel for Methanex suggested that Illinois State police provided a traffic escort which accompanied the Lieutenant Governor's party from the airport in Decatur to the Decatur Country Club where the dinner was held<sup>85</sup>; and the dinner was later reported in the business press<sup>86</sup>. Thus the adjective "secret"

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<sup>80</sup> Transcript Day 1, p. 180 (lines 11-14).

<sup>81</sup> E.g., Reply, para. 61.

<sup>82</sup> E.g., Second Am. Claim, paras. 223-227.

<sup>83</sup> E.g., *id.*, para. 228 (noting that participants in the meeting were "known to have condemned methanol . . . as a 'foreign' product").

<sup>84</sup> Am. Defense, para. 126, n.218 (citing proper forms, on record at 18 JS tab 28). There was no obligation to make further disclosures. *Id.*, paras. 177, 180; Rejoinder, paras. 59-60; Transcript Day 2, p. 402 (lines 8-20); *McCormick v. United States*, 500 U.S. 257, 272 (1991); *Bruce v. Riddle*, 631 F.2d 272, 280 (4th Cir. 1980).

<sup>85</sup> Transcript Day 4, p. 800 (lines 10-11) (Ms Claudia Callaway).

<sup>86</sup> E.g., Second Am. Claim, para. 232 .

seems excessive; and a more appropriate modifier would be "private". The Tribunal cannot infer that a private dinner to which representatives of the media were not invited is, for that reason, "secret" or that it is redolent per se of some illegality.

41. Methanex has submitted that the singular purpose of this dinner was to discuss ethanol and methanol with then-Lieutenant Governor Davis<sup>87</sup>. Nothing in the record supports that contention. Of the ADM participants present, only Mr Roger Listenberger was exclusively involved with ethanol for the company. Each of the three witnesses - Messrs Listenberger, Weinstein, and Vind - who attended the dinner testified that the subject was discussed only marginally<sup>88</sup>.
42. Mr Listenberger, then ADM Vice-President in charge of marketing fuel ethanol, testified that he was asked to attend to answer questions that might be raised about ethanol<sup>89</sup>, but he stated that ethanol was not discussed "very much," and that it only "came up a few times"<sup>90</sup>. He explained:

*"One time in specific that I remember is as we were preparing to leave or walking out of the room, I asked Mr Davis if he felt that in the upcoming election if MTBE would be an issue because it was getting a lot of press at that time as a serious groundwater contamination problem, and I asked him about that, and he said, no, he didn't think it would be an issue<sup>91</sup>."*

Mr Listenberger testified that neither methanol nor Methanex were discussed at the dinner<sup>92</sup>.

43. Mr Daniel Weinstein, a banker who at the time worked as a volunteer in Mr Davis's campaign<sup>93</sup>, was in Chicago for a meeting that Mr Davis was holding with labour leaders. He was then invited to accompany Messrs Davis and Vind to Decatur<sup>94</sup>. Mr Weinstein testified, in response to a question about the conversation at the dinner:

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<sup>87</sup> Id., para. 223 ("It is apparent . . . that there was only one issue on the agenda for the meetings: ethanol".).

<sup>88</sup> Discussion infra of their testimony.

<sup>89</sup> Transcript Day 4, p. 803 (lines 12-13) (Mr Roger Listenberger).

<sup>90</sup> Id., p. 775 (line 4).

<sup>91</sup> Id., p. 775 (lines 8-15).

<sup>92</sup> Id., p. 775 (lines 16-21).

<sup>93</sup> Id., p. 815 (Mr Daniel Weinstein).

<sup>94</sup> Id., p. 816-17.

"[T]hey just talked about the company and what they did, some of their various products [,] the countries they were in. Just kind of an overview, nothing really specific, but very general"<sup>95</sup>. Mr Weinstein testified that he did not recall any discussion of ethanol, methanol or MTBE<sup>96</sup>.

44. Mr Richard Vind of Regent International, which sought to promote the use of ethanol as a fuel additive<sup>97</sup>, arranged the meeting of then-Lieutenant Governor Davis with ADM officials<sup>98</sup>. Mr Vind explained in his witness statement:

*"9. On August 4, 1998, I met Gray Davis at Meggs Field Airport in Chicago. Mr. Davis was late to arrive, and the weather had deteriorated, which required us to amend our flight plan and itinerary. Because of the late arrival in Decatur, we were forced to abandon the scheduled plant tour and went instead directly to the Decatur Country Club, where we arrived at about 8:00 p.m. Because of the late arrival, ADM Chairman Dwayne Andreas was not available, so, as I recall it, the attendees included Rick Reising, then-ADM General Counsel, Marty Andreas, Vice President, Allen Andreas, CEO, and Roger Listenberger, ADM sales executive. In addition to these ADM executives, Dan Weinstein, a Davis supporter, was present along with myself.*

*10. The conversation at dinner was about Gray Davis's election campaign, and ADM's business. Neither methanol nor Methanex was discussed. I do not recall MTBE being a topic of discussion during the dinner.*

*11. Gray Davis and I left the dinner around 10:00-10:30 that night and returned by plane to Chicago's Meggs Field. I then escorted Gray Davis to his hotel, and returned to my hotel alone<sup>99</sup>."*

There are some minor discrepancies between the accounts of two of the witnesses (Mr Listenberger was certain that Mr Rick Reising, ADM's General Counsel, was not present at the dinner<sup>100</sup>, while Mr

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<sup>95</sup> Id., p. 819 (lines 7-10).

<sup>96</sup> Id., pp. 820-821.

<sup>97</sup> Witness Statement of Richard Vind, 21st November 2003, para. 2.

<sup>98</sup> Id., para. 6.

<sup>99</sup> Id., paras. 9-11.

<sup>100</sup> E.g., Transcript Day 4, p. 803 (line 4) (Mr Roger Listenberger).

Vind recalled that he was<sup>101</sup>), but the accounts are consistent in all major features; and the witnesses impressed the Tribunal as credible throughout the skilled cross-examination to which they were subjected by Methanex's Counsel.

45. Methanex also assembled statements by officers of ADM which, according to Methanex, reveal an intent critical to its central argument in this case<sup>102</sup>. However, statements touting ethanol or invoking nationalist imagery with respect to ethanol and methanol which were made in other fora and/or by ADM officers who did not attend the dinner and which Methanex recites in its written submissions are not relevant to what transpired at the dinner on 4th August 1998.
46. Legislation in democratic systems involves, by its nature, participation by a wide spectrum of private individuals and interest groups in addition to the members of the legislature and the executive, insofar as its endorsement is also necessary for a bill to become law<sup>103</sup>. While there may be circumstances in which facts would support an inference that one "invisible hand" was lurking behind and controlling a seemingly democratic process which had been elaborately contrived to conceal its machinations, it is clear beyond peradventure that the facts in the record do not warrant such an inference here.
47. **Dot 6:** As support for its inference of discriminatory intent, Methanex produced a witness statement by Mr Robert T. Wright, Methanex's Director of Government and Industry Relations. Mr Wright stated that he had been told, four years earlier, by an unnamed lobbyist for an unnamed trade association, of a statement allegedly made, at that time, by California Senator Burton. According to this source, Mr Burton reportedly said "[i]f you're here on the MTBE issue, you're [meaning out of luck]"<sup>104</sup>.
48. According to Mr Wright's paraphrase of what was recounted to him of what Senator Burton is alleged to have said, Mr Burton also reportedly stated that "if one wanted to benefit from the direction in which MTBE was headed, they could sell Methanex stock short"<sup>105</sup>. Mr Wright interprets this as evidence "that the intentions and effect

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<sup>101</sup> E.g., Witness Statement of Richard Vind, 21st November 2003, para. 9.

<sup>102</sup> E.g., Second Am. Claim, paras. 212, 228, 273-274.

<sup>103</sup> One participant group is paid lobbyists, which Methanex itself retained.

<sup>104</sup> Aff. of Robert T. Wright, 4th November 2002, para. 3 (Second Am. Claim at Exh. B); Supp. Aff. of Robert T. Wright, 29th January 2003, para. 13 (12 JS tab A).

<sup>105</sup> Aff. of Robert T. Wright, 4th November 2002, para. 3.

of the MTBE prohibition were directed at methanol" and that "the direct linkage between the pending decision by the Governor to ban MTBE and the predicted negative impact on Methanex's share price was clear"<sup>106</sup>.

49. To begin, this is double hearsay presented four years after the fact; yet Methanex presented it to the Tribunal, enclosed in quotation marks, as if it were a direct quote. Its evidentiary value is further frayed by the failure to identify the person who supposedly witnessed Senator Burton's statement and relayed it to Mr Wright. Furthermore, the Tribunal does not have any context in which to try to understand or interpret these comments.
50. Even if one ignores these problems, the statements, on their own terms, fail to prove the "direct linkage" which Mr Wright purports to find in them. Senator Burton's alleged comments were said to be made following (i) the passage of California Senate Bill 521; (ii) the release of the University of California Report; and not long before (iii) the issuance of the California Executive Order<sup>107</sup>, which California Senate Bill 521 required "within 10 days from the date of the completion of the public hearings"<sup>108</sup>. Such remarks could have been made by anyone aware of what was then happening in California, for by then the outcome was hardly unanticipated.
51. While the Tribunal has not assessed the credibility of additional memoranda which were submitted with Mr Michael Macdonald's affidavit and accompanying Methanex's Reply<sup>109</sup>, those documents indicate that, in the context in which they were allegedly uttered, Senator Burton would have been saying nothing extraordinary<sup>110</sup>. For example, in a memorandum at the end of January 1999, the lobbyist Ms Susan McCabe of Brady & Berliner wrote: "I think Burton's comments accurately reflected the general belief in the Legislature that MTBE will be phased out within a fairly quick time frame"<sup>111</sup>.

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<sup>106</sup> *Ibid.*

<sup>107</sup> Cf. Supp. Aff. of Robert T. Wright, 29th January 2003, para. 13.

<sup>108</sup> S. 521, 1997-98 Reg. Sess. § 3(e) (Cal. 1997) (enacted).

<sup>109</sup> Reply, para. 37, n. 54-55 (citing attachments to Mr Michael Macdonald's third affidavit); Memorandum from Susan McCabe, Brady & Berliner, to John Lynn (31st January 1998) (19 JS tab 13); Memorandum from Rose & Kindel (25th -29th January 1999) (19 JS tab 14A).

<sup>110</sup> Reply, para. 37 (citing January 1999 memos from Ms Susan McCabe of Brady & Berliner and from Rose & Kindel).

<sup>111</sup> *Ibid.* (internal quotation marks omitted) (quoting Memorandum from Susan McCabe, Brady & Berliner, to John Lynn (31st January 1999), at 2).

Even if the Tribunal were to assume that Senator Burton made the comments indicated by Mr Wright and arguably confirmed by Ms McCabe's memorandum, this does not suggest, let alone demonstrate, that Methanex or methanol was the target of the legislative initiative by California.

### **3) The Tribunal's Conclusion**

52. The Tribunal can understand Methanex's conviction that all of these "dots," if (i) they were to be taken as the only dots; (ii) they were to be accepted at face value as submitted by Methanex; and, moreover, (iii) they were carefully connected as Methanex proposes, would show that the "real" reason Governor Davis enacted Executive Order D-5-99 was to favour ethanol and to harm Methanex and methanol. Methanex's difficulties, however, are manifold.
53. For one thing, many of Methanex's individual dots do not withstand scrutiny. Far more damaging is the fact that there are other very important dots which Methanex ignores. There is a timeline indicating that the prohibitions against MTBE were passed by California<sup>112</sup>, with wide popular support. Methanex has alleged that the process by which the California ban was enacted was corrupted by campaign contributions from ADM to then-Lieutenant Governor Davis. But, as noted above, political contributions to candidates for office in the United States are not prohibited; and there is no allegation by Methanex, still less any indication in the record, that ADM's contributions were in violation of the law or that Mr Davis himself behaved in violation of the law in this regard. MTBE users also made sizeable contributions to Mr Davis's campaign.
54. Most importantly of all, Methanex cannot explain how its proposed theory deals with the fact that California Senate Bill 521, which mandated gubernatorial action regarding MTBE, was passed by the California legislature during the tenure of Mr Davis's predecessor, Governor Pete Wilson. Its implementation was contingent on findings by the scientific study to be conducted by researchers at the University of California, which was to be followed by public hearings, public testimony and peer review, whereupon the Governor (whoever he or she might have been) had no discretion to deviate from the

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<sup>112</sup> In addition to the Governor Davis's Executive Order, ultimate passage by the California government refers to S. 989, 1999-2000 Reg. Sess. (Cal. 1999).

results and recommendations of the study. As we have already found above, Governor Gray Davis followed the strict protocol and limited discretion required by California Senate Bill 521.

55. Methanex's contention that the California ban was designed to transfer the oxygenate market to ethanol founders on the very terms of the Governor's Executive Order and subsequent action, and is simply unsupportable on the evidence. Executive Order D-5-99 called for additional studies, namely studies of the environmental and health effects of ethanol to be completed by 31st December 1999, and instructed the state EPA to request a federal waiver of oxygenate requirements<sup>113</sup>. Far from trying to assist the ethanol industry to become the oxygenate of choice, California determined that the newest version of its reformulated gasoline could meet EPA standards without using oxygenates in substantial parts of the market and applied to the EPA for a waiver of the Clean Air Act's oxygenate requirement. This application, which was still being pursued by California at the closing of the main hearing in this case<sup>114</sup>, is inconsistent with the hypothesis that the California Executive Order and its implementing regulations were designed to injure MTBE and methanol producers in order to transfer the market to the ethanol industry or to encourage the development of an ethanol industry in California.
56. As against this clear public record, Methanex invites the Tribunal to accept a conspiratorial thesis, based on the character of certain of ADM's other principal officers; the supposedly "secret" dinner which ADM, as a company with other non-ethanol related operations in California, hosted for Mr Davis; and a statement purportedly made by Senator Burton, which is, on its own terms, inconclusive and, in any event, is supported only by unreliable double hearsay.
57. Methanex acknowledges that none of its submissions is conclusive and that its own conclusions are perforce inferential. It urges the Tribunal to resort to inference. Inference is an appropriate mode of decision in circumstances in which firmer evidence is not available. In the present case, where the timeline of the California legislation, scientific study, public hearings, the Executive Order, and initiatives to secure an oxygenate waiver are all objectively confirmed, the argument for resorting to inference as a way of reaching a conclusion con-

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<sup>113</sup> 1999 Cal. Executive Order D-5-99 paras. 2, 10.

<sup>114</sup> E.g., *Davis v. U.S. EPA*, 336 F.3d 965 (2003) (16 JS tab 41).

sistent with none of the objective evidence - and, indeed, necessarily characterising the behaviour on the part of key actors as criminal - is simply untenable. The Tribunal is not averse to trying to "connect the dots" as a way of testing Methanex's hypothesis, but the dots Methanex has provided and which it affects to find so vivid, have all but faded into chiaroscuro in the course of this adversarial procedure.

58. In particular, Methanex has not made good any of its suspicions about the meeting over dinner on 4th August 1998, an event which looms so centrally in its thesis. The witnesses who attended the dinner hosted by ADM for Mr Davis all persuasively testified that no "secret deal" was cut there to replace MTBE with ethanol as the oxygenate in California reformulated gasoline, in return for campaign donations.
59. Hence the Tribunal is unable to accept the inferences, contrary to the record, which Methanex has pressed of a deal or understanding supposedly reached at this dinner. This conclusion undermines Methanex's contention that the political contributions which were made after the dinner were payments for what Methanex contends had there been agreed. Moreover, the subsequent behaviour of the California Government as a whole, including Governor Davis, is utterly inconsistent with Methanex's hypothesis.
60. In summary, the Tribunal's finds that (i) the Governor of California, Mr Gray Davis, according to the terms of the 1997 California Senate Bill 521 and exercising his statutorily limited discretion thereunder (which Methanex does not impugn as a US measure), made California Executive Order D-5-99 without any intent to harm methanol or Methanex and without any intent to favour ethanol or ADM, contrary to Methanex's allegations; and (ii) there is no credible evidence that Mr Davis as the Governor of California or California intended thereafter to favour the United States ethanol industry (or particular companies within it, including ADM) or to harm US or foreign methanol producers (including Methanex), contrary to Methanex's allegations.

## **PART IV - CHAPTER A**

### **INTRODUCTION**

1. As pleaded in its Second Amended Statement of Claim, Methanex claims that the California ban of MTBE as a gasoline additive breached

the USA's obligations under NAFTA Articles 1102, 1105 and 1110<sup>1</sup> which the USA owed to a Canadian investor, and that Methanex and its investments (including Methanex-US and Methanex-Fortier) have incurred loss or damage by reason of, or arising out of, that breach. As previously indicated, the relevant US measures which allegedly effected one or more of these breaches causing loss to Methanex and Methanex's investments are (i) the California Executive Order D-5-99 and (ii) the CaRFG3 California Regulations.

2. Methanex's alleged damages are to "a substantial portion of their customer base, goodwill, and market for methanol in California"<sup>2</sup>. Methanex alleged that the US measures have also "contributed to the continued idling" of Methanex-Fortier's plant in the USA; further, the measures have "reduced the return to Methanex, Methanex-US and Methanex-Fortier on capital investments made in developing and serving the US MTBE market, increased their cost of capital, and reduced the value of their investments"<sup>3</sup>. Methanex also claims that the US measures have and will continue to cause "substantial downward pressure on the global methanol price"<sup>4</sup> and claims for damages for that loss<sup>5</sup>. It also claims damages incurred in other US states and foreign countries to the extent that bans there can be traced to the US measures<sup>6</sup>. In sum, Methanex claims damages of approximately US\$ 970 million, together with the costs of the arbitration, attorneys' and experts' fees, Canadian Goods and Services tax payable on the above amounts and applicable interest<sup>7</sup>. This is, in short, a claim for US \$1 billion or more.
3. As previously indicated, the USA's response is advanced both on jurisdictional grounds and on the merits, as to both fact and law. As also indicated above, the Tribunal decided in the Partial Award and its order of 2nd June 2003 following the procedural meeting in March 2003, that it was not possible to decide the USA's extant jurisdictional objections without also hearing the factual evidence relating to Methanex's Claim (excepting quantum). Accordingly, in this Award, the Tribunal addresses the Disputing Parties' respective cases on

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<sup>1</sup> For ease of reference, these and other provisions of NAFTA Chapter 11 are set out in full in Annex 4 to this Chapter.

<sup>2</sup> Second Am. Claim, para. 322.

<sup>3</sup> *Ibid.*

<sup>4</sup> *Id.*, para. 323.

<sup>5</sup> *Ibid.*

<sup>6</sup> See *id.*, para. 324.

<sup>7</sup> *Id.*, para. 327.

jurisdiction and the merits in the conjoined procedure provided in Article 21(4) of the UNCITRAL Rules.

4. Although many of the relevant factual issues and much of the legal materials overlap to a material extent, it is nonetheless convenient to consider in turn Methanex's case separately under NAFTA Articles 1101, 1102, 1105 and 1110 in light of the factual decisions already made by the Tribunal in this Award. It is also appropriate to start with the substantive cases advanced by Methanex under Articles 1102, 1105 and 1110 before concluding with Article 1101, where the principal jurisdictional issues are raised by the Disputing Parties' respective cases, for the other provisions may have jurisdictional implications, as explained in Part IV B, paragraphs 1 and 2 below. As regards other issues relating to the merits of Methanex's Claim, including NAFTA Articles 1116 and 1117, the Tribunal need not address them in detail in this Award for reasons explained further below.

## **ANNEX 4 TO PART IV - CHAPTER A RELEVANT NAFTA ARTICLES**

### **Article 1101**

*Article 1101: Scope and Coverage*

1. *This Chapter applies to measures adopted or maintained by a Party relating to:*

- (a) investors of another Party;*
- (b) investments of investors of another Party in the territory of the Party; and*
- (c) with respect to Articles 1106 and 1114, all investments in the territory of the Party.*

### **Article 1102**

*Article 1102: National Treatment*

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.*

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

3. The treatment accorded by a Party under paragraphs 1 and 2 means, with respect to a state or province, treatment no less favorable than the most favorable treatment accorded, in like circumstances, by that state or province to investors, and to investments of investors, of the Party of which it forms a part.

### **Article 1105**

#### *Article 1105: Minimum Standard of Treatment*

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. ...

### **Article 1110**

#### *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 non-discriminatory 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.

### **Article 1116**

#### *Article 1116: Claim by an Investor of a Party on Its Own Behalf*

1. An investor of a Party may submit to arbitration under this Section a claim that another Party has breached an obligation under:

(a) Section A ...

and that the investor has incurred loss or damage by reason of, or arising

*out of, that breach.*

*2. An investor may not make a claim if more than three years have elapsed from the date on which the investor first acquired, or should have first acquired, knowledge of the alleged breach and knowledge that the investor has incurred loss or damage.*

### **Article 1117**

*Article 1117: Claim by an Investor of a Party on Behalf of an Enterprise*

*1. An investor of a Party, on behalf of an enterprise of another Party that is a juridical person that the investor owns or controls directly or indirectly, may submit to arbitration under this Section a claim that the other Party has breached an obligation under:*

(a) Section A...

*and that the enterprise has incurred loss or damage by reason of, or arising out of, that breach.*

*2. An investor may not make a claim on behalf of an enterprise described in paragraph 1 if more than three years have elapsed from the date on which the investor first acquired, or should have first acquired, knowledge of the alleged breach and knowledge that the enterprise has incurred loss or damage.*

## **PART IV - CHAPTER B**

### **ARTICLE 1102 NAFTA**

#### **1) Introduction**

1. An affirmative finding of the requisite "relation" under NAFTA Article 1101, as decided in the Partial Award for the purposes of this case, does not necessarily establish that there has been a corresponding violation of NAFTA Article 1102 by the USA. But an affirmative finding under NAFTA Article 1102, which does not require the demonstration of the malign intent alleged by Methanex, could conceivably provide evidence relevant to a determination as to whether the "relation" required by NAFTA Article 1101 exists in this case. The potentially asymmetrical connection between these two Chapter 11 provisions

was one of the reasons the Tribunal felt it appropriate to conjoin the jurisdictional and merits phases in the main hearing under Article 21(4) of the UNCITRAL Rules. of Article 1102.

2. Hence, although Methanex's principal arguments directly addressing Article 1101 may fail, Methanex's jurisdictional case may nonetheless derive support from its arguments under Article 1102. For this reason, the Tribunal thinks it appropriate to inquire into Methanex's claims with respect to Article 1102, before turning to its case under Article 1101. Insofar as these claims can be sustained, they might repair the deficiency with respect to the necessary showing of the "relation" under Article 1101. This inquiry, by its nature, requires a consideration of some of the same material which the Tribunal has examined elsewhere, but this examination is to be conducted here through the prism of Article 1102.

## **2) Methanex's Case on Breach of Article 1102 NAFTA**

3. Methanex did not originally bring any claim for breach of Article 1102 NAFTA. It was only in the draft Amended Statement of Claim of 12 February 2001 that Methanex sought to introduce a claim based on discrimination against foreign producers of methanol including Methanex<sup>1</sup>. The claim in respect of Article 1102 nonetheless became the prime focus of Methanex's submissions on breach of NAFTA Chapter 11. Methanex makes its submissions in respect of Article 1102 under three broad headings:
4. **(i) Like circumstances:** The starting point for Methanex's analysis of Article 1102 is the proposition that Article 1102 does not require that investments be identical, merely that the two investors or investments be in "like circumstances". On this basis, it is irrelevant that Methanex is in identical circumstances with other US methanol producers and that it is not in identical circumstances with US ethanol producers. The sole question is whether Methanex is, as it claims, in like circumstances with US ethanol producers. Relying on the expert legal opinion of the late Sir Robert Jennings, Methanex submits that GATT/WTO decisions provide particularly relevant and useful precedents in determining the scope of "likeness" under Article 1102<sup>2</sup>.

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<sup>1</sup> Draft Amended Statement of Claim at Sections I.A-I.B.

<sup>2</sup> Second Am. Claim, para. 300 (citing Expert Op. of Robert Jennings, 4th November 2002, at p. 10 (Second Am. Claim, Exhibit C).

5. Further, relying on the expert legal opinion of Dr Claus-Dieter Ehlermann<sup>3</sup>, as well as the *Asbestos*<sup>4</sup> and *S.D. Myers*<sup>5</sup> cases, Methanex maintains that "the most accurate and widely recognised test of 'likeness' is competition"<sup>6</sup>. It contends that "if two or more investors or their investments compete for the same business, they are in 'like circumstances'" for the purposes of Article 1102<sup>7</sup>.
6. Applying Article 1102 to the facts, Methanex claims that Methanex and other methanol producers are in like circumstances with US domestic ethanol producers because they both produce oxygenates used in manufacturing reformulated gasoline and because they compete for customers in the oxygenate market<sup>8</sup>. In this respect, Methanex relied on a list prepared by the US EPA identifying methanol and ethanol as oxygenates<sup>9</sup>. It maintains that the fact that methanol and ethanol are used in slightly different ways does not affect the existence of a competitive relationship: its central case is that integrated oil refineries buy either methanol or ethanol, i.e. prior to the California ban of MTBE, Methanex sold methanol to integrated oil refineries in California for the purposes of manufacturing MTBE, whereas since the ban those refineries have shifted to using ethanol<sup>10</sup>. It claims that every ethanol sale took away a sale of methanol and, in this respect, Methanex relies on an unsigned contract that it concluded with Valero Refining and Marketing Company giving Valero the right to cease purchases of methanol where demand for MTBE was reduced pursuant to the MTBE ban<sup>11</sup>. So far as concerns gasoline blenders, Methanex claims that there is direct competition in that gasoline blenders previously bought MTBE from MTBE producers, and that every purchase of ethanol by a gasoline blender displaced a sale of methanol to an

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<sup>3</sup> Expert Op. of Claus-Dieter Ehlermann, 4th November 2002 (Second Am. Claim Exhibit D).

<sup>4</sup> *European Communities-Measures Affecting Asbestos and Asbestos-Containing Products* (Eur. Comm. v. Can.), WT/DS135/AB/R (hereinafter *Asbestos*), (2001) 40 ILM 1408 (Second Am. Claim App., 3 LA tab 79).

<sup>5</sup> *S. D. Myers v. Canada*, Partial Award, (2001) 40 ILM 1193 (Second Am. Claim App., 4 LA tab 97).

<sup>6</sup> Second Am. Claim, para. 301.

<sup>7</sup> *Id.*, para. 303.

<sup>8</sup> *E.g.*, Second Am. Claim at Section V.B.

<sup>9</sup> Reply, para. 27 (citing U.S. Evtl. Protection Agency, Oxygenate Identification (22 JS tab 20)); Second Am. Claim, para. 70.

<sup>10</sup> *E.g.*, Second Am. Claim, paras. 78-80; Reply, para. 236.

<sup>11</sup> Second Am. Claim, para. 80; Reply, para. 23; see also Contract Between Methanex Methanol Company and Valero Refining and Marketing Company (Second Am. Claim, Exhibit A tab 1).

MTBE producer. Thus it claims that consumers have a binary choice between purchasing methanol and purchasing ethanol<sup>12</sup>.

7. Further, applying the highly similar GATT/WTO "like products" test also leads to the conclusion that ethanol and methanol are "like". Referring to the test set out in Dr Ehlermann's legal opinion, Methanex emphasises that methanol and ethanol are capable of serving the same or similar end uses, and that consumers have perceived and treated methanol and ethanol as alternatives. Methanex claims that there is no doubt that it and its investments have not received the same treatment in California as ethanol - it claims that California has banned MTBE and methanol from the oxygenate market and effectively given ethanol a monopoly, and that such discrimination was not justified by spurious environmental concerns.
8. **(ii) Most favourable treatment:** Methanex claims that, pursuant to Article 1102(3), it is entitled to "treatment no less favorable than the most favorable treatment accorded, in like circumstances" to domestic investors and their investments, as appears from the face of Article 1102(3) and as is consistent with the interpretation adopted in the *Pope & Talbot* case<sup>13</sup>. Methanex argues that the fact that the US measures may have discriminated against some domestic US methanol producers and their investments is irrelevant and does not excuse an Article 1102 violation<sup>14</sup>. Methanex cites, in support of its interpretation, various decisions of the WTO, the European Commission and the US Supreme Court<sup>15</sup>.
9. **(iii) Burden of proof:** Methanex contends that once it is established that there was less favourable treatment, the burden shifts to the USA to justify such treatment on the basis that the MTBE ban is a valid environmental measure. Methanex maintains that there is no provision in Chapter 11 explicitly permitting environmental exceptions to the national treatment obligation, and refers to NAFTA Article 2101 which specifically incorporates Article XX GATT<sup>16</sup>. It claims that GATT and WTO case law place the burden on the US regarding the validity of an environmental measure that denies national treatment. In this respect, Methanex relies in particular on *United States-Standards for*

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<sup>12</sup> E.g., Second Am. Claim at Section V.B.

<sup>13</sup> *Pope & Talbot, Inc. v. Canada*, Final Award, paras. 39-42 (NAFTA 2001) (Second Am. Claim, App., 4 LA tab 92).

<sup>14</sup> Second Am. Claim, paras. 308-312.

<sup>15</sup> *Ibid.*

<sup>16</sup> Reply, para. 188.

*Reformulated and Conventional Gasoline*<sup>17</sup> and also the NAFTA Chapter 20 case, *Cross-Border Trucking*<sup>18</sup>. So far as concerns discharging this burden, Methanex claims that the USA must satisfy four criteria: it must show that the measures adopted (i) are necessary to fulfill the environmental objective, i.e. necessary to protect the environment of California, (ii) are proportionate, (iii) are the least restrictive of foreign investment, and (iv) do not constitute a disguised restriction on foreign investments. On the facts presented, it claims that none of these criteria are satisfied<sup>19</sup>.

10. Methanex also claims that the USA's protection of its domestic ethanol industry violates numerous provisions of the GATT, as well as various trade provisions of NAFTA.

### **3) The Tribunal's Decision Regarding Article 1102 NAFTA**

11. Article 1102(3) NAFTA provides as follows:

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

Methanex contends that this paragraph governs its claim in the present case<sup>20</sup>.

12. In order to sustain its claim under Article 1102(3), Methanex must demonstrate, cumulatively, that California intended to favour domestic investors by discriminating against foreign investors and that Methanex and the domestic investor supposedly being favored by California are in like circumstances. It is Methanex's contention that California, in deciding to ban MTBE, intended to favour domestic ethanol producers, of which class ADM is a member, and to harm producers of methanol<sup>21</sup>. Additionally, it is Methanex's position that

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<sup>17</sup> *United States-Standards for Reformulated and Conventional Gasoline*, (US v. Braz.), WT/DSZ/AB/R (WTO 1996) (Reply App. LA tab 15).

<sup>18</sup> *In re Cross-Border Trucking Services*, Final Report (NAFTA 2001) (discussed at Transcript Day 1, pp. 14, 38-39 (Mr Dugan for Methanex) and on record during the jurisdictional phase).

<sup>19</sup> E.g., Reply, paras. 191-197.

<sup>20</sup> E.g., Second Am. Claim, para. 294.

<sup>21</sup> E.g., id., para. 298.

ethanol and methanol are in like circumstances<sup>22</sup>. The USA opposed both of these contentions on legal and factual grounds<sup>23</sup>.

13. *Methodologies*: The Disputing Parties proposed different methodologies for applying Article 1102 NAFTA. According to Methanex: "Article 1102 requires a three-step analysis. First, the Tribunal must determine whether the U.S. ethanol industry is "in like circumstances" with Methanex and its investments. Second, if they are in like circumstances, the Tribunal must determine whether any portion of the domestic ethanol industry received better treatment than Methanex and its investments did. Third, if the Tribunal finds that Methanex is not accorded the most favorable treatment, then the burden shifts to the U.S. to justify the disparate treatment accorded to methanol producers by showing that the measures should be permitted because they implement valid environmental goals"<sup>24</sup>.
14. The USA proposed a different methodology: "[T]he function of the national treatment provision is to address discrimination on the basis of nationality of ownership of an investment. The function of addressing nationality-based discrimination is served by comparing the treatment of the foreign investor to the treatment accorded to a domestic investor that is most similarly situated to it. In ideal circumstances, the foreign investor or foreign-owned investment should be compared to a domestic investor or domestically-owned investment that is like it in all relevant respects, but for nationality of ownership. When nationality is the only variable, such a comparison serves the Article's purpose of ascertaining whether the treatment accorded differed on the basis of nationality"<sup>25</sup>.
15. "In like circumstances", according to the USA, does not import identity between comparator and compared: "[I]n like circumstances' allows for a certain degree of flexibility in the national treatment analysis, such as where there is no identical domestically-owned counterpart to the foreign-owned investment. In such a case, a tribunal may look farther afield and expand the scope of domestically-owned comparators as long as they are similar enough to justify considering their circumstances to be "like" that of the foreign investor or investment"<sup>26</sup>. In its Fourth Article 1128 submission, the Government of

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<sup>22</sup> E.g., *Ibid.*

<sup>23</sup> E.g., Am. Defense at Section III.B.

<sup>24</sup> Reply, para. 168.

<sup>25</sup> Rejoinder, para. 152.

<sup>26</sup> *Id.*, para. 154.

Canada proposed a formula similar to that of the USA<sup>27</sup>.

16. The major distinction between the two proposed methodologies is in the specific method of selecting what the USA called the "comparator" for purposes of determining like circumstances. In the formula quoted above, Methanex's methodology begins by assuming that its comparator is the ethanol industry, while the USA proposes a procedure in which the comparator that is to be selected is that domestic investor or domestically-owned investment which is like or, if not like, then close to the foreign investor or investment in all relevant respects, but for nationality of ownership. Despite the difference in approach, it is clear that if the result of the application of the US procedure were to identify the ethanol industry as the comparator, Methanex's methodology would simply be the final sequence in the US methodology.
17. The key question is: who is the proper comparator? Simply to assume that the ethanol industry or a particular ethanol producer is the comparator here would beg that question. Given the object of Article 1102 and the flexibility which the provision provides in its adoption of "like circumstances", it would be as perverse to ignore identical comparators if they were available and to use comparators that were less "like", as it would be perverse to refuse to find and to apply less "like" comparators when no identical comparators existed. The difficulty which Methanex encounters in this regard is that there are comparators which are *identical* to it.
18. The USA contended at the main hearing in June 2004: "It is not contested that there is a substantial methanol industry in the United States and that US investors own methanol marketing and production units just like Methanex"<sup>28</sup>. In point of fact, 47% of methanol producers in the United States are domestic<sup>29</sup>. The California ban had precisely the same effect on the American investors and investments as it had on the Canadian investor, Methanex.
19. In this respect, the NAFTA award in *Pope & Talbot v. Canada* is instructive. There, a US investor in Canada, which was obliged to pay export fees, alleged that it was in like circumstances with Canadian producers in other provinces that were not subject to export fees.

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<sup>27</sup> See Canada's Fourth Article 1128 Submission, para. 11.

<sup>28</sup> Transcript Day 2, at p. 265.

<sup>29</sup> First Expert Report of Mr Burke, para. 66.

The tribunal, however, rejected the claim for there were more than 500 Canadian producers in other provinces which were subject to the fees.<sup>30</sup> That is, the tribunal selected the entities that were in the most "like circumstances" and not comparators that were in less "like circumstances". It would be a forced application of Article 1102 if a tribunal were to ignore the identical comparator and to try to lever in an, at best, approximate (and arguably inappropriate) comparator. The fact stands - Methanex did not receive less favourable treatment than the identical domestic comparators, producing methanol.

20. To address this obstacle to its case, Methanex proposes a number of theories. To begin, Methanex invokes Article 1102(3) and emphasises the word "most":

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

Methanex reads this provision to mean that "Methanex and other Canadian or Mexican investors and investments are entitled to the best, not the worst, treatment accorded to like domestic investors and their investments"<sup>31</sup>.

21. In the Tribunal's view, this is an entirely plausible reading of the provision: if a component state or province differentiates, as a matter of domestic law or policy, between members of a domestic class, which class happens to serve as the comparator for an Article 1102 claim, the investor or investment of another party is entitled to the most favourable treatment accorded to some members of the domestic class. The Tribunal need not enter into Methanex's citation of WTO cases, however, because Article 1102(3) simply does not resolve Methanex's difficulty. The California ban does not differentiate between foreign investors or investments and various MTBE producers in California or, if it is relevant, methanol feedstock producers in the United States. There is no more or less favourable treatment here. The treatment is uniform, for the ban applies to all MTBE manufacturers. Article 1102(3) is not relevant to this case.

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<sup>30</sup> *Pope & Talbot, Inc.*, paras. 87-88.

<sup>31</sup> Second Am. Claim, para. 308.

22. Thus, even assuming that Methanex, as a methanol producer, is deemed to be affected, as a legal and factual matter, under NAFTA and international law, by California's ban of MTBE, Methanex's claim under Article 1102 would fail because it did not receive treatment less favourable than United States investors in like circumstances.
23. Nonetheless, the Tribunal will consider in further detail the arguments proffered by the Disputing Parties regarding the "like circumstances" of methanol and ethanol. Methanex argues that its investments are in "like circumstances" with the domestic US ethanol industry by reference to GATT jurisprudence<sup>32</sup>. As described above, Methanex's position is that: "Methanol and ethanol are both oxygenates under U.S. law. Methanex and other methanol producers are in 'like circumstances' with US domestic ethanol producers because they both produce the same product-oxygenates used in manufacturing reformulated gasoline-and because they both compete directly for customers in the oxygenate market"<sup>33</sup>.
24. The USA, on the other hand, notes that methanol and ethanol differ chemically, and contends that the products have different end uses<sup>34</sup>. Only ethanol is an oxygenate additive to gasoline while methanol is not a gasoline oxygenate and, moreover, is prohibited from being used as such under United States federal law<sup>35</sup>; it is a feedstock for the production of MTBE which is then used as an oxygenate for gasoline<sup>36</sup>. The USA also notes that the two products do not share the same tariff classification under the Harmonized System of Tariffs<sup>37</sup>. In addition, the USA argues that the consumer taste test is not relevant, because the products are not in competition<sup>38</sup>.

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<sup>32</sup> E.g., Second Am. Claim, paras. 298-301 (citing Expert Op. of Robert Jennings, 4th November 2002, at p. 10 for its discussion of the applicability of GATT jurisprudence and citing Expert Op. of Claus-Dieter Ehlermann, 4th November 2002, para. 24 for its explanation that GATT jurisprudence identifies "like products" on the basis of "competitive relationships between and among products"); see generally *id.* At Section V.B (arguing that methanol and ethanol are essentially interchangeable and present consumers with a "binary choice").

<sup>33</sup> *Id.*, para. 304.

<sup>34</sup> Am. Defense, paras. 138-140 (asserting that methanol and ethanol are not essentially interchangeable and disagreeing with Methanex's contention that the products directly compete).

<sup>35</sup> E.g., *id.*, paras. 142, 147-148 (discussing why methanol is not and cannot be used as an oxygenate in gasoline).

<sup>36</sup> E.g., *id.*, para. 318.

<sup>37</sup> *Id.*, para. 323.

<sup>38</sup> *Id.*, para. 322.

25. Moreover, the USA questions the applicability of GATT to the construction of Chapter 11 of NAFTA<sup>39</sup>. The USA avers that the drafters of NAFTA used "like products" when they intended to do so and that the resort to the words "like circumstances" in Article 1102 indicates an intention to differentiate between the two terms, just as the objects and purposes of GATT differ from those of Chapter 11 of NAFTA<sup>40</sup>. In any case, the USA argues, even under GATT law, a rigorous application of the four-part test in the decision of the Appellate Body in the *Asbestos* case<sup>41</sup> would establish that ethanol and methanol are not "like products" in terms of physical properties, end uses, consumer tastes and habits and tariff classifications<sup>42</sup>. Using the four-part test with respect to ethanol and MTBE, the USA submitted that the differences were even starker.<sup>43</sup> In particular, the USA emphasised that *Asbestos* had found that the health hazard posed by a product is a pertinent factor in the examination of "likeness"<sup>44</sup>, and, in this regard, the USA adduced evidence of the hazards of MTBE.
26. In its Reply, Methanex accuses the USA of insisting that "like" be "identical"<sup>45</sup>. (The Tribunal would note that this was not the USA's argument.) Methanex argues:

*"The relevant economic sector here is the production and sale of oxygenates used in the manufacture of RFG and oxygenated gasoline. Both ethanol and methanol are oxygenates, and both are used in the manufacture of RFG and oxygenated gasoline. The fact that each oxygenate is used in slightly different ways in the gasoline manufacturing process is irrelevant . . ."*<sup>46</sup>.

On the facts, Methanex argues that there was no valid environmental, health or safety justification for the MTBE ban<sup>47</sup>, the burden of proof was on the USA<sup>48</sup> and exceptions to national treatment are to be construed narrowly, as "local interests often try to use pseudo-

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<sup>39</sup> *Id.*, paras. 11, 282.

<sup>40</sup> *Id.*, paras. 302-304.

<sup>41</sup> *Asbestos*, para. 101.

<sup>42</sup> Am. Defense, paras. 309-325.

<sup>43</sup> *Id.*, paras. 326-342.

<sup>44</sup> Am. Defense, para. 331 (citing *Asbestos*, para. 92).

<sup>45</sup> Reply, para. 173.

<sup>46</sup> *Id.*, para. 177.

<sup>47</sup> *Id.*, para. 187.

<sup>48</sup> *Id.*, paras. 188-190.

environmental measures to disguise the more favourable treatment they seek vis-à-vis foreign competitors"<sup>49</sup>.

27. In its Rejoinder, the USA argues that Methanex had received national treatment, the GATT provisions were irrelevant and Methanex had not proved that it had received less favourable treatment. The International Institute for Sustainable Development (IISD), in its carefully reasoned Amicus submission, also disagrees with Methanex's contention that "trade law approaches can simply be transferred to investment law"<sup>50</sup>.
28. The incontrovertible fact is that Methanex produced methanol as a feedstock for MTBE and not as a gasoline additive in its own right. Aside from the federal prohibition of the use of methanol as an oxygenate, methanol has been tried as a fuel in only limited experiments, but would require, if it were to be used, significant and expensive retro-adjustments in gasoline engines. As a result, the ethanol and methanol products cannot be said to be in competition, even assuming that this trade law criterion were to apply. Insofar as there is a binary choice, it is between MTBE and other lawful and practicable oxygenates. Methanex's alternative theory of like products fails on the facts.
29. In conclusion, the Tribunal decides that Methanex's claim under Article 1102 fails for a number of reasons, any one of which would suffice to reject its claim. At the very threshold, Methanex encounters the issue of whether the California ban meted out treatment that it accords in like circumstances to domestic investors. As the Tribunal has observed above and in its Partial Award, NAFTA, as a treaty, is to be interpreted in accordance with Articles 31 and 32 of the Vienna Convention on the Law of Treaties, which codifies the customary international rules of treaty interpretation. Hence, the Tribunal begins with an inquiry into the plain and natural meaning of the text of Article 1102. Paragraphs 1, 2, and 3 of Article 1102 enjoin each Party to accord to investors or investments of another Party "treatment no less favorable than that it accords, in like circumstances, to its investors [or investments] . . . ". These provisions do not use the term of art in international trade law, "like products", which appears in and plays a critical role in the application of GATT Article III. Indeed, the term "like products" appears nowhere in NAFTA Chapter 11.

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<sup>49</sup> Id., paras. 191-192.

<sup>50</sup> Brief of Amicus Curiae, International Institute for Sustainable Development, para. 34 (9th March 2004).

30. The drafting parties of NAFTA were fluent in GATT law and incorporated, in very precise ways, the term "like goods" and the GATT provisions relating to it when they wished to do so. In NAFTA Chapter 3 dealing with "National Treatment and Market Access for Goods", Article 301(1) provides:

*"Each Party shall accord national treatment to the goods of another Party in accordance with Article III of the General Agreement on Tariffs and Trade (GATT), including its interpretative notes, and to this end Article III of the GATT and its interpretative notes, or any equivalent provision of a successor agreement to which all Parties are party, are incorporated into and made part of this Agreement."*

Article 301(2) provides:

*"The provisions of paragraph 1 regarding national treatment shall mean, with respect to a state or province, treatment no less favorable than the most favorable treatment accorded by such state or province to any like, directly competitive or substitutable goods, as the case may be, of the Party of which it forms a part."*

According to NAFTA Article 300, Chapter 3 of NAFTA, including its definitions, applies (unless provided otherwise, an exception that is important in this discussion) only to Part Two of NAFTA, that is Chapter 3 to Chapter 8. With respect to trade in goods in Part Two, the obligation of "no less favorable" treatment applies to "any like, directly competitive or substitutable goods, as the case may be". These rather precise criteria allow the importing or receiving state relatively little discretionary scope with respect to the goods entitled to national treatment.

31. In Chapter 7, "Agriculture and Sanitary and Phytosanitary Measures", Article 712(4) provides:

*"Each Party shall ensure that a sanitary or phytosanitary measure that it adopts, maintains or applies does not arbitrarily or unjustifiably discriminate between its goods and like goods of another Party, or between goods of another Party and like goods of any other country, where identical or similar conditions prevail."*

Article 712(4) speaks only of "like goods" and not "any like, directly competitive or substitutable goods, as the case may be" as in Article 301. It is clear that "like goods" is not short-hand for "any like, directly competitive or substitutable goods, as the case may be", because Article 710 states that Article 301 does not apply to any sanitary or phytosanitary measure<sup>51</sup>.

32. In Chapter 9, entitled "Standards-Related Measures", which is the first chapter in Part III, entitled "Technical Barriers to Trade", Article 904 provides:

*Right to Take Standards-Related Measures*

1. *Each Party may, in accordance with this Agreement, adopt, maintain or apply any standards-related measure, including any such measure relating to safety, the protection of human, animal or plant life or health, the environment or consumers, and any measure to ensure its enforcement or implementation. Such measures include those to prohibit the importation of a good of another Party or the provision of a service by a service provider of another Party that fails to comply with the applicable requirements of those measures or to complete the Party's approval procedures.*

*Right to Establish Level of Protection*

2. *Notwithstanding any other provision of this Chapter, each Party may, in pursuing its legitimate objectives of safety or the protection of human, animal or plant life or health, the environment or consumers, establish the levels of protection that it considers appropriate in accordance with Article 907(2).*

*Non-Discriminatory Treatment*

3. *Each Party shall, in respect of its standards-related measures, accord to goods and service providers of another Party:*

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<sup>51</sup> Articles 301 (National Treatment) and 309 (Import and Export Restrictions), and the provisions of Article XX(b) of the GATT as incorporated into Article 2101(1) (General Exceptions), do not apply to any sanitary or phytosanitary measure.

- (a) *national treatment in accordance with Article 301 (Market Access) or Article 1202 (Cross-Border Trade in Services); and*
- (b) *treatment no less favorable than that it accords to like goods, or in like circumstances to service providers, of any other country.*

#### *Unnecessary Obstacles*

*4. No Party may prepare, adopt, maintain or apply any standards-related measure with a view to or with the effect of creating an unnecessary obstacle to trade between the Parties. An unnecessary obstacle to trade shall not be deemed to be created where:*

- (a) the demonstrable purpose of the measure is to achieve a legitimate objective; and*
- (b) the measure does not operate to exclude goods of another Party that meet that legitimate objective."*

It is noted that Article 904(3)(a) grants to goods and service providers the national treatment standard of Article 301. Article 904(3) uses "like goods" for goods and "like circumstances" for service providers.

33. It is thus apparent from the text that the drafters of NAFTA were careful and precise about the inclusion and the location of the respective terms, "like goods", "any like, directly competitive or substitutable goods, as the case may be", and "like circumstances". "Like goods" is never used with respect to the investment regime of Chapter 11 and "like circumstances", which is all that is used in Article 1102 for investment, is used with respect to standards-related measures that might constitute technical barriers to trade only in relation to services; nowhere in NAFTA is it used in relation to goods.
34. It may also be assumed that if the drafters of NAFTA had wanted to incorporate trade criteria in its investment chapter by engrafting a GATT-type formula, they could have produced a version of Article 1102 stating "Each Party shall accord to investors [or investments] of another Party treatment no less favorable than it accords its own investors, in like circumstances with respect to any like, directly competitive or substitutable goods". It is clear from this constructive exercise how incongruous, indeed odd, would be the juxtaposition in a single provision dealing with investment of "like circumstances"

and "any like, directly competitive or substitutable goods".

35. In any event, the drafters did not insert the above italicised words in Article 1102; and it would be unwarranted for a tribunal interpreting the provision to act as if they had, unless there were clear indications elsewhere in the text that, at best, the drafters wished to do so or, at least, that they were not opposed to doing so. In fact, the intent of the drafters to create distinct regimes for trade and investment is explicit in Article 1139's definition of investment.
36. Article 1139, in paragraphs (a) to (h)<sup>52</sup>, specifies what are investments for the purposes of Chapter 11 and, perforce, jurisdiction under it; in paragraphs (i) and (j) it specifies what are not investments:

*"but investment does not mean,*

*(i) claims to money that arise solely from*

*(i) commercial contracts for the sale of goods or services by a national or enterprise in the territory of a Party to an enterprise in the territory of another Party, or*

*(ii) the extension of credit in connection with a commercial transaction, such as trade financing, other than a loan covered by subparagraph (d); or*

*(j) any other claims to money, that do not involve the kinds of interests set out in subparagraphs (a) through (h); . . . "*

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<sup>52</sup> These investments are:

*"(a) an enterprise; (b) an equity security of an enterprise; (c) a debt security of an enterprise (i) where the enterprise is an affiliate of the investor, or (ii) where the original maturity of the debt security is at least three years, but does not include a debt security, regardless of original maturity, of a state enterprise; (d) a loan to an enterprise (i) where the enterprise is an affiliate of the investor, or (ii) where the original maturity of the loan is at least three years, but does not include a loan, regardless of original maturity, to a state enterprise; (e) an interest in an enterprise that entitles the owner to share in income or profits of the enterprise; (f) an interest in an enterprise that entitles the owner to share in the assets of that enterprise on dissolution, other than a debt security or a loan excluded from subparagraph (c) or (d); (g) real estate or other property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes; and (h) interests arising from the commitment of capital or other resources in the territory of a Party to economic activity in such territory, such as under (i) contracts involving the presence of an investor's property in the territory of the Party, including turnkey or construction contracts, or concessions, or (ii) contracts where remuneration depends substantially on the production, revenues or profits of an enterprise; ...".*

37. The issue here is not the relevance of general international law, as the late Sir Robert Jennings proposed on behalf of Methanex, or the theoretical possibility of construing a provision of NAFTA by reference to another treaty of the parties, for example the GATT. International law directs this Tribunal, first and foremost, to the text; here, the text and the drafters' intentions, which it manifests, show that trade provisions were not to be transported to investment provisions. Accordingly, the Tribunal holds that Article 1102 is to be read on its own terms and not as if the words "any like, directly competitive or substitutable goods" appeared in it.
38. For all these reasons, the Tribunal decides that Methanex's claim under Article 1102 fails, for, without regard to the question of causation, the California MTBE ban did not differentiate between foreign and domestic MTBE producers; nor, if it is relevant, did it differentiate between foreign and domestic methanol producers. The Tribunal also decides that Methanex's case under Article 1101 is not assisted by its arguments under Article 1102.

## **PART IV - CHAPTER C**

### **ARTICLE 1105 NAFTA**

#### **1) Introduction**

1. As noted in the previous Chapter, at the outset of the Tribunal's discussion of NAFTA Article 1102, an affirmative finding of a malign intent under NAFTA Article 1101 might satisfy the requirements of a showing of the requisite "relation" under NAFTA Article 1105. But a failure to find a malign intent under Article 1101 might yet be repaired by an affirmative finding that an investor had not been accorded treatment in accordance with international law. Hence in fairness to Methanex, the Tribunal, as part of the joinder of jurisdictional questions and the merits, will now turn to the material adduced with respect to the claims under Article 1105 to determine whether a possible finding of a violation under Article 1105 could fulfil the requirements of Article 1101.

#### **2) Methanex's Case Regarding Article 1105 NAFTA**

2. Methanex submits that the US measures were intended to discriminate against foreign investors and their investments and that intentional discrimination is, by definition, inequitable. Thus it is claimed

that the USA's breach of Article 1102 NAFTA establishes a breach of Article 1105 as well.

3. Methanex's pleaded claim under Article 1105 was commendably succinct. It was developed in three paragraphs in the Second Amended Statement of Claim and consisted of a single assertion: "the California measures were intended to discriminate against foreign investors and their investments, and intentional discrimination is, by definition, unfair and inequitable"<sup>1</sup>. Methanex went on to state, "[T]his is a straightforward case of raw economic protectionism. On such facts, the United States' breach of Article 1102 'establishes a breach of Article 1105 as well'"<sup>2</sup>. Methanex's Reply devoted only four paragraphs to its Article 1105 claim - two of which argued against the validity of the FTC's interpretation of Article 1105<sup>3</sup> and two of which restated its contention that "intentional discrimination violates even the minimum standard of treatment required by Article 1105"<sup>4</sup>.
4. Both in its written and oral submissions, Methanex contended that the FTC's interpretation of 31st July 2001 is a purported amendment, as opposed to a valid interpretation, of Article 1105; and it is therefore not binding on this Tribunal under Article 1131(2) NAFTA. In oral argument, Methanex assailed the FTC's interpretation as invalid substantively because Article 1131 requires the Tribunal "to take into account all of international law"<sup>5</sup>; and invalid procedurally because [t]hat's too distinct and too important a deletion from the Treaty to be anything other than an amendment"<sup>6</sup>.
5. Accordingly, Methanex contends that the Tribunal should disregard the interpretation on the basis that it is nothing more than an attempt by the USA retroactively to suppress a legitimate claim. Methanex relies on the legal opinion of the late Sir Robert Jennings in support of its contentions at the jurisdictional phase of this case:

*"It would be wrong to discuss these three-Party 'interpretations' of what have become key words in this arbitration, without protesting the impropriety of the three governments*

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<sup>1</sup> Second Am. Claim, para. 313; see id., para. 314 (referencing the NAFTA award in *S.D. Myers*).

<sup>2</sup> Id., para. 315.

<sup>3</sup> Reply, paras. 203-204; see generally Free Trade Commission Clarifications Related to NAFTA Chapter 11, 31st July 2001.

<sup>4</sup> Id., para. 205; see id., para. 206.

<sup>5</sup> Transcript Day 8, p. 1854 (lines 6-7).

<sup>6</sup> Id. at p. 1855 (lines 16-18).

*making such an intervention well into the process of the arbitration, not only after the benefit of seeing the written pleadings of the parties but also virtually prompted by them<sup>7</sup>."*

Methanex contends that, in any event, the interpretation should have no material impact on the proceedings as it cannot alter the substance of NAFTA's investment protections.

6. In response, the USA argued that the FTC's interpretation is binding on this Tribunal and, by its terms, precludes the contention that a breach of Article 1102 also breaches Article 1105 (or, as the case may be, another article in Chapter Eleven, such as Article 1110)<sup>8</sup>. Even ignoring the FTC's interpretation, the USA argues, nationality-based discrimination was cabined exclusively under Article 1102<sup>9</sup>. Further, according to the USA, Methanex has not demonstrated the existence of a rule of customary international law that prohibits a state from differentiating between nationals and aliens<sup>10</sup>.
7. At the main hearing in June 2004, Methanex placed considerable weight on the description of the general standard emerging for Article 1105(1) set out in the award in the *Waste Management v. Mexico* arbitration:

*"98. The search here is for the Article 1105 standard of review, and it is not necessary to consider the specific results reached in the cases discussed above. But as this survey shows, despite certain differences of emphasis a general standard for Article 1105 is emerging. Taken together, the S.D. Myers, Mondev, ADF and Loewen cases suggest that the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety-as might be the*

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<sup>7</sup> Expert Op. of Robert Jennings, 6th September 2001 (Methanex's Submission in Response to the NAFTA Free Trade Commission Interpretation, 18th September 2001, Exh. 1).

<sup>8</sup> Am. Defense at Part IV A.

<sup>9</sup> See *id.*, para. 365.

<sup>10</sup> See, e.g., *id.*, paras. 366-370.

*case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.*

*99. Evidently the standard is to some extent a flexible one which must be adapted to the circumstances of each case<sup>11</sup>.*

8. According to Methanex, California's actions in banning MTBE and methanol and precipitously introducing ethanol were arbitrary, grossly unfair, unjust and idiosyncratic in the sense that there was a pandering to a domestic US industry, i.e. the domestic ethanol industry. These actions were discriminatory because they discriminated against foreign-owned investments such as the investments of Methanex. In addition, Methanex argues that there was a complete lack of transparency because the critical event was not the public hearings held in California, but rather the meeting between Mr Davis and ADM in Decatur, Illinois. Methanex claims that the promotion of ethanol in California was driven by the political debt that Governor Davis felt he owed to ADM in return for its political contributions, which was not in any way apparent in the administrative process<sup>12</sup>. Methanex submits that, whenever a political official implicitly favours one competitor in return for political contributions and shuts another competitor out of the market, that action is arbitrary, grossly unfair, unjust, and idiosyncratic as the decision is not made on the merits<sup>13</sup>.

### **3) The Tribunal's Decision Regarding Article 1105 NAFTA**

9. Article 1105 NAFTA provides:

*"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.*

*2. Without prejudice to paragraph 1 and notwithstanding Article 1108(7)(b), each Party shall accord to investors of another Party, and to investments of investors of another*

<sup>11</sup> *Waste Mgmt. Inc. v. Mexico*, Arb (AF)/00/3, paras. 98-99 (ICSID 2004); e.g., Transcript Day 8, pp. 1939, 1944 (Mr Dugan for Methanex); Transcript Day 9, pp. 2151-2153 (Ms Guymon for the USA).

<sup>12</sup> Transcript Day 8, pp. 1944-1945.

<sup>13</sup> *Id.* at pp. 1940-1942.

*Party, non-discriminatory treatment with respect to measures it adopts or maintains relating to losses suffered by investments in its territory owing to armed conflict or civil strife.*

*3. Paragraph 2 does not apply to existing measures relating to subsidies or grants that would be inconsistent with Article 1102 but for Article 1108(7)(b)."*

Article 1108(7)(b), to which Article 1105(3) refers, provides: "(b) subsidies or grants provided by a Party or a state enterprise, including government supported loans, guarantees and insurance". Article 1131(2) provides: "2. An interpretation by the Commission of a provision of this Agreement shall be binding on a Tribunal established under this Section".

10. As recited earlier in this Award, the FTC issued on 31st July 2001 an interpretation of Article 1105(1), as follows:

*"B. Minimum Standard of Treatment in Accordance with International Law*

*1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.*

*2. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.*

*3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1)."*

The purport of this FTC interpretation has been discussed in a number of NAFTA arbitral awards<sup>14</sup>, some of which are relevant to this case.

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<sup>14</sup> See, e.g., *Metalclad Corp. v. Mexico*, 5 ICSID Reports 209 (Second Am. Claim App., 3 LA tab 85); *S. D. Myers v. Canada*, Partial Award 40 ILM 1408 (Second Am. Claim App., 4 LA tab 97); *Mondev Int'l Ltd. v. United States*, 6 ICSID Reports 181, 42 ILM 85 (Am. Defense App., 4 LA tab 61); *The Loewen Group, Inc. v. United States*, 42 ILM 811 (Am. Defense App., 4 LA tab 58); *ADF Group Inc. v. United States*, 6 ICSID Reports 470, (Am. Defense App., 1 LA tab 2).

11. The tribunal in *Mondev*, for example, emphasised that the application of the customary international law standard does not per se permit resort to other treaties of the NAFTA Parties or, indeed, other provisions within NAFTA<sup>15</sup>. The ADF tribunal emphasised that recourse to customary international law "must be disciplined by being based on State practice and judicial or arbitral case law or other sources of customary or general international law"<sup>16</sup>. The Loewen tribunal observed, by way of obiter dictum: "Manifest injustice in the sense of a lack of due process leading to an outcome which offends a sense of judicial propriety is enough, even if one applies the [FTC] Interpretation according to its terms"<sup>17</sup>.
12. Most recently, as more fully cited above from Methanex's argument, the NAFTA tribunal in *Waste Management* attempted the difficult task of synthesising the postinterpretation jurisprudence of Article 1105, as: "[T]he minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in any administrative process."
13. Methanex marshals a number of arguments, which are considered below. Ultimately, however, the Tribunal decides that Methanex's claim under Article 1105 fails for a number of reasons.
14. First, even assuming that Methanex had established discrimination under Article 1102, (which the Tribunal has found it did not) and ignoring, for the moment, the FTC's interpretation - the plain and natural meaning of the text of Article 1105 does not support the contention that the "minimum standard of treatment" precludes governmental differentiations as between nationals and aliens. Article 1105(1) does not mention discrimination; and Article 1105(2), which does mention it, makes clear that discrimination is not included in the previous paragraph. By prohibiting discrimination between nationals and aliens with respect to measures relating to losses suf-

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<sup>15</sup> *Mondev Int'l Ltd.*, paras. 120-121.

<sup>16</sup> *ADF Group Inc.*, para. 184.

<sup>17</sup> *The Loewen Group, Inc.*, para. 132.

ferred by investments owing to armed conflict or civil strife, the second paragraph imports that the preceding paragraph did not prohibit - in all other circumstances - differentiations between nationals and aliens that might otherwise be deemed legally discriminatory: *inclusio unius est exclusio alterius*. The textual meaning is reinforced by Article 1105(3), which makes clear that the exception in paragraph 2 is, indeed, an exception.

15. Elsewhere, when the NAFTA Parties wished to incorporate a norm of nondiscrimination, they did so - as one finds in Article 1110(1)(b) which requires that a lawful expropriation must, among other requirements be effected "on a nondiscriminatory basis". But Article 1110(1)(c) makes clear that the NAFTA Parties did not intend to include discrimination in Article 1105(1). Article 1110(1)(c) establishes that another requirement for a lawful expropriation is that it be effected "in accordance with due process of law and Article 1105(1)". If Article 1105(1) had already included a non-discrimination requirement, there would be no need to insert that requirement in Article 1110(1)(b), for it would already have been included in the incorporation of Article 1105(1)'s due process requirement.
16. This is not an instance of textual ambiguity or lacuna which invites a tribunal even to contemplate making law. When the NAFTA Parties did not incorporate a nondiscrimination requirement in a provision in which they might have done so, it would be wrong for a tribunal to pretend that they had. Thus, even if Methanex had succeeded in establishing that it had suffered a discrimination for its claim under Article 1102, it would not be admissible for it, as a matter of textual interpretation, to establish a claim under Article 1105.
17. This textual analysis places the FTC's interpretation in perspective. The interpretation, it will be recalled, stated in relevant part that: "3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1)". In clarifying that, for purposes of the present case, a determination of discrimination under Article 1102 would not establish a breach of Article 1105(1), the FTC simply confirmed the text.
18. In this respect, the rather severe words of the late Sir Robert Jennings, in his September 2001 legal opinion for Methanex - referring to the

"impropriety" of the FTC Interpretation under the circumstances of the case<sup>18</sup> - lack a predicate in this case. For, as far as Methanex's textual claim under Article 1105(1) was concerned, the interpretation changed nothing. Moreover, as a factual matter, the Tribunal cannot now assume that the three NAFTA Parties had Methanex's claim specifically in mind; the USA has observed that every NAFTA claimant in cases pending in 2001 has argued that the FTC interpretation was specifically targeted against it<sup>19</sup>.

19. If there were rules of customary international law prohibiting differentiations by a government between foreign investors or their investments and national investors or their investments, a matter to which the Tribunal will turn in a moment, Sir Robert's opinion might be more understandable; but in oral submissions at the main hearing Methanex cited only one case, which had been delivered a month earlier and whose purport is, on examination, not helpful to its argument.
20. But even if Methanex's assertions of the existence of a customary rule were correct, the FTC interpretation would be entirely legal and binding on a tribunal seised with a Chapter 11 case. The purport of Article 1131(2) is clear beyond peradventure (and any investor contemplating an investment in reliance on NAFTA must be deemed to be aware of it). Even assuming that the FTC interpretation was a far-reaching substantive change (which the Tribunal believes not to be so with respect to the issue relating to this case), Methanex cites no authority for its argument that far-reaching changes in a treaty must be accomplished only by formal amendment rather than by some form of agreement between all of the parties.
21. Article 39 of the Vienna Convention on the Law of Treaties says simply that "[a] treaty may be amended by agreement between the parties". No particular mode of amendment is required and many treaties provide for their amendment by agreement without requiring a re-ratification. Nor is a provision on the order of Article 1131 inconsistent with rules of international interpretation. Article 31(3)(a) of the Vienna Convention provides that:

*"3. There shall be taken into account, together with the context:*

*(a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions."*

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<sup>18</sup> Expert Op. of Robert Jennings, 6th September 2001.

<sup>19</sup> Rejoinder, para. 186.

22. Nor is Article 1131(2) improper under general principles of law or international constitutional principles. If a legislature, having enacted a statute, feels that the courts implementing it have misconstrued the legislature's intention, it is perfectly proper for the legislature to clarify its intention. In a democratic and representative system in which legislation expresses the will of the people, legislative clarification in this sort of case would appear to be obligatory. The Tribunal sees no reason why the same analysis should not apply to international law.
23. From the time of the *Alabama* award<sup>20</sup>, it has been accepted that States may agree to arbitrate by specifying the principles and rules of law they wish the tribunal to apply. This is frequently referred to as arbitration on an agreed basis<sup>21</sup>. When the parties wish to arbitrate on an agreed basis, a tribunal is then bound by law and honour to respect and give effect to the parties's selection of the rules of law to be applied.
24. Nevertheless, the Tribunal agrees with the implication of Methanex's submission with respect to the obligations of an international tribunal - that as a matter of international constitutional law a tribunal has an independent duty to apply imperative principles of law or jus cogens and not to give effect to parties' choices of law that are inconsistent with such principles. Yet even assuming that the USA errs in its argument for an approach to minimum standards that does not prohibit discrimination, this is not a situation in which there is a violation of a jus cogens rule. Critically, the FTC interpretation does not exclude non-discrimination from NAFTA Chapter 11, an initiative which would, arguably, violate a jus cogens and thus be void under Article 53 of the Vienna Convention on the Law of Treaties. All the FTC's interpretation of Article 1105 does, in this regard, is to confine claims based on alleged discrimination to Article 1102, which offers full play for a principle of non-discrimination.

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<sup>20</sup> The Washington Treaty of 8 May 1871 between the United Kingdom and the USA included agreement on three rules applicable to the United Kingdom as a neutral during the Civil War, which ensured that the United Kingdom would be held liable by the Geneva tribunal, even though these rules imposed higher duties than those previously accepted under international law (subject only to quantum and jurisdiction over the so-called "Indirect Claims"). See Tom Bingham, *The Alabama Claims Arbitration*, 54 ICLQ 1 (2005).

<sup>21</sup> See generally W. Michael Reisman, *Nullity and Revision: The Review and Enforcement of International Judgments and Awards* (1971).

25. As to the question of whether a rule of customary international law prohibits a State, in the absence of a treaty obligation, from differentiating in its treatment of nationals and aliens, international law is clear. In the absence of a contrary rule of international law binding on the States parties, whether of conventional or customary origin, a State may differentiate in its treatment of nationals and aliens. As the previous discussion shows, no conventional rule binding on the NAFTA Parties is to the contrary with respect to the issues raised in this case. Indeed, the text of NAFTA indicates that the States parties explicitly excluded a rule of non-discrimination from Article 1105.
26. Customary international law has established exceptions to this broad rule and has decided that some differentiations are discriminatory. But the International Court of Justice has held that "[t]he Party which relies on a custom of this kind must prove that this custom is established in such a manner that it has become binding on the other Party"<sup>22</sup>. In his oral submissions at the main hearing, Counsel for Methanex cited only one case. That award, *Waste Management*, in the relevant part of the excerpt quoted above, states that "the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is . . . discriminatory and exposes the claimant to sectional or racial prejudice . . ." <sup>23</sup>. The tribunal, presumably deriving this part of its synthesis from *Loewen*, opined that the conduct must have been "discriminatory and expose[d] the claimant to sectional or racial prejudice"<sup>24</sup>. The Tribunal need not comment on the accuracy of the cumulative requirement in this part of the *Waste Management* synthesis, since Methanex failed, as explained in Part III of this Award, to establish that California and the California ban on MTBE was discriminatory or in any way exposed it to "sectional or racial prejudice". Methanex offered no other authority for its assertion.
27. For all the above reasons, the Tribunal decides that Methanex's claim under Article 1105 NAFTA fails. The Tribunal also decides that Methanex's case under Article 1101 is not assisted by its arguments under Article 1105.

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<sup>22</sup> *Rights of Asylum (Colombia v. Peru)*, 1950 ICJ Rep. 266, 276 (US Reply Mem. on Jurisdiction, Admissibility, and the Proposed Amendment App., 1 LA tab 11).

<sup>23</sup> *Waste Mgmt. Inc.*, para. 98.

<sup>24</sup> *Id.* (emphasis added).

## **PART IV - CHAPTER D**

### **ARTICLE 1110 NAFTA**

#### **1) Introduction**

1. As in the Tribunal's consideration of Methanex's claims under Articles 1102 and 1105 in the previous chapters, the Tribunal has considered it appropriate to examine Methanex's claim arising under Article 1110 in order to determine if Methanex could thereby satisfy the threshold requirements of the required "relation" under Article 1101 NAFTA.

#### **2) Methanex's Case on Breach of Article 1110 NAFTA**

2. In summary, Methanex claims that a substantial portion of its investments, including its share of the California and wider US oxygenate markets, was taken by a discriminatory measure and handed to the US domestic ethanol industry. It submits that this was "tantamount . . . to expropriation" within Article 1110<sup>1</sup>. It also submits that the various exceptions listed in Article 1110 have been met, i.e. the US measures were not intended to serve a public purpose, were not in accordance with due process of law and Article 1105, and that no compensation has been paid<sup>2</sup>.
3. In its Second Amended Statement of Claim, Methanex's argument under Article 1110 is again commendably concise. Indeed, after reproducing the pertinent parts of Article 1110, Methanex makes its case that the California ban was expropriatory in four short paragraphs, which merit citation:

*"317. . . . First, a substantial portion of Methanex's investments, including its share of the California and larger U.S. oxygenate market were taken by facially discriminatory measures and handed over to the domestic ethanol industry. Such a taking is at a minimum "tantamount . . . to expropriation" under the plain language of Article 1110.*

*318. Second, these measures were not intended to serve a "public purpose" as is required by Article 1110(a), but rather were primarily a mechanism for seizing Methanex's, Methanex U.S.' and Methanex Fortier's share of the California*

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<sup>1</sup> Second Am. Claim at Section VII.C; Reply, paras. 207-208, 217.

<sup>2</sup> Second Am. Claim at Section VII.C; Reply, paras. 213-214.

*oxygenate market and handing it directly to the domestic ethanol industry.*

*319. Third, the discriminatory nature of the measures fail to meet the requirement of Article 1110 (c) that they comply with "due process of law and Article 1105(1)."*

*320. Finally, Methanex has not been compensated for the harms it has suffered as a result of these measures<sup>3</sup>.*

By its Amended Statement of Defense, the USA responded that Methanex had failed to establish in detail what investments had been taken and that allegations that the US measures, which it contends were not expropriatory, negatively impacted upon its investments fail to establish a taking<sup>4</sup>. In its Reply, Methanex argued that intentionally discriminatory regulations are not exempt from liability for expropriation and that, in this case, California's ban did expropriate its investments<sup>5</sup>. In its Rejoinder, the USA contended that Methanex has never proved that its assets were expropriated and argued that the ban was not expropriatory<sup>6</sup>.

4. At the main hearing in June 2004, Methanex also relied on the definition of expropriation under NAFTA decided by the tribunal in the *Metalclad* case, to the effect that:

*"... 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 the use of reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the Host state<sup>7</sup>."*

5. Methanex claims that California took Methanex's share of the California market and gave this to the ethanol industry, which amounted to a significant deprivation. Methanex also relies on the definition of

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<sup>3</sup> Second Am. Claim, paras. 317-320.

<sup>4</sup> See Am. Defense at Sections V.B-V.D.

<sup>5</sup> See Reply at Sub-section III.D.1.

<sup>6</sup> See Rejoinder at Part V.

<sup>7</sup> *Metalclad Corp. v. Mexico, Arb(AF)/97/1*, 5 ICSID Reports, 209, para. 103 (Second Am. Claim App., 3 LA tab 85); see Transcript Day 8, at 1949; Reply, para. 216.

investment in Article 1139(g) NAFTA, which includes a reference to intangible property, to support its contention that customer base, market share and goodwill may constitute investments which are the subject of an expropriation claim<sup>8</sup>. In addition, Methanex relies, inter alia, on the NAFTA awards in the *Pope & Talbot* and *S.D. Myers* cases as instances where NAFTA tribunals have recognised that market share is an investment capable of supporting an expropriation claim under Article 1110 NAFTA<sup>9</sup>.

### 3) The Tribunal's Decision Regarding Article 1110 NAFTA

6. In this case, there is no expropriation decree or a creeping expropriation. Nor was there a "taking" in the sense of any property of Methanex being seized and transferred, in a single or a series of actions, to California or its designees. Insofar as Methanex can make a claim under Article 1110(1), it is not a claim for nationalization or expropriation, simpliciter, but for "measures tantamount to expropriation". Thus, Methanex must establish that the California ban was tantamount to expropriation, within the meaning of Article 1110 NAFTA.
7. In the Tribunal's view, Methanex is correct that an intentionally discriminatory regulation against a foreign investor fulfils a key requirement for establishing expropriation. But 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 alios, a foreign investor or investment is not deemed expropriatory and compensable unless 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.
8. As the arbitration tribunal decided in *Revere Copper & Brass, Inc. v. OPIC* :

*"We regard these principles as particularly applicable where the question is, as here, whether actions taken by a government contrary to and damaging to the economic interests of aliens are in conflict with undertakings and assurances*

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<sup>8</sup> See Reply, paras. 218-221, 241.

<sup>9</sup> See Reply, para. 222; see also *Pope & Talbot, Inc. v. Canada*, Interim Award, para. 96 (NAFTA 2000) (Am. Defense App., 4 LA tab 71); *S. D. Myers v. Canada*, Partial Award, para. 281 (NAFTA 2000) (Second Am. Claim App., 4 LA tab 97).

*given in good faith to such aliens as an inducement to their making the investments affected by the action*<sup>10</sup>."

And in *Waste Management v. Mexico*, the tribunal stated, with respect to the "minimum standard of fair and equitable treatment", that "in applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied upon by the claimant"<sup>11</sup>.

9. No such commitments were given to Methanex. Methanex entered a political economy in which it was widely known, if not notorious, that governmental environmental and health protection institutions at the federal and state level, operating under the vigilant eyes of the media, interested corporations, nongovernmental organizations and a politically active electorate, continuously monitored the use and impact of chemical compounds and commonly prohibited or restricted the use of some of those compounds for environmental and/or health reasons. Indeed, the very market for MTBE in the United States was the result of precisely this regulatory process. Methanex appreciated that the process of regulation in the United States involved wide participation of industry groups, nongovernmental organizations, academics and other individuals, many of these actors deploying lobbyists. Methanex itself deployed lobbyists. Mr Wright, Methanex's witness, described himself as the government relations officer of the company<sup>12</sup>.
10. Methanex entered the United States market aware of and actively participating in this process. It did not enter the United States market because of special representations made to it. Hence this case is not like *Revere*, where specific commitments respecting restraints on certain future regulatory actions were made to induce investors to enter a market and then those commitments were not honoured.
11. Methanex has alleged that the process by which the California ban was enacted was "corrupted" by contributions from ADM to then-Lieutenant Governor, later Governor Davis. But, as noted in Chapter III B, political contributions to candidates for office in the United States are not prohibited and there is no indication in the record, still less any allegation from Methanex, that ADM's contributions

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<sup>10</sup> *Revere Copper & Brass, Inc. v. Overseas Private Invest. Corp.*, 56 ILR 258, 17 ILM 1321, 1331, cited in *Waste Mgmt. Inc.* (2004).

<sup>11</sup> *Waste Mgmt. Inc.*, 43 ILM 967, para. 98 (emphasis added).

<sup>12</sup> See Aff. of Robert T. Wright, 4th November 2002, para. 1 (Second Am. Claim Exh. B).

were in violation of the law or that Mr Davis behaved in violation of the law in this regard.

12. As Governor, Mr Davis followed the protocol established in California Senate Bill 521; there is no indication in the record that he varied from it in any way. Indeed, on the evidence adduced before this Tribunal, it would have been extraordinary if he had made a different decision. The terms of Governor Davis's Executive Order and subsequent action by the state of California are inconsistent with Methanex's contention that the California ban was designed to transfer the gasoline oxygenate market to ethanol<sup>13</sup>.
13. As against the public record, Methanex has developed a conspiratorial thesis, principally based on the general character of some of ADM's principal officers, a statement purportedly made by Senator Burton (which is supported only by unreliable hearsay), and an allegedly "secret" dinner which ADM hosted for Mr Davis. This thesis has already been considered in Chapter III B above. The first two bases do not lead the Tribunal to draw any appropriate, relevant conclusions, and Methanex has been unable to prove its suspicions about the dinner, an event which looms centrally in its thesis.
14. Methanex acknowledges that none of its submissions is conclusive and that its own conclusions are perforce inferential. Here, as so often elsewhere in its case, it urges the Tribunal to resort to inference. Inference is an appropriate mode of decision in circumstances in which firmer evidence is unavailable. But in the present case, where the time-line of California Senate legislation, scientific study, public hearing, executive order and initiatives to secure an oxygenate waiver are all objectively confirmed, the argument for resorting to inference as a way of reaching a conclusion inconsistent with the objective evidence is untenable. The behaviour of the California Government as a whole is inconsistent with Methanex's hypothesis.
15. For reasons elaborated here and earlier in this Award, the Tribunal concludes that the California ban was made for a public purpose, was non-discriminatory and was accomplished with due process. Hence, Methanex's central claim under Article 1110(1) of expropria-

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<sup>13</sup> See supra Chapter III B (noting, for example, that California's application for a waiver from the Clean Air Act's oxygenate requirement was inconsistent with the allegation that California intended to injure MTBE and methanol producers in order to transfer the market to the ethanol industry or to encourage the development of an ethanol industry in California).

tion under one of the three forms of action in that provision fails. From the standpoint of international law, the California ban was a lawful regulation and not an expropriation.

16. Nor has Methanex established that the California ban manifested any of the features associated with expropriation. In *Feldman v. Mexico*, the tribunal held that:

*"... the regulatory action has not deprived the Claimant of control of his company, . . . interfered directly in the internal operations . . . or displaced the Claimant as the controlling shareholder. The claimant is free to pursue other continuing lines of business activity . . . . Of course, he was effectively precluded from exporting cigarettes . . . . However, this does not amount to Claimant's deprivation of control of his company"<sup>14</sup>.*

Methanex claims that it lost customer base, goodwill and market share. The USA contends that none of these qualify as investments under Article 1139 and hence are not compensable.

17. The USA is correct that Article 1139 does not mention the items claimed by Methanex. But in *Pope & Talbot Inc. v. Canada*, the tribunal held that "the Investor's access to the U.S. market is a property interest subject to protection under Article 1110"<sup>15</sup>. Certainly, the restrictive notion of property as a material "thing" is obsolete and has ceded its place to a contemporary conception which includes managerial control over components of a process that is wealth producing. In the view of the Tribunal, items such as goodwill and market share may, as Professor White wrote, "constitute [] an element of the value of an enterprise and as such may have been covered by some of the compensation payments"<sup>16</sup>. Hence in a comprehensive taking, these items may figure in valuation. But it is difficult to see how they might stand alone, in a case like the one before the Tribunal.
18. For all the above reasons, the Tribunal decides that Methanex's claim under Article 1110 NAFTA fails. The Tribunal also decides that Methanex's case under Article 1101 is not assisted by its arguments under Article 1110.

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<sup>14</sup> *Feldman v. Mexico*, Arb(AF)/99/1, para. 152 (ICSID 2002) (Am. Def. App., 3 LA tab 33).

<sup>15</sup> *Pope & Talbot Inc.*, para. 96.

<sup>16</sup> Gillian White, *Nationalisation of Foreign Property* 49 (1961), cited at Am. Defense, para. 169, fn. 622.

## **PART IV - CHAPTER E**

### **ARTICLE 1101 NAFTA**

#### **1) Introduction**

1. Having concluded that an examination of the evidence in the record through the prisms of NAFTA Articles 1102, 1105, and 1110 fails, it remains for the Tribunal to determine whether the requirements of Article 1101 have been fulfilled.
2. Following the Partial Award, as recorded above, the Disputing Parties addressed the USA's extant jurisdictional objections, in writing and orally at the procedural meeting in March 2003 and the main hearing in June 2004. In short, the jurisdictional issue is whether the two US measures "relate" to Methanex as an investor or its investments within the meaning of Article 1101(1)(a) and (b) NAFTA.

#### **2) The USA's Case Regarding Article 1101(1) NAFTA**

3. The USA makes four main points in response to Methanex's contention that it has satisfied the jurisdictional requirements of Article 1101(1) NAFTA.
4. First, relying on the Partial Award, the USA contends that it is insufficient for Methanex to make a showing of intent to harm MTBE producers or to benefit ethanol producers, and that Methanex must prove that the intent underlying the ban of MTBE was to address methanol producers. It submits that, on the facts, Methanex has not come close to the required proof<sup>1</sup>. At the main hearing in June 2004, it also submitted that, given the joining of issues of jurisdiction to the merits under Article 21(4) of the UNCITRAL Rules, the issue of whether the US measures "relate to" methanol producers must now be decided on the factual evidence, not on the basis of any assumed facts in Methanex's favour<sup>2</sup>.
5. The USA's second main argument is that Methanex errs in suggesting that, even though it has no direct evidence that California intended to harm methanol producers, the Tribunal should consider its evidence regarding ethanol as relevant because ethanol and methanol compete as products<sup>3</sup>. It submits that this contention of Methanex fails on legal

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<sup>1</sup> E.g., Am. Defense, paras. 109-110; Rejoinder, paras. 16-20; id. at Section I.A.

<sup>2</sup> Transcript Day 2, pp. 477-478.

<sup>3</sup> E.g., Am. Defense, para. 111; id. at Section I.B.; Rejoinder at Section II.B.

and factual grounds. As to the legal grounds, the USA contends that the assertion of competition is no different from that originally pleaded by Methanex and rejected by the Tribunal in the Partial Award which, it submits, necessarily rejected the notion that mere cross-elasticity of demand between a feedstock, like methanol, and a downstream product, like ethanol, could supply the legally significant connection that was otherwise lacking<sup>4</sup>. It also submits that the Partial Award is final and binding on the Disputing Parties, including Methanex<sup>5</sup>.

6. As to the facts, the USA contends that the evidential record does not show the existence of the competition alleged by Methanex. It relies in particular on the evidence of Mr James Caldwell and Mr Bruce Burke to show that neither legally nor as a practical matter could methanol be used as a competing oxygenate to ethanol<sup>6</sup>. It contends that there is no "binary choice" between methanol and ethanol for the three groups of oxygenate consumers to which that Methanex refers; namely: integrated oil refineries, merchant ether-oxygenate producers and wholesale gasoline blenders<sup>7</sup>.
7. Third, the USA contends that Methanex, in its Reply, narrowed its contention on competition to one sub-category of the market, namely those integrated refiners in California that own gasoline refining, MTBE production, and gasoline distribution facilities<sup>8</sup>. The USA goes on to argue, however, that the evidential record does not establish that there are refiners in California of the type relied on by Methanex<sup>9</sup>, or that there is a market with respect to any such integrated refiners in which methanol and ethanol can be considered to compete in an economic sense<sup>10</sup>. It also submits that the evidence confirms that participants in the market view methanol as no more than a feedstock, while the absence of evidence of Methanex being affected by the MTBE ban confirms that the US measures do not relate to Methanex.
8. Fourth, the USA submits that the evidential record does not support

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<sup>4</sup> E.g., Rejoinder, paras. 5, 18; *id.* at Section II.B.

<sup>5</sup> E.g., *id.*, para. 42.

<sup>6</sup> E.g., Am. Defense at Section I.B (citing Mr Caldwell and Mr Burke); see also Bruce Burke, First Expert Report (December 2003) (13 JS tab B); Witness Statement of James W. Caldwell, 1st December 2003 (13 JS tab C).

<sup>7</sup> Am. Defense at Section I.B.

<sup>8</sup> Rejoinder, para. 36.

<sup>9</sup> *Id.*, para. 46. But cf. Am. Defense, para. 162.

<sup>10</sup> Am. Defense at Sub-Section I.B.3; Rejoinder at Sub-Section I.B.2.

Methanex's claims that the US measures were intended to benefit domestic ethanol producers<sup>11</sup>. The decision to ban MTBE was firmly grounded in the administrative and scientific record and the recommendations and findings of the UC Report. The USA relies on the expert evidence of Dr Fogg, Dr Happel and Professor Whitelaw to establish that the US measures were amply supported by the scientific information at the time the measures were adopted<sup>12</sup>.

9. In addition, the USA contends that questions of foreseeability are not to be equated with questions of intent. It submits that the former give rise to an objective test, while the latter give rise to a subjective test. To hold otherwise would be to impede the decision-making processes of policy makers, who may seek to predict possible impacts of measures that they pass, but are not therefore to be taken as having intended such impacts<sup>13</sup>. The USA also contends that no adverse inferences are to be drawn from the fact that members of the Andreas family did not appear as witnesses from ADM<sup>14</sup>. In this respect, it relies on Article 24(1) of the UNCITRAL Rules<sup>15</sup> (as well as Article 9(5) of the IBA Rules<sup>16</sup>) and contends that the criteria there for drawing adverse inferences are not met<sup>17</sup>.

### 3) Methanex's Case Regarding Article 1101(1) NAFTA

10. In its Second Amended Statement of Claim, Methanex challenges the two US measures adopted by California: the 1999 California

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<sup>11</sup> Am. Defense at Section I.C.

<sup>12</sup> Id. at Sub-section I.C.5., paras. 196-199.

<sup>13</sup> E.g., Rejoinder, paras. 12, 124.

<sup>14</sup> Id., para. 62.

<sup>15</sup> UNCITRAL Rules, Art. 24(1) ("Each party shall have the burden of proving the facts relied on to support his claim or defence.").

<sup>16</sup> Article 9(5) of the IBA Rules provides: "*If a Party fails without satisfactory explanation to make available any other relevant evidence, including testimony, sought by one Party to which the Party to whom the request was addressed has not objected in due time or fails to make available any evidence, including testimony, ordered by the Arbitral Tribunal to be produced, the Arbitral Tribunal may infer that such evidence would be adverse to the interests of that Party.*" (Methanex concedes that Article 9 of the IBA Rules has no direct application as there had been no agreement to apply this part of the IBA Rules in the joint letter of the Disputing Parties dated 14th August 2000.)

<sup>17</sup> Rejoinder, para. 62.

Executive Order and the 2000 California Regulations<sup>18</sup>. Methanex seeks to establish the required legally significant connection between the US measures and itself and its investments based on the claim that California intended to harm foreign methanol producers, including Methanex and conversely, to discriminate in favour of ethanol and ethanol producers, including ADM<sup>19</sup>.

11. According to Methanex, California's discriminatory intent was demonstrated by the unreasonableness of having the University of California purport to undertake the thorough and comparative analysis its researchers had been asked to do under California Senate Bill 521, but in a time frame and with funding which would not permit a proper analysis to be done. The UC Report, Methanex argues, was "heavily criticized by the U.S. Government itself"; and its researchers "bungled the cost analysis" by including the sunk costs of cleaning up the LUSTs<sup>20</sup>. Also, Methanex alleges that while the UC Report did not recommend an immediate ban, Governor Davis went beyond what the study recommended by, according to Methanex, effectively doing just that<sup>21</sup>.
12. Methanex contends that the evidence that a better solution was available, but not implemented, also indicates the presence of a malign intent. Methanex argues that it was undisputed that surface-water MTBE contamination was resolved by banning two-stroke engines, not by banning MTBE<sup>22</sup>. According to Methanex, for ground water contamination, "more suitable measures" would have required "complying with the longstanding federal UST upgrade mandate; accelerating [California's] own program to fix its leaking gasoline [USTs]; [or] stringently enforcing its UST laws . . ." <sup>23</sup>. Methanex concludes that singling out MTBE rather than banning "the use of all potentially harmful chemicals leaking from its underground gasoline storage tanks . . . implies an intent [by California] to benefit ethanol, not to protect the environment"<sup>24</sup>.
13. Methanex contends that California's leaking gasoline USTs gave the state a pretext for creating the previously non-existent ethanol market coveted by the ethanol lobby, as well as the in-state ethanol

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<sup>18</sup> Second Am. Claim, paras. 19-22.

<sup>19</sup> *Id.*, paras. 142-143.

<sup>20</sup> Transcript Day 1, at pp. 71 (lines 7-8), 70 (lines 18-19); Reply, para. 79.

<sup>21</sup> Transcript Day 1, at p. 72 (lines 6-17).

<sup>22</sup> Reply, para. 108.

<sup>23</sup> *Id.*, para. 156.

<sup>24</sup> *Id.*, para. 157.

industry that California had been unsuccessfully trying to create. Methanex argues that California accomplished these protectionist ends by banning all of ethanol's competitors, instead of adopting the obvious neutral option of addressing the underlying problem by eliminating leaking gasoline USTs.

14. Methanex notes that the 1999 California Executive Order banning MTBE specifically required state agencies to take steps intended to "foster ... biomass ethanol development in California"<sup>25</sup>. Moreover, Methanex points out the Executive Order called for such steps even though the UC Report on which it was purportedly based, had not evaluated the environmental risks associated with ethanol. Methanex alleges that California's discriminatory intent is confirmed by the testimony of Mr Michael P. Kenny, Executive Director of CARB, given on behalf of Governor Davis, before a US Senate committee in October 1999, in which he stated that "[o]nce MTBE is eliminated in California, the only feasible oxygenate will be ethanol"<sup>26</sup>. In addition, Methanex argues that "the California Executive Order did not require or even authorize the study of methanol or any other alternative to ethanol, even though methanol could have been substituted for MTBE rather than ethanol"<sup>27</sup>.
15. Discriminatory intent, according to Methanex, is also to be inferred from the role that ADM played in securing the California ban on its competitors. Relying upon Mr Listenberger's witness statement, Methanex argues that one of the questions for ADM at the time of the August 1998 meeting was whether it was going to support Mr Davis politically<sup>28</sup>. Methanex contends that "[t]he fact that ethanol was the purpose of the [August 1998] meeting can be inferred from all the ethanol participants who were there..."<sup>29</sup>. Methanex concludes that all of this, in the context of ADM's financial contributions to Mr Davis and others, points to ADM trading its political contributions for a share of the market in California<sup>30</sup>.
16. As Counsel for Methanex put it in his opening at the main hearing in June 2004, the core of Methanex's case is that the challenged measures constitute nothing more than a politically corrupt sham

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<sup>25</sup> *Id.*, para. 94.

<sup>26</sup> Testimony of Michael P. Kenny, Exec. Off., Cal. Air Res. Bd., for U.S. Senate, Comm. On Env't'l & Pub. Works, Subcomm. on Clean Air, Wetlands, Private Prop. & Nuclear Safety, at p. 6 (23 JS tab 45).

<sup>27</sup> Second Am. Claim, para. 159.

<sup>28</sup> Transcript Day 1, at p. 177 (lines 3-8); Witness Statement of Roger Listenberger, 24th October 2003 (13 JS tab F).

<sup>29</sup> Transcript Day 1, p. 177.

<sup>30</sup> *E.g.*, *id.*, p. 180.

designed by Governor Davis to protect the domestic ethanol industry (and ADM) and to harm foreign producers of methanol (and Methanex) because Governor Davis "succumbed to the temptation to favour the interest of large campaign contribut[ors]"<sup>31</sup>. Methanex argues that this is the "only credible inference that can be drawn from this pattern of facts . . . that led Governor Davis to both ban MTBE and then rush to embrace ethanol before any thorough evaluation of its advantages [or] disadvantages had been undertaken . . ."<sup>32</sup>.

17. Finally, Methanex submits that the legally significant relationship required by Article 1101(1) is evidenced by the latest amendments to the CaRFG3 regulations, effective on 1 May 2003. Those amendments which name methanol expressly as a prohibited oxygenate, are said clearly to satisfy the relationship test under Article 1101<sup>33</sup>.

#### **4) The Tribunal's Decision Regarding Article 1101(1) NAFTA**

18. On the evidence before us, the Tribunal concludes that Methanex has failed to establish, on the balance of probabilities, that in adopting the challenged measures California intended to harm foreign methanol producers, including Methanex.
19. To show intent, Methanex placed considerable emphasis on the alleged inadequacy of the scientific evidence supporting the MTBE ban and on the viability of other, less drastic remedial solutions. But the issue before this Tribunal under Article 1101 (on Methanex's pleaded case) is whether the California ban of MTBE was, in fact, intended to harm (or to address) producers and marketers of methanol. Thus, the question is whether the scientific conclusions which were presented to the Governor were so faulty that the Tribunal may reasonably infer that the science merely provided a convenient excuse for the hidden regulation of methanol producers. As we have seen from an examination of the UC Report and the whole of the scientific evidence presented in Chapter III, that proposition is simply not tenable on the evidential record adduced in these arbitration proceedings.
20. Thus, the Tribunal is satisfied that no malign pretext underlay California's conduct and measures, as represented by the California Executive Order and California Regulations. To our minds, the sci-

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<sup>31</sup> *Id.*, p. 181.

<sup>32</sup> *Ibid.*

<sup>33</sup> *E.g.*, *id.*, p. 123; Transcript Day 8, pp. 1799-1800.

entific and administrative record establishes clearly that Governor Davis and the California agencies acted with a view to protecting the environmental interests of the citizens of California, and not with the intent to harm foreign methanol producers. Faced with widespread and potentially serious MTBE contamination of its water resources, California ordered a careful assessment of the problem and thereafter responded reasonably to independent findings that large volumes of the state's ground and surface water had become polluted by MTBE and that preventative measures were called for. The evidential record establishes no ill will towards Methanex or methanol. Indeed, the weight of evidence (which we have considered above in Chapter III A of this Award) contradicts entirely one of Methanex's core assertions--that the US measures constituted nothing more than a politically corrupt sham designed by Governor Davis to protect the domestic ethanol industry (and ADM) and to harm foreign producers of methanol (and Methanex).

21. Moreover, the weight of the evidence as regards the personal conduct of Mr Davis, as the Lieutenant Governor and Governor of California (which we have considered above in Chapter III B of this Award) also contradicts entirely Methanex's other core assertion--that Mr Davis was motivated by a malign intent to favour ethanol and ADM, having succumbed to the temptation to favour the interest of large campaign contributors. First, there is no evidence of any such intent; nor any evidence that Mr Davis succumbed to any such temptation. Second, after the UC Report, the limited discretion allowed to the Governor of California under the California Senate Bill left Mr Davis with no rational alternative but to make his Executive Order; and indeed an order in any other terms would have seemed irrational at the time. Third, it does not avail Methanex to allege a politically corrupt sham when Methanex has from the outset expressly disclaimed any allegation of criminal conduct against Mr Davis.
22. Having concluded on the evidential record that no illicit pretext underlay California's conduct and that Methanex has failed to establish that the US measures were intended to harm foreign methanol producers (including Methanex) or benefit domestic ethanol producers (including ADM), it follows on the facts of this case that there is no legally significant connection between the US measures, Methanex and its investments. As such, the US measures do not "relate to" Methanex or its investments as required by Article 1101(1). Accordingly, the USA succeeds on its jurisdictional chal-

lenge under Article 1101, as regards Methanex's claim pleaded in its Second Amended Statement of Claim; and the Tribunal concludes that it lacks jurisdiction to determine Methanex's substantive claims alleged under NAFTA Articles 1102, 1105 and 1110.

## **PART IV - CHAPTER F SUMMARY AND CONCLUSIONS**

### **1) Introduction**

1. Given the Tribunal's decisions so far in this Award, as regards the jurisdictional issues under Article 1101 and issues under Articles 1002, 1005 and 1110 on the merits of Methanex's claim, it is unnecessary for the Tribunal to decide other issues relating to the merits. Nonetheless, given the fact that these issues were fully argued before the Tribunal and their potential relevance to the Tribunal's decisions on costs later in this Award, it is appropriate to summarise briefly what our decision might have been if seised with jurisdiction to decide such issues.
2. **Articles 1116 and 1117 NAFTA and Causation:** The Tribunal would be minded to decide these issues against Methanex and in favour of the USA, on the facts of this case.
3. **Loss and Damage:** The Tribunal would be minded to decide these issues against the USA and in favour of Methanex on the facts of this case, at this stage of these arbitration proceedings (quantum having been reserved to another hearing, if necessary).
4. **Ownership of Methanex-US and Methanex-Fortier:** The Tribunal would be minded to decide these issues against the USA and in favour of Methanex, given the weight of the evidential record comprising Mr McDonald's testimony and Methanex's annual returns adduced by the USA, at least at this stage of these arbitration proceedings (quantum being reserved, as already indicated).

### **2) Summary and Conclusions**

5. By virtue of the Tribunal's decisions above on the Disputing Parties' respective cases under Article 1101 NAFTA, it follows that the Tribunal has no jurisdiction to decide the merits of Methanex's claims in regard to the two US measures, the California Executive Order and the California Regulations. Accordingly, the Tribunal decides, pursu-

ant to Article 21 of the UNCITRAL Rules and Article 1101, that it has no jurisdiction to determine the claims advanced by Methanex in its Second Amended Statement of Claim.

6. By virtue of the Tribunal's decisions above on the Disputing Parties' respective cases under Article 1102, 1105 and 1110 NAFTA, it follows that Methanex's claims fail on the merits. Accordingly, assuming that the Tribunal had jurisdiction to determine the claims advanced by Methanex in its Second Amended Statement of Claim, the Tribunal decides, pursuant to Article 21(4) of the UNCITRAL Rules and Articles 1102, 1105 and 1110 NAFTA, to dismiss on their merits all claims there advanced by Methanex.
7. In these circumstances, there remains for decision by the Tribunal only the issues relating to the arbitration and legal costs of these proceedings under Articles 38, 39 and 40 of the UNCITRAL Rules, to which we turn next.

## **PART V ARBITRATION AND LEGAL COSTS**

### **1) Introduction**

1. An arbitration tribunal required to apply the UNCITRAL Rules has a broad discretion in relation to its award in respect of costs under Articles 38 and 40 of the UNCITRAL Rules.
2. Article 38 of the UNCITRAL Rules provides as follows:  
*"The arbitral tribunal shall fix the costs of arbitration in its award. The term "costs" includes only:*

*(a) The fees of the arbitral tribunal to be stated separately as to each arbitrator and to be fixed by the tribunal itself in accordance with article 39;*

*(b) The travel and other expenses incurred by the arbitrators;*

*(c) The costs of expert advice and of other assistance required by the arbitral tribunal;*

*(d) The travel and other expenses of witnesses to the extent such expenses are approved by the arbitral tribunal;*

*(e) The costs for legal representation and assistance of the successful party if such costs were claimed during the arbitral proceedings, and only to the extent that the arbitral tribunal determines that the amount of such costs is reasonable;*

*(f) Any fees and expenses of the appointing authority as well as the expenses of the Secretary-General of the Permanent Court of Arbitration at The Hague."*

3. Article 40 of the UNCITRAL Rules provides, in material part, as follows:

*1. Except as provided in paragraph 2, the costs of arbitration shall in principle be borne by the unsuccessful party. However, the arbitral tribunal may apportion each of such costs between the parties if it determines that apportionment is reasonable, taking into account the circumstances of the case.*

*2. With respect to the costs of legal representation and assistance referred to in article 38, paragraph (e), the arbitral tribunal, taking into account the circumstances of the case, shall be free to determine which party shall bear such costs or may apportion such costs between the parties if it determines that apportionment is reasonable... ."*

4. The Tribunal addresses separately below: (i) the Costs of the Arbitration under Articles 38(a), (b), (c) and (f) and 39(1)<sup>1</sup> of the UNCITRAL Rules; and (ii) the Disputing Parties' Legal Costs under Article 38(e) of the UNCITRAL Rules.

## **2) The Costs of the Arbitration**

5. The Tribunal determines that there is no compelling reason not to apply the general approach required by the first sentence of Article 40(1) of the UNCITRAL Rules. Although over the last five years, Methanex has prevailed on certain arguments and other issues against the USA, Methanex is the unsuccessful party both as to jurisdiction and the merits of its Claim. There is no case here for any apportionment under Article 40(1) of the Rules or other departure from this general principle. Accordingly, the Tribunal decides that Methanex as the unsuccessful party shall bear the costs of the arbitration.

6. It follows that Methanex shall be responsible for reimbursing the USA for all sums which the USA has deposited successively with the LCIA and ICSID as deposit-holder in connection with the costs of the arbitration together with interest accruing thereon, in the total amount of US \$1,071, 539.21 (comprising US \$1,050,000 by way of interim deposits and US \$21, 539.21 as interest).

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<sup>1</sup> Article 39(1) requires the fees of the arbitral tribunal to be reasonable in amount, taking into account inter alia the time spent by the arbitrators.

7. The unused balance on the deposit currently held by ICSID will be returned by the Administrative Secretary to whichever Disputing Party or Parties is appropriate, consistent with the Tribunal's decision and its implementation by Methanex. Subject to such reimbursement by Methanex in the full amount to the USA, the Tribunal's Administrative Secretary will liaise with the Disputing Parties to ensure that any balance of the deposit held by ICSID is applied accordingly and will make a written report to the Disputing Parties and the Tribunal in due course.
8. The total costs of the arbitration amount to approximately US \$1.5 million. In accordance with Article 38 of the UNCITRAL Arbitration Rules, a detailed written account will be provided by letter to the Disputing Parties as soon as practicable after this Award is communicated to the Disputing Parties, with a statement of all arbitral fees and expenses for each of the four Arbitrators, the Tribunal's Legal Secretaries, the Tribunal's Administrative Secretary, the LCIA and ICSID, together with a statement of the deposits held successively by the LCIA and ICSID that will take into consideration the several sums paid by the Disputing Parties and the interest credited on those sums.

### **3) The Disputing Parties' Legal Costs**

9. Both Disputing Parties have claimed an award in respect of their respective legal costs. The Tribunal has taken into account the practices of certain arbitration tribunals where no order is made in respect of legal costs. The practices of international tribunals vary widely<sup>2</sup>. Certain tribunals are reluctant to order the unsuccessful party to pay the costs of the successful party's legal representation unless the successful party has prevailed over a manifestly spurious position taken by the unsuccessful party. Other arbitral tribunals consider that the successful party should not normally be left out of pocket in respect of the legal costs reasonably incurred in enforcing or defending its legal rights.
10. In the present case, the Tribunal favours the approach taken by the Disputing Parties themselves, namely that as a general principle the successful party should be paid its reasonable legal costs by the unsuccessful party.

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<sup>2</sup> Wetter & Priem, "Costs and their Allocation in International Commercial Arbitrations" (1991) 2 Am Rev Int Arb 249.

11. In this case, the USA has emerged as the successful party, as regards both jurisdiction and the merits. The Tribunal has borne in mind that, at the time of the Partial Award, it could have been argued that the USA had lost several important arguments on the admissibility issues; but over time the Partial Award does not affect the end-result of the dispute overall, as decided by this Final Award. Likewise, the issues on which the USA did not prevail in this Award were of minor significance. The Tribunal does not consider any apportionment appropriate under Article 40(2) of the UNCITRAL Rules.
12. Accordingly, the Tribunal decides that Methanex shall pay to the USA the amount of its legal costs reasonably incurred in these arbitration proceedings. The Tribunal assesses that amount in the sum claimed by the USA, namely US \$2,989,423.76, which the Tribunal deems to be reasonable in the circumstances within the meaning of Article 38(e) of the UNCITRAL Rules. It is also far inferior to the sum claimed by Methanex in respect of its own legal costs, namely US \$11- 12 million.

#### **4) Summary**

13. For these reasons, the Tribunal decides that Methanex shall bear all the costs of the arbitration and shall pay to the USA (i) the sum of US\$ 2,989,423.76 in respect of the USA's legal costs and (ii) the sum of US\$ US \$1,071, 539.21, being the USA's share of the interim deposits paid for the costs of the arbitration. In addition, Methanex's claim for legal and arbitration costs is dismissed by the Tribunal.

## **PART VI THE TRIBUNAL'S OPERATIVE ORDER**

1. For the reasons set out above, the Tribunal makes the following decisions in this Award:
  - (1) *Jurisdiction*: The Tribunal decides, pursuant to Article 21 of the UNCITRAL Arbitration Rules and Article 1101 NAFTA, that it has no jurisdiction to determine the claims advanced by Methanex in its Second Amended Statement of Claim;
  - (2) *Merits*: Assuming that the Tribunal had jurisdiction to determine the claims advanced by Methanex in its Second Amended Statement of

Claim, the Tribunal decides, pursuant to Article 21(4) of the UNCITRAL Arbitration Rules and Articles 1102, 1105 and 1110 NAFTA, to dismiss on their merits all claims there advanced by Methanex;

(3) *Legal Costs*: The Tribunal decides, pursuant to Articles 38(e) and 40(2) of the UNCITRAL Arbitration Rules, that Methanex shall pay to or to the order of the USA the sum of US \$2,989,423.76 within 30 days of the date of this award in respect of the USA's legal costs incurred in these arbitration proceedings;

(4) *Arbitration Costs*: The Tribunal decides, pursuant to Articles 38(a), (b), (c) & (f), 39(1) and 40(1) of the UNCITRAL Arbitration Rules, that Methanex shall bear in full the other costs of the arbitration, requiring Methanex to indemnify the USA within 30 days of the date of this award in the further sum of US \$1,071,539.21.

Made by the Tribunal on [3 August] 2005;

Place of Arbitration: The International Centre for Settlement of Investment Disputes, The World Bank, Washington DC, USA.

[signed]

*J. William F. Rowley*

[signed]

*Van Vechten Veeder*

[signed]

*W. Michael Reisman*

## APPENDIX 1 TO THE AWARD

The California Senate Bill 1997

## APPENDIX 2 TO THE AWARD

The First US Measure: The California Executive Order D-5-99 of 25th March 1999 (the "California Executive Order")

## APPENDIX 3 TO THE AWARD

The Second US Measure: The California Phase Three Reformulated Gasoline Regulations of September 2000 (the "California Regulations")

## APPENDIX 4 TO THE AWARD

The Tribunal's Decision on the Place of Arbitration of 7th September 2000

## APPENDIX 5 TO THE AWARD

The Tribunal's Decision on Amici of 15th January 2001

## APPENDIX 6 TO THE AWARD

The Tribunal's Partial Award of 7th August 2002