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INTERNATIONAL LAWYERS

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*New York Toronto*

PRIVILEGED & CONFIDENTIAL

STATEMENT OF CLAIM  
UNDER THE ARBITRATION RULES  
OF THE  
UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW  
AND  
THE NORTH AMERICAN FREE TRADE AGREEMENT

BETWEEN:

POPE & TALBOT, INC.

Claimant / Investor

- AND -

GOVERNMENT OF CANADA

Respondent / Party

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Pursuant to Article 18 of the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL) and Articles 1116 and 1120 of the North American Free Trade Agreement (NAFTA), the Claimant hereby submits its Statement of Claim.

**A. NAMES AND ADDRESSES OF THE PARTIES**

Claimant/  
Investor                      POPE & TALBOT, INC.  
   1500 S.W. First Avenue  
   Portland, OR 97201

Respondent/  
Party                              GOVERNMENT OF CANADA  
   Office of the Deputy Attorney General of Canada  
   Justice Building  
   284 Wellington Street  
   Ottawa, ON K1A 0H8

**B. THE FACTS**

*Introduction*

This is a case about the discriminatory application of a quota scheme concerning exports from Canada. The complaint arises from an effect – perhaps accidental, perhaps intentional – of Canada's implementation of the most recent settlement between the United States and Canada of their long-running controversy over exports of softwood lumber from Canada. The essence of the controversy has been that the United States has taken the position that stumpage fees charged by Canadian provinces for harvesting lumber are set at below-market rates and that therefore the exports of lumber carry a subsidy against which the United States is entitled to impose a countervailing duty. Canada disagrees. In 1996 the two governments reached a provisional settlement whereby Canada agreed to impose an Export Control Regime to limit the quantity of softwood lumber exported from Canada to the United States. The Export Control Regime is not imposed on all exports, but only on certain exports from certain parts of Canada. The Claim in the present case is based on the unfair allocation of the rights to export softwood lumber free of the export fee (or at a reduced fee rate), in violation of several provisions of the Investment Chapter of NAFTA. This Claim is not about the legitimacy of the Canada-US *Softwood Lumber Agreement per se* but it is about the specific and unfair manner in which Canada chose to implement this Agreement.

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*Procedural History of the Dispute*

1. On December 24, 1998 Pope & Talbot, Inc., the Investor in this Claim, served upon the Government of Canada ("Canada") a Notice of Intent to Submit a Claim to Arbitration<sup>1</sup> ("Notice of Intent") in accordance with Article 1119 of the NAFTA. The Notice of Intent was delivered to Canada by the Investor at least 90 days before the submission of this Claim.
2. This Claim is submitted less than three years from the date the Investor first acquired, or should have first acquired, knowledge of the breach and knowledge that the Investor had incurred loss or damage, pursuant to Article 1116 of the NAFTA. Pursuant to Article 1120 of the NAFTA, the Investor submits this Claim on the basis that more than six (6) months have elapsed since the events giving rise to the Claim.
3. With the submission of this Claim on March 25, 1999, the Investor and the Investment have filed their waivers and the Investor has filed its consent to the extent required by NAFTA Article 1121(1).<sup>2</sup>
4. The Investor has fulfilled its obligations under Article 1118 of the NAFTA. Canada wrote to the Investor on January 5, 1999 requesting a meeting to consult.<sup>3</sup> From that date onwards the Parties exchanged numerous letters<sup>4</sup> in an attempt to agree upon a time and place for the consultation meeting. Despite the repeated attempts of the Investor to hold a consultation at a mutually-acceptable place and time, the disputing Parties were unable to agree to a consultation prior to the submission of this Claim. Canada has therefore waived any right to call for further and subsequent discussions.
5. The Investor submitted its Notice of Intent to Canada as a confidential document and it marked all pages of the document as such. On January 5, 1999, Canada informed the Investor that it intended to make the Notice of Intent public. On January 6, 1999, the Investor advised Canada that in its view the issues of whether and when specific documents such as the Notice of Intent are made public, and determinations as to

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<sup>1</sup> A copy of which is included as Schedule 1 to this Claim.

<sup>2</sup> A copy of which is included as Schedule 2 to this Claim.

<sup>3</sup> A copy of which is included in Schedule 3 to this Claim.

<sup>4</sup> Copies of these letters are included in Schedules 3 and 4 to this Claim.

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whether a document contains confidential information, are matters that must be mutually agreed upon between the disputing parties or be the subject of an order by the Tribunal.<sup>5</sup>

6. Despite the description by a previous NAFTA Investor-State Tribunal of the Notice of Intent as a "constitutive pleading" which was subject to confidentiality,<sup>6</sup> Canada unilaterally released the Notice of Intent to the Canadian media.<sup>7</sup>

### *Jurisdiction of this Tribunal*

7. The Investor's Claim is within the jurisdiction of this Tribunal. The Claim meets the requirements set out in Section B of Chapter 11 of the NAFTA, including the application of the UNCITRAL Arbitration Rules as applicable, for seeking compensation from an Investor-State Dispute Settlement Tribunal for any harm caused by the breach of a Party's obligations under Section A of Chapter 11.
8. Sections A and B of NAFTA Chapter 11 contain the contract between the disputing Parties and the arbitration agreement between them, pursuant to paragraph 1 of Article 18 of the UNCITRAL Arbitration rules. A copy of this NAFTA chapter is annexed to this Statement of Claim.<sup>8</sup>
9. To bring a claim, a claimant must be an investor of a Party. The Investor, Pope & Talbot, Inc., is a corporation incorporated in the State of Delaware in the United States of America. The Investor owns the Investment, Pope & Talbot Ltd., a company operating under the laws of British Columbia, through a wholly-owned subsidiary, Pope & Talbot International Ltd., a company also operating under the laws of British Columbia. Pope & Talbot Ltd. operates lumber manufacturing operations in the province of British Columbia, Canada.<sup>9</sup> Pope & Talbot Ltd. constitutes an "investment" as defined by NAFTA Article 1139.

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<sup>5</sup> A copy of which is included in Schedule 4 to this Claim.

<sup>6</sup> Award on Confidentiality, *Ethyl v. Canada*, July 2, 1998 at 2, a copy of which is included in Schedule 5 to this Claim.

<sup>7</sup> Press release dated February 15, 1999, contained in Schedule 3 to this Claim.

<sup>8</sup> A copy of which is included as Schedule 6 to this Claim.

<sup>9</sup> Copies of these incorporation documents are included as Schedule 7 to this Claim.

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*Canada's Infringing Measures*

10. Section A of Chapter 11 of the NAFTA requires each of the NAFTA Parties to provide a certain standard of treatment to the investors of each other Party. Section A includes the obligations:

(a) to grant national treatment to investors;<sup>10</sup>

(b) to provide most-favoured nation treatment to investors;<sup>11</sup> ] withdrawn by Investor

(c) to meet minimum standards of treatment;<sup>12</sup>

(d) to not impose performance requirements;<sup>13</sup> and

(e) to pay without delay the fair market value in the case of expropriation or a measure tantamount to expropriation.<sup>14</sup>

11. The Investor alleges in its Notice of Intent to Submit a Claim and in this Statement of Claim that Canadian government measures breach these obligations of Section A of Chapter 11 and have caused loss or damage to the Investor.

12. NAFTA Article 201 defines the term "measure" as including "any law, regulation, procedure, requirement or practice". This is a broad, non-exhaustive definition.

13. On March 19, 1996, Canada and the United States of America exchanged diplomatic letters through which Canada undertook to add certain softwood lumber products to its *Export Control List*. On March 26, 1996, Canada added softwood lumber products to the *Export Control List*,<sup>15</sup> thereby requiring exporters of softwood lumber products originating from the provinces of Quebec, Ontario, Manitoba, Alberta and British

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<sup>10</sup> NAFTA Article 1102.

<sup>11</sup> NAFTA Article 1103.

<sup>12</sup> NAFTA Article 1105.

<sup>13</sup> NAFTA Article 1106.

<sup>14</sup> NAFTA Article 1110.

<sup>15</sup> SOR/96-175, a copy of which is included as Schedule 8 to this Claim.

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Columbia to obtain an export permit in order to qualify to export such products to the United States of America.

14. On May 29, 1996, Canada and the United States of America entered into a bilateral agreement, entitled the *Softwood Lumber Agreement*.<sup>16</sup> This five-year-long Agreement, retroactive to April 1, 1996, established a limit on the free export of softwood lumber by Canadian softwood lumber producers into the United States.
15. In order to give effect to the *Softwood Lumber Agreement*, Canada created the following Export Control Regime (the "Export Control Regime"):
  - (a) Canada amended the *Export Control List*<sup>17</sup> to require that exporters of softwood lumber products originating from the provinces of Quebec, Ontario, Alberta and British Columbia (the "Listed Provinces") obtain an export permit to export such products to the United States of America;
  - (b) Canada promulgated the *Export Permits Regulations (Softwood Lumber Products)*<sup>18</sup> to provide for a permit application regime for softwood lumber exporters;
  - (c) Canada promulgated the *Softwood Lumber Products Export Permits Fees Regulations*<sup>19</sup> to require the payment of fees for the issuance of export permits for softwood lumber products; and
  - (d) Canada provided for a discretionary allocation regime that authorized the Canadian Minister of Foreign Affairs and International Trade (the "Minister") to

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<sup>16</sup> A copy of which is included as Schedule 9 to this Claim.

<sup>17</sup> SOR/96-315, a copy of which is included as Schedule 10 to this Claim.

<sup>18</sup> SOR/96-319, as amended by SOR/96-480, enacted under paragraphs 12(a) and (b) of the *Export and Import Permits Act*, R.S.C. 1985, c. E-19, as amended by S.C. 1994, c. 47, s. 112(1), copies of which are included as Schedule 11 to this Claim.

<sup>19</sup> SOR/96-317, as amended by SOR/96-481, enacted under paragraphs 19(1)(a) and 19.1(a) of the *Financial Administration Act*, R.S.C. 1985, c. F-11, copies of these provisions are included as Schedule 12 to this Claim.

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exempt certain producers from paying the full fee for export permits, based upon the annual quota levels fixed under the *Softwood Lumber Agreement*.<sup>20</sup>

16. On October 31, 1996, the Minister issued *Notice to Exporters No. 94*,<sup>21</sup> which outlined Canada's policy regarding who would qualify for a limited exemption from paying fees to obtain the mandatory export permits. *Notice No. 94* stated that only certain softwood lumber producers in the Listed Provinces would qualify for allocation of the annual quota levels fixed under the *Softwood Lumber Agreement* and that export permits would only be issued at the discretion of the Minister.
17. In addition to *Notice No. 94*, a number of other notices<sup>22</sup> have been issued by Canada. Including *Notice No. 94*, these notices govern how the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of the businesses of lumber producers are affected by Canada's allocation of quota including:
- (a) How Canada treats the acquisition or expansion of a softwood lumber producer's business with respect to quota allocation;
  - (b) How Canada treats the transfer of quota already allocated based on a "business as usual approach"; and
  - (c) How work stoppages and other uncontrollable events impacting on a producer's business or investment affect Canada's decisions regarding allocation of quota.
18. Under the Export Control Regime, producers of softwood lumber from the Listed Provinces that export to the United States of America are required by Canada to pay the fee called for by the *Softwood Lumber Agreement*. This fee is currently US\$104.18 per thousand board feet.
19. If the Minister determines that a producer qualifies under Canada's quota allocation policy, the producer is permitted to export a limited amount of softwood lumber to the United States "fee-free" (i.e. without the US\$104.18 permit charge) and to export a lesser amount of softwood lumber at the lower fee base ("LFB") rate, which is currently US\$52.09 per thousand board feet.

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<sup>20</sup> As per Article II (2) of the *Softwood Lumber Agreement*.

<sup>21</sup> A copy of which is included as Schedule 13 to this Claim.

<sup>22</sup> Copies of which are included as Schedule 14 to this Claim.

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20. Softwood lumber producers located in the Non-listed Provinces and territories (i.e. Saskatchewan, Manitoba, New Brunswick, Prince Edward Island, Nova Scotia, Newfoundland, the Yukon or the Northwest Territories) do not require permits to export to the United States. These producers do not have to pay any export permit fees.<sup>23</sup>
21. Canada's measures that have resulted in harm to the Investor and its Investment in Canada include:
- (a) requiring permits for export to the United States of softwood lumber products originating in only the provinces of British Columbia, Alberta, Ontario and Quebec under the *Export Control List*;
  - (b) requiring the payment of export permit fees; and
  - (c) unfairly and inequitably allocating "fee-free" and "LFB" quota amounts to the Investment of the Investor from 1996 onwards.

#### *The Softwood Lumber Industry*

22. The North American softwood lumber industry is a stable and mature industry with an established base of customers, markets and products. Canadian softwood lumber exports to the United States ("US") represent a one-third share of US softwood lumber consumption. Canada has historically exported as much as 65% of its lumber production to the US.<sup>24</sup>
23. The export of Canadian softwood lumber to the US has been an important and highly contentious feature of the Canada-US trading relationship. Disputes between these countries over softwood lumber exports have continued for the past 20 years.<sup>25</sup>

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<sup>23</sup> Article III (5) and (6).

<sup>24</sup> *Canada-United States Softwood Lumber Agreement - Quarterly Statistical Monitor*, No. 7, Fourth Quarter Ending December 31, 1998, Published January 1999, (hereafter referred to as the "QSM"). Tables 1 & 2, copies of which are attached as Schedule 15 to this Claim.

<sup>25</sup> *The North American Wood Products Market, Outlook for 1998 to 2002*, Widman & Associates, September 1998 (hereafter referred to as "Widman") at 37-38, for a brief chronological synopsis of the ongoing dispute.

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24. The most recent attempt to resolve the on-going Canada-US softwood lumber dispute is the *Softwood Lumber Agreement*, which is in effect until March 31, 2001. In the *Agreement*, Canada has agreed to limit fee-free lumber exports to the US to a maximum of 14.7 billion board feet ("BBF") annually from the four main producing provinces: Ontario, Quebec, Alberta and British Columbia.
  25. The *Softwood Lumber Agreement* is not the subject of this Claim. Rather, this dispute arises from the Investor's claim that Canada has breached its NAFTA obligations with respect to the unfair and inappropriate implementation of Canada's obligations under the *Softwood Lumber Agreement*.
  26. Softwood lumber is a standardized product that is one of the primary materials used in building construction in North America. New residential housing accounts for over one-third of softwood lumber consumption and repair and remodelling accounts for slightly over 30% of consumption. The remainder of consumption is accounted for through non-residential construction and materials handling.<sup>26</sup>
  27. The North American softwood lumber market is a commodity market.<sup>27</sup> There is virtually no market differentiation for standard commodity softwood lumber based on where the product is harvested or where it is manufactured. In Canada, all softwood lumber producers, whether in British Columbia or any other province, sell their products based on the same universal grading system.<sup>28</sup>
  28. Purchasers in the North American market generally expect and receive a standard commodity product. Because the market for softwood lumber is a commodity market, there is no premium for the actual product from a specific company or region. The main criteria for softwood lumber purchasers when making purchase decisions for a standard graded product is price.
  29. The price of softwood lumber is determined independently by producers on a weekly basis or even more frequently depending on supply and demand.

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<sup>26</sup> Widman 1998 at 2, 31.

<sup>27</sup> David Leckey, *Buying and Selling Softwood Lumber* (Random Lengths Publications, Eugene Oregon: 1998) at 3. The author describes the North American softwood lumber market as a "near perfect example of a 'free market', controlled only by supply and demand."

<sup>28</sup> National Lumber Grades Authority, *Standard Grading Rules for Canadian Lumber* (N.L.G.A., Vancouver B.C.: 1990), an excerpt from which is included as schedule 16 to this Claim.

30. In 1998, US softwood lumber consumption reached a record high of approximately 52.5 BBF.<sup>29</sup> In 1997, US softwood lumber consumption was approximately 51 BBF, with 18 BBF being imported from Canada. This represented approximately a 35% share of the US softwood lumber market for imports from Canada.<sup>30</sup>

31. Despite record US consumption, British Columbia's softwood lumber production has declined over the past three years. British Columbia has been the "only major producing region in North America to experience a decline in softwood lumber production between 1996 and 1997".<sup>31</sup> Commentators on the softwood lumber industry have further noted that:

*While a few sawmill closures and curtailments have taken place in the United States over the past year, (statistics) show that the British Columbia industry was the clear loser. Between calendar year 1996 and October 1998 BC softwood lumber production plummeted by 1.139 billion board feet ... the BC interior still lost close to 400 million board feet, in spite of the fact that 80-90% of regional output is shipped to the United States.<sup>32</sup>*

32. The dramatic decline of coastal British Columbia's softwood lumber production can be attributed in large part to the collapse of the Japanese market. This collapse does not explain the decline of consumption of interior British Columbia's softwood lumber by the US. Since the beginning of the *Softwood Lumber Agreement*, the Province of British Columbia has had a declining share of the US softwood lumber market while Canada's overall share has remained in the 34-35% range.<sup>33</sup>

33. In the calendar year prior to Canada implementing its Export Control Regime, 1995, British Columbia possessed a 19.78% share of the US consumption of softwood lumber.

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<sup>29</sup> Doug Smyth, *The Impact of US and Canadian Softwood Lumber Production, Consumption and Shipments to Japan on Prices, 1996 To 1998 - Part 2*, I.W.A. Canada, January 1999 (hereafter referred to as the "I.W.A. Report"), at 2-3. This is a projected figure as 4<sup>th</sup> quarter 1998 statistics were not yet available.

<sup>30</sup> QSM, Table 5 - "United States Apparent Softwood Lumber Consumption by Source of Supply".

<sup>31</sup> I.W.A. Report 1999, at 5.

<sup>32</sup> I.W.A. Report 1999, at 25.

<sup>33</sup> QSM, No. 7, Tables 5 and 6, copies of which are attached as Schedule 17 to this Claim.

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By the end of 1997, a year and a half into the term of the Agreement, that British Columbia share had declined to 17.40%.<sup>34</sup>

*Operations in the Canadian Softwood Lumber Industry*

34. The Investor operates three (3) lumber mills in the British Columbia southern interior through its Investment:
- (1) Castlegar, in the Arrow Lakes region, is the Investment's largest mill with production of approximately [REDACTED] board feet per day. The products produced at Castlegar include machine stress rated ("MSR") and dimension lumber from multiple species of fibre, including Spruce-Pine-Fir ("SPF"), Hemlock/ Fir, and Fir/ Larch;
  - (2) Grand Forks, and (3) Midway are located in the Boundary Region of the British Columbia interior producing MSR and dimension lumber, and to a lesser extent, boards and timbers. Multiple species of fibre are processed, dominated by SPF, Fir/ Larch and Cedar.

In addition, the Investor controls Harmac Pacific Inc., a publicly traded pulp and paper company that operates a facility located at Nanaimo, British Columbia.

35. The Investment is a commodity producer manufacturing almost entirely commodity grade softwood lumber for the softwood lumber market. A recent study has rated the Investment's mills as among the most efficient in British Columbia with high recovery rates. The Investment has no retail sales operations.
36. The Investment primarily obtains the timber used to produce softwood lumber from two sources:
- (a) Forest licences and other rights from the Province of British Columbia; and
  - (b) Third parties using their own rights to cut timber.

These two sources have provided the Investment with sufficient timber to increase its capacity to meet market demand.

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<sup>34</sup> QSM, No. 7, Tables 5 and 6.

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37. The Investor and the Investment determines the price at which it sells its product based on the available price as determined by the commodity market. Most sales transactions are made on an "F.O.B." basis. The price of softwood lumber is determined by the Investor and the Investment on a weekly basis or even more frequently depending on supply and demand. The Investor and Investment assess the market price using research tools, such as price reporter newsletters, to indicate recent activity in the market in the previous week. In conjunction with price reporters, the Investor's and the Investment's network of intermediaries maintain contact with customers to help determine market price at any time.
38. One of the main factors with respect to determining total price (i.e. with freight cost included) is the proximity of the mill to the market. The Investment has direct railroad access to the US market from the Burlington Northern Sante Fe Railway, Union Pacific, Canadian Pacific and road links with the use of common carriers. This access to the US market assists the Investment to maintain competitive prices.
39. In 1994, the Investment had total sales of softwood lumber of approximately [REDACTED] board feet ("MMBF"). This included [REDACTED] in sales to the US. In 1995, the Investment had total sales of softwood lumber of approximately [REDACTED]. This included an estimated [REDACTED] in sales to the US. Approximately 94% of the total sales of the Investment are exported to customers in the United States.

#### *The Softwood Lumber Agreement*

40. Under the *Softwood Lumber Agreement*, the Government of United States of America committed to Canada not to permit the use of its domestic trade remedy laws against softwood lumber imports from Canada.
41. Under the *Softwood Lumber Agreement*, Canada committed to the Government of the United States of America that it would put a permit mechanism into place to monitor and restrain the export of softwood lumber produced in Quebec, Ontario, Alberta and British Columbia to the United States. The Agreement left it up to Canada to determine how to implement these commitments.
42. Canada agreed to restrain exports of softwood lumber in the following manner:
- (a) 14,700,000,000 board feet of softwood lumber products from the Listed Provinces per year could be exported to the United States without payment of a permit fee (the "established base" or "EB");

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- (b) 650,000,000 board feet per year could be exported with payment of a US\$50 per thousand board feet permit fee (the "lower fee base" or "LFB"); and
  - (c) all other exports would be subject to a fee of US\$100 per thousand board feet (the "upper fee base" or "UFB").<sup>35</sup>

- 43. The *Softwood Lumber Agreement* also contained a trigger price mechanism, which could result in an additional 92 million board feet of "fee-free" quota being made available after every quarter in which the price of selected softwood lumber benchmark products reached a fixed market price.<sup>36</sup>
- 44. The *Softwood Lumber Agreement* provided that Canada would be responsible for allocation of the EB and LFB among softwood lumber exporters. Canada was to have done so by no later than September 30, 1996.<sup>37</sup> Canada did not comply with this obligation and did not allocate the EB and LFB quotas until November 1996.
- 45. The Investor and the Investment were not parties to the *Softwood Lumber Agreement* nor did they participate as negotiators on behalf of the softwood lumber industry. The Investor's only direct involvement with the *Softwood Lumber Agreement* was its consent to waive its domestic US trade remedy rights.<sup>38</sup>

#### Quota Allocation

- 46. On June 19, 1996, Canada issued *Notice to Exporters No. 92*. This notice contained a questionnaire to survey the historic export performance of softwood lumber producers, secondary manufacturers and wholesalers in the Listed Provinces (between 1994 and the first quarter of 1996). *Notice No. 92* also provided an address and facsimile number to which comments about the method of allocation could be sent. The Investor completed its questionnaire and submitted it on July 19, 1996.

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<sup>35</sup> Under Article II(3), these fees are adjusted annually for inflation.

<sup>36</sup> Article III(1).

<sup>37</sup> Article II(4).

<sup>38</sup> A copy of which is included as Schedule 18 to this Claim.

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47. A coalition of industry associations from British Columbia, Alberta and Quebec sent a joint submission to the Minister on June 19, 1996, concerning the issue of quota allocation. The Investor was not directly involved in its drafting.
48. The Submission contained the following eight points of agreement:
1. Quota should be allocated to primary producers and re-manufacturers.
  2. Quota must be allocated to companies, with a separate allocation for each company's operations within each of the four provinces.
  3. Quota must be transferable.
  4. To avoid speculation, quota may only be held by or sold to primary producers and re-manufacturers or sold with softwood lumber.
  5. Fees paid for additional export rights for lumber from the four provinces must be returned to the respective provinces by the Government of Canada.
  6. Quota must be allocated by province.
  7. Allocations shall be made for the term of the agreement. Allocations will be reviewed annually for the purpose of reallocating unused quota within a province and will be redistributed among the other provinces.
  8. The Government of Canada should take the advice of the advisory committees established by each of the affected provinces in making quota allocations or considering transfers within the provinces. Transfers between provinces will normally be viewed positively (recommended) if the applicant can demonstrate there would be no adverse effect on the operation from which the quota is transferred.<sup>39</sup>
49. On August 9, 1996, the Quebec Association of Softwood Lumber Manufacturers provided the Minister with a separate submission that argued for a single scheme of quota allocation, rather than one based on provincial allocations related to historic export levels. It also argued for a 4% reserve of the EB quota to be set aside for "new entrants", rather than producers with established markets and existing capacity, such as the Investor.
50. Issued on October 31, 1996, Canada unveiled the basic framework of its quota allocation policy with *Notice to Exporters No. 94*. Under Canada's new policy, allocation was purportedly to be made on a provincial basis. The provincial share of available EB and LFB quota was calculated by:

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<sup>39</sup> Affidavit of Claudio Valle, Director of Trade Controls Policy Division, Export and Import Control Bureau, Department of Foreign Affairs and International Trade, dated January 15, 1997 at 8-9.

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- (a) determining the total exports to the United States from each Listed Province for 1995;
  - (b) adding the total for all four Listed Provinces combined; and
  - (c) dividing the total exports for each Listed Province by the total.
51. Using this formula, British Columbia was to receive 59% of the available EB and LFB quota.
52. Individual producers were to receive their respective share of the total EB and LFB quota allocated to each Listed Province on a pro-rata basis. In British Columbia, the pro-rata amount for each primary producer was determined by:
- (a) arriving at an historic export number (i.e. the average of a producer's export performance for 1994 and 1995, or the performance in 1995 alone, if the average would result in a number 35% lower than the 1995 number);
  - (b) totalling the historic export numbers of each producer; and
  - (c) dividing each firm's historic export number by the total.
53. The initial amounts of available EB and LFB quota were reduced by Canada through the creation of a number of reserves. Accordingly, British Columbia did not receive 59% of 14.7 billion board feet of EB, or 59% of 650 million board feet of LFB quota, and as such, softwood lumber producers in British Columbia did not receive their full share of the overall EB and LFB quotas. Instead, they received their pro-rata share of British Columbia's portion, after the reserves were deducted.
54. Initial allocation of the 14.7 billion board feet of EB quota was subject to the following reserves:
- (a) 294 million board feet for the Minister to allocate to "new entrants";
  - (b) 170 million board feet for the Minister to award as one-time, transitional adjustments; and
  - (c) 50 million board feet for the Minister's reserve.

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55. Initial allocation of the 650 million board feet of LFB quota was subject to the following reserves that were at the discretion of the Minister:
- (a) 110 million board feet to allocate to "new entrants"; and
  - (b) 50 million board feet to award as one-time, transitional adjustments.
56. It has never been clear what specific criteria were to be used by the Minister to allocate his discretionary, transitional reserves. The allocation of transitional reserves was not allocated on a provincial basis. British Columbia producers did not receive their historic share of these reserves (i.e. a cumulative share equal to 59% of the available reserves).
57. Although the Minister set out basic criteria for allocation of the reserves for new entrants, there is no evidence that British Columbia producers received their historic share of the new entrants reserves (i.e. a cumulative share equal to 59% of the total available).
58. In addition to the amounts of initial EB and LFB quota set aside by the Minister for new entrants, 184 million board feet of bonus "fee-free" quota was also set aside for new entrants in 1996. This additional 184 million board feet of bonus quota was obtained by way of the trigger price mechanism set out in the *Softwood Lumber Agreement*. In this case it was triggered during the first two quarters of the operation of Canada's Export Control Regime. Allocations from the new entrants reserve were to be used by no later than March 31, 1998.
59. In determining EB and LFB quota allocations for the second and third years of the operation of the Export Control Regime, the Minister departed from a formula that would guarantee to producers a fair share based upon their historic export performance.
60. The Minister used the preceding year of exports for each producer as the basis for his allocation in the following year (i.e. 1996/97 export totals were used to calculate 1997/98 allocations). The Minister included the utilisation of reserve allocations made in the previous year. Including utilisation of reserve allocations in the calculation of a producer's export performance for the coming year compounded this negative effect. Not only was the reserve allocation recipient given the benefit of extra EB and LFB quota in the first 18 months of the Export Control Regime, the recipient could also claim to have exported more than those who were given no extra EB or LFB quota.

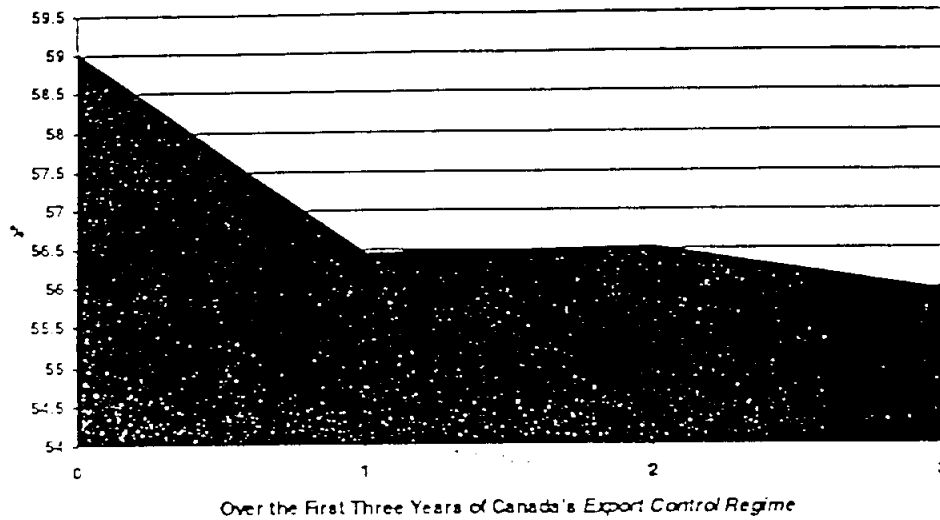
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Therefore such a recipient was given a greater share of the EB and LFB quota for the following years than they otherwise would have been entitled to.

61. The effect of the Minister's inclusion of reserve allocations in calculation of entitlement for future years was to arbitrarily and inequitably redistribute EB and LFB quota among the Listed Provinces.
62. As indicated in the graphs on the following page, British Columbia's share of fee-free softwood lumber exports has fallen from 59% prior to Canada's imposition of the Export Control Regime to under 56% by March 1999.
63. Producers in Quebec, who were attributed with only 23.0% of the historic share of the total exports, were responsible for exporting 25.3% of fee-free quota lumber to the United States by the fourth quarter of year three (i.e. by March 4, 1999). This is an increase of approximately 10% of the allocation of EB quota to Quebec.
64. In addition to the inequitable transfer of EB quota from British Columbia to producers in other provinces, Canada has also allocated bonus amounts of EB quota (derived either from extra "fee-free" quota awarded under the trigger price mechanism or from a redistribution of unused quota from other companies) in an unfair and inequitable manner.
65. During the second year of the *Softwood Lumber Agreement* (April 1, 1997 to March 31, 1998), producers in Quebec were allocated over 44% of "bonus" quota, whereas producers in British Columbia were provided with only 33% of bonus quota. British Columbia producers were entitled to 59% of bonus quota based on their historic share of Canadian exports to the United States, and the promise that the Minister would allocate quota on a provincial basis as set out in *Export Notice No. 94*.

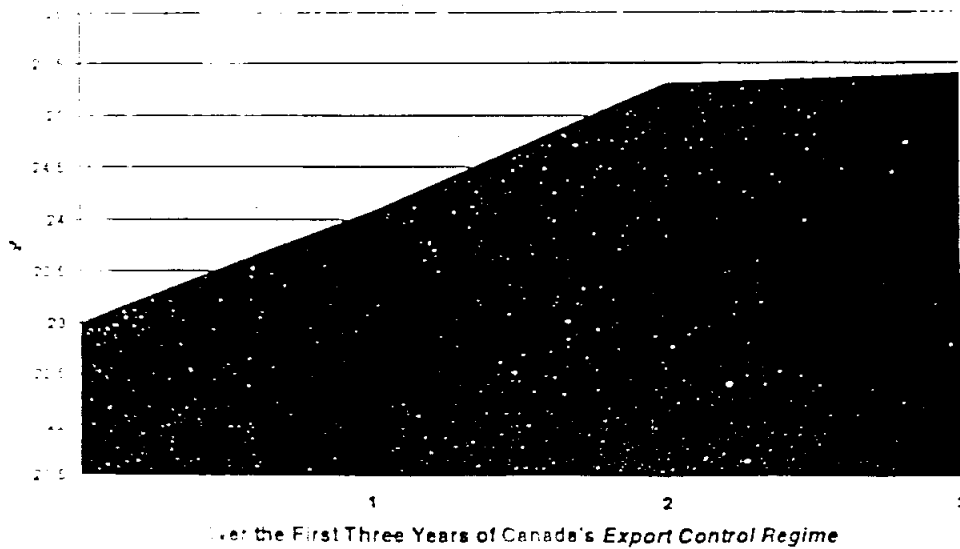
British Columbia's Declining Share of Fee-Free Softwood Lumber Exports

Source: Canada, Export and Import Control Bureau

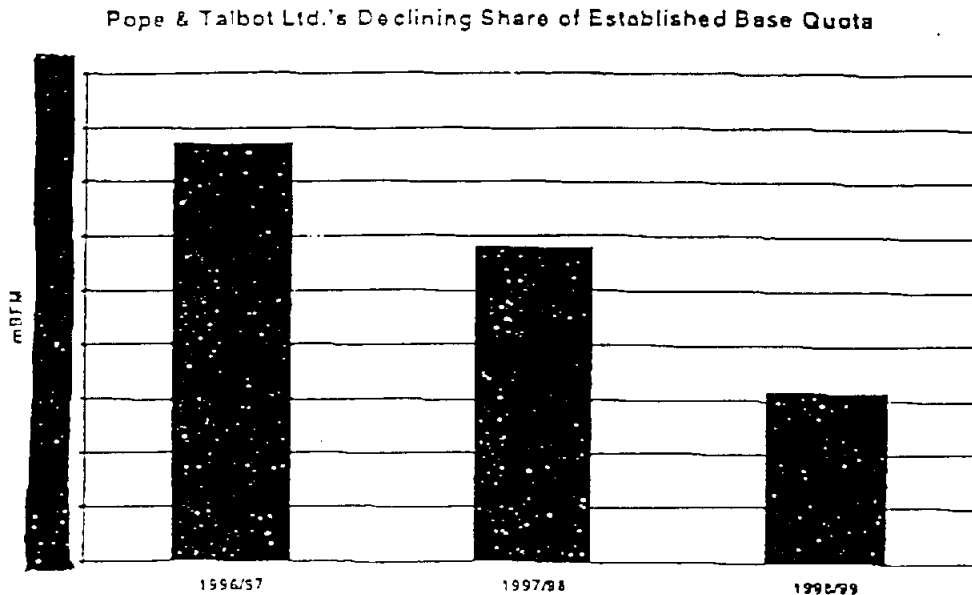


Quebec's Increasing Share of Fee-Free Softwood Lumber Exports

Source: Canada, Export and Import Control Bureau



66. As indicated in the following graph, the Investment, despite having always fully utilised the EB and LFB quota allocated to it (and therefore not having ever been penalised for under-utilisation), has suffered a loss of 6.3% in allocated EB quota over the first three years of the *Softwood Lumber Agreement*. This is a decrease of almost 25% more than the average loss of quota experienced by other producers in the Province of British Columbia.

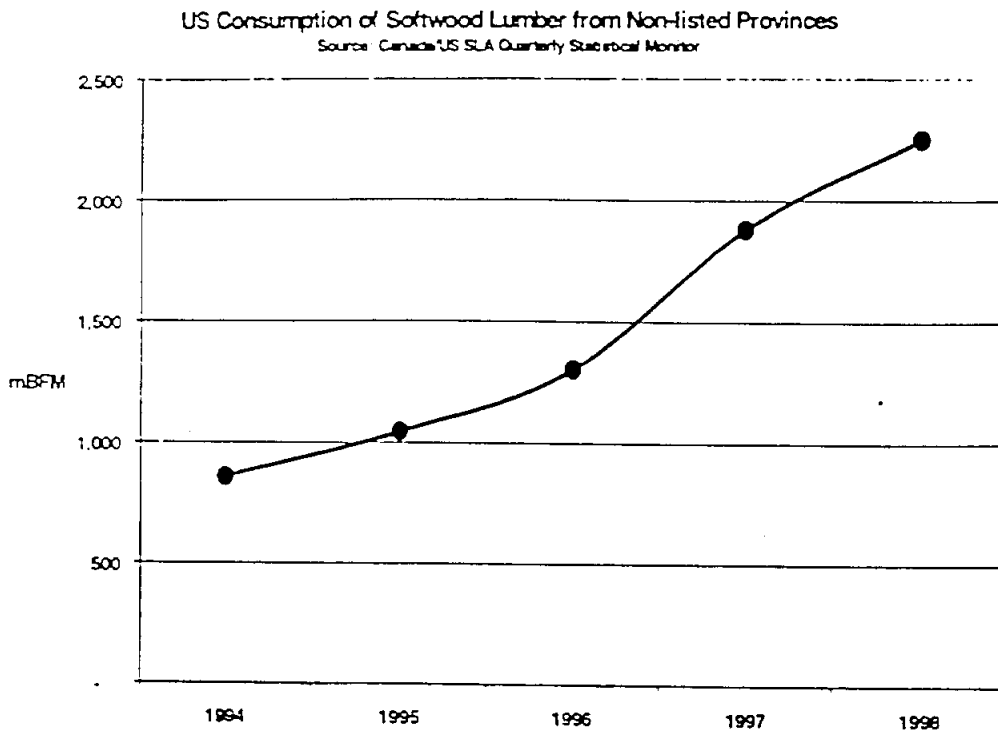


67. The Investment contacted Canada for an explanation and for redress about what it felt was an unfair and inequitable distribution of EB quota. In response, Canada informed the Investor that its Investment is being treated in accordance with the rules.<sup>40</sup> Canada has not provided an adequate explanation for the decline in EB quota.
68. In summary, British Columbia's share of the fee-free quota has been reduced while at the same time Quebec's share has inexplicably increased. On account of the special bonus rules, this inequitable treatment has been compounded to the detriment of the Investment and other producers operating in British Columbia.

<sup>40</sup> A copy of this correspondence can be found in Schedule 19.

*Export Performance of the Non-listed Provinces*

69. During the same period in which British Columbia producers and the Investment have experienced significant erosion in their allocation of EB quota, softwood lumber producers in Non-listed Provinces have been dramatically increasing their fee-free exports to the United States of America.
70. As indicated in the graph below, softwood lumber exports to the United States of America from producers in Non-listed Provinces have increased by almost 100% -- from 958 million board feet in 1994 to 1.892 billion board feet in 1997.<sup>41</sup>
71. The available 1998 figures indicate that softwood lumber exports from the Non-listed Provinces are continuing to grow at this rate.



<sup>41</sup> QSM No. 7, Table 2, a copy of which is included as Schedule 15 to this claim.

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*NAFTA Obligations Breached*

72. The Investor alleges that Canada has acted in a manner inconsistent with at least the following five provisions of the NAFTA Investment Chapter through the promulgation of the measures described in the paragraphs above:

- (a) National Treatment;
- (b) Most Favoured Nation Treatment; *withdrawn by Investor*
- (c) Minimum Standards of Treatment;
- (d) Performance Requirements; and
- (e) Expropriation.

As a result of Canada's actions, the Investor and its Investments have suffered economic harm.

**National Treatment**

73. NAFTA Article 1102 sets out the NAFTA's national treatment obligation for investment. Under Article 1102(2) the investments of investors of other NAFTA Parties must be given the best in-jurisdiction treatment with respect to the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of investments in like circumstances to the investments of Canadian investors.

74. NAFTA Article 1102(3) requires a Canadian province to provide the best treatment accorded, in like circumstances, by that province to investors and investments of investors of other NAFTA Parties. By comparison, Paragraphs (1) and (2) of NAFTA Article 1102 oblige Canada to provide the best treatment, in like circumstances, accorded by Canada anywhere in Canada to investors and investments of other NAFTA parties.

75. Canada's national treatment obligation requires it to provide to the Investor, and its Investment, the best treatment that it accords to other softwood lumber producers in Canada with respect to the Export Control Regime. Canada has failed to maintain this obligation with respect to the export fees imposed on the export of softwood lumber from the Listed Provinces and with respect to the allocation of the duty-free softwood lumber quota.

76. Canada's addition of softwood lumber in the Export Control Regime harms the Investor and its Investments in Canada contrary to Article 1102. The best treatment available in

Canada is provided to Canadian softwood lumber producers operating in Non-listed Provinces who may export an unlimited amount of export fee-free softwood lumber to the United States. By failing to provide export fee-free treatment to investments of investors of other NAFTA Parties, Canada has failed to meet its national treatment obligation contained in Article 1102.

77. Canada has also failed to extend national treatment in its allocation of fee-free quota to the Investment. Investments of Canadian investors operating in Listed Provinces other than British Columbia have received, and continue to receive, better treatment than the Investor receives for its Investment within the Province of British Columbia.

#### Most Favoured Nation Treatment

*withdrawn by Investor*

78. NAFTA Article 1103 sets out the NAFTA's most-favoured nation treatment obligation for investment. Under this article, the investments of investors of NAFTA Parties must be given the best in-jurisdiction treatment in like circumstances to the investments of investors from non-NAFTA Parties. The Investor reserves its right to make a Claim under Article 1103 should the evidence indicate that this obligation has been breached in respect of any investments of investors of non-NAFTA parties exporting softwood lumber from Canada to the United States.
79. Canada's addition of softwood lumber to the Export Control Regime could constitute discrimination against NAFTA Party investors and their investments in Canada contrary to Article 1103. The best treatment available in Canada is provided to softwood lumber producers operating in Non-listed Provinces who export an unlimited amount of export fee-free softwood lumber to the United States. By failing to provide to the Investment the export fee-free treatment available to investments of investors of non-NAFTA Parties in the Non-listed Provinces, Canada could fail to meet its most-favoured nation treatment obligation contained in Article 1103.

#### Minimum Standard of Treatment

80. NAFTA Article 1105 sets out the obligation for Canada to treat the investment of an investor in accordance with international law, including fair and equitable treatment. Article 1105 imports into the NAFTA the international law requirements of basic due process, economic rights, obligations of good faith and natural justice.
81. Canada's measures affecting the operations of investments of investors from other NAFTA Parties were applied in a secretive, unfair and inequitable manner. In the annual

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allocation of the duty-free softwood lumber export quota, Canada has failed to accord to the Investor the treatment in accordance with international law in violation of NAFTA Article 1105.

82. Canada has breached its obligations to meet international minimum standards as set out in NAFTA Article 1105 by, among other things:
- (a) failing to permit the Investor and its Investment to have a fair hearing respecting the allocation of its quota;
  - (b) failing to inform the Investor and its Investment of the process governing the allocation of annual quota;
  - (c) failing to provide adequate reasons to the Investor and its Investment respecting the allocation of its annual quota; and
  - (d) failing to provide any review procedure regarding the allocation of annual quota.

#### Performance Requirements

83. NAFTA Article 1106 prohibits a number of specified governmental activities collectively referred to as performance requirements. Under Article 1106(1), a Party may not impose or enforce certain requirements, commitments or undertakings in connection with the establishment, acquisition, expansion, management, conduct or operation of an investment of an investor in its territory. Under Article 1106(3), a Party may not condition the receipt, or continued receipt, of an advantage in connection with an investment on compliance with certain performance requirements.
84. Pursuant to NAFTA 1106, a NAFTA Party may not:
- (a) require investments to export a given level of goods from its territory (Article 1106 (1)(a)).
  - (b) require an investment to restrict sales of goods it produces in its territory by relating such sales in any way to the volume of its exports (Article 1106 (1)(e)).
  - (c) condition the receipt of an advantage on compliance with restrictions on the sales of an investment's goods in its territory by relating such sales in any way to the volume of its exports (Article 1106 (3)(d)).

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85. Canada's Export Control Regime for softwood lumber products requires the Investment to export a certain amount of softwood lumber at the EB and LFB levels each year or face a reduction of its EB or LFB quotas in future years. The Regime also requires the Investment to restrict its sales of lumber bound for the United States by relating such sales to the volume of exports at which no permit fee will be charged.
86. The Export Control Regime regulates the initial and continuing receipt of the advantage of being allowed to export at EB or LFB rates. Canada has related sales by the Investment of its products to customers from the United States to its volume of exports by restricting sales above a certain level and by imposing a punitive export permit fee.
87. Canada's imposition of the Export Control Regime results in a preference for Canadian softwood lumber operations operating outside of the Listed Provinces. As a result of the imposition of the Export Control Regime, the consumption of softwood lumber exported to the United States outside of the Listed Provinces has substantially increased.

### Expropriation

88. A fundamental obligation contained in the NAFTA Investment Chapter relates to compensating investors who have had an investment expropriated by a government measure. NAFTA Article 1110, which sets out this obligation, reads:

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.

2. Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place ("date of expropriation"), and shall not reflect any change in value occurring because the intended expropriation had become known earlier. Valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.

3. Compensation shall be paid without delay and be fully realizable.
  4. If payment is made in a G7 currency, compensation shall include interest at a commercially reasonable rate for that currency from the date of expropriation until the date of actual payment.
  5. If a Party elects to pay in a currency other than a G7 currency, the amount paid on the date of payment, if converted into a G7 currency at the market rate of exchange prevailing on that date, shall be no less than if the amount of compensation owed on the date of expropriation had been converted into that G7 currency at the market rate of exchange prevailing on that date, and interest had accrued at a commercially reasonable rate for that G7 currency from the date of expropriation until the date of payment.
  6. On payment, compensation shall be freely transferable as provided in Article 1109.
  7. This Article does not apply to the issuance of compulsory licenses granted in relation to intellectual property rights, or to the revocation, limitation or creation of intellectual property rights, to the extent that such issuance, revocation, limitation or creation is consistent with Chapter Seventeen (Intellectual Property).
  8. For purposes of this Article and for greater certainty, a non-discriminatory measure of general application shall not be considered a measure tantamount to an expropriation of a debt security or loan covered by this Chapter solely on the ground that the measure imposes costs on the debtor that cause it to default on the debt.
39. Under international law, expropriation refers to the act by which governmental authority is used to deny some benefit of property to an investor. This denial can be actual or constructive. The NAFTA does not define the term expropriation other than to make clear that it includes expropriations, nationalisations and measures tantamount to nationalisation and expropriation. The definition of expropriation under the NAFTA extends to direct and indirect measures.
40. There are many examples where the term "expropriation" has been used to deal with indirect takings. This term also applies to government action that harms or delays the effective enjoyment of an investment. Comment (g) of §712 of the American Law Institute's *Restatement (Third) of the Foreign Relations Law of the United States* (1986) states that restrictions on the taking by a state of the property of a national of another state apply:

*... not only to avowed expropriations in which the government formally takes title to property, but also to other actions of the government that have the effect of "taking" the property, in whole or in large part, outright or in stages ("creeping expropriation"). A state is responsible as for an expropriation of property under Subsection (1) when it subjects alien property to taxation.*

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*regulation, or other action that is confiscatory, or that prevents, unreasonably interferes with, or unduly delays, effective enjoyment of an alien's property or its removal from the state's territory.*

91. International law and the NAFTA both impose standards on the treatment to those whose property has been expropriated. Article 1110 of the NAFTA does not prevent expropriatory actions by governments from taking place, but requires that governments compensate investors for interferences with their property rights as set out in the NAFTA.
92. Article 1139 of the NAFTA contains a broad definition of the property interests that are protected as "investments" by NAFTA's expropriation obligation. This definition reads as follows:

#### Article 1139: Definitions

For purposes of this Chapter:

investment means:

- (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;

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):

93. Canada's Export Control Regime has deprived the Investment of its ordinary ability to alienate its product to its traditional and natural market. This deprivation has resulted in harm to the Investment and to the Investor.
94. The initial date of expropriation was April 1, 1996, and each time Canada reduced the Investment's allocation of fee-free quota, a further expropriation occurred.
95. Canada has acted in a manner inconsistent with its NAFTA Article 1110 obligations through the following:
  - (a) depriving the Investor of its ability to carry out its otherwise legal business operations on a discriminatory basis and not in accordance with the due process of law and NAFTA Article 1105(1); and

Statement of Claim of Pope & Tulbot  
March 25, 1999

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- (b) failing to provide compensation to the Investor in the fashion and on the basis set out in NAFTA Article 1110

*Economic Harm to the Investor and the Investment*

96. As a result of the implementation of Canada's Export Control Regime in a manner inconsistent with Section A of NAFTA Chapter 11, the Investor and the Investment have suffered economic harm through interference with the operations of the company.
97. The Investment advised Canada that it was "unhappy" with its allotted EB quota and that it objected to the erosion of its traditional markets.<sup>42</sup> The erosion of the Investment's fee-free EB quota from 1996 to 1998 was [REDACTED]. This erosion cost the Investment approximately CAD\$ [REDACTED] per year in additional export fee payments.
98. In response to the implementation of Canada's Export Control Regime, the Investment has undertaken numerous mill shutdowns rather than be forced to pay quota fees. For example, the Midway mill experienced a two-week shutdown in October 1997. Castlegar had a five-day shutdown in the third quarter of 1998. The Investment's Canadian mills had five days of down-time in the second quarter of 1998 and seven more days in the fourth quarter of 1998.
99. In addition, the Investment has been forced to adjust its product mix and has ceased selling previously profitable products. [REDACTED]
100. A further effect of the Export Control Regime is the creation of an artificially low Canadian softwood lumber "discount" market price. The effect of the Export Control Regime is to artificially distort the Canadian market for softwood lumber. The quarterly set quota allowance forces Canadian producers to make a number of decisions after their quarterly fee-free EB quota has been exhausted. For example, a producer must decide whether to export at the LFB or UFB fee levels, to seek and develop alternative markets or products, or to simply shutdown mills until they are able to obtain fee-free exports in the next quarter. A similar harmful effect has occurred on sales made by the Investment to Australia.

<sup>42</sup> A copy of which is included in Schedule 17 of this Claim.

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101. The main alternative market for the Investment is the Canadian domestic market. Canadian purchasers recognize that softwood exporters, such as the Investment, would rather sell to Canadian customers at a discounted price than export and pay the export fees, thus incurring further losses. As a result, Canadian softwood lumber purchasers are able to negotiate significant discounts on their purchases of Canadian softwood lumber from Canadian producers.
102. In response to the effects of the Export Control Regime on the softwood lumber market, the Investor and the Investment have attempted to develop non-US markets, alternative products and improve mill efficiency. [REDACTED]
103. In addition, due to a number of economic factors including the implementation of the Export Control Regime, the market for wood chips has been adversely affected in British Columbia. Wood chip fibre from softwood lumber mills is one of the primary sources of fibre material used in the pulp and paper manufacturing process. The decreasing supply of wood chips due to lost production on the British Columbia coast has resulted in economic loss for the Investor's Investment in Harmac Pacific Inc., which must purchase increasingly expensive wood chips for its pulp and paper operation.
104. The effect of Canada's Export Control Regime has been to decrease the value of the Investor's investments in Canada.

C. THE POINT AT ISSUE

105. There is one basic point at issue: Has Canada taken measures inconsistent with its obligations under Section A of Chapter 11 of the NAFTA? If the answer to this question is yes, what is the quantum of compensation to be paid to the Investor as a result of the inconsistency of Canada with its obligations arising under Chapter 11 of the NAFTA?

**D. RELIEF SOUGHT AND APPROXIMATE DAMAGES CLAIMED**

The Investor claims the following:

i. Damages as compensation caused by or arising out of Canada's measures that are inconsistent with its obligations contained in Part A of Chapter 11 of the NAFTA for not less than the following:

(a)	Minimum Standard of Treatment	US\$ 50,578,700
(b)	National Treatment	US\$ 125,657,900
(c)	Most Favoured Nation Treatment	US\$ 125,657,900
(d)	Performance Requirements	US\$ 125,657,900
(e)	Expropriation	US\$ 80,000,000

Withdrawn  
by  
Investor

ii. Costs associated with these proceedings, including all professional fees and disbursements.

iii. Fees and expenses incurred to oppose the effect of the *Softwood Lumber Agreement* and those changes to Canadian domestic law made pursuant to that Agreement.

iv. Pre-award and post-award interest at a rate to be fixed by the Tribunal.

v. Tax consequences of the award to maintain the integrity of the award.

vi. An Interim Order providing interim measures of protection pursuant to NAFTA Article 1134 to preserve the rights of the Investor and to provide that the Investment's annual softwood lumber allocation from Canada not be decreased pending a final award of the Tribunal.

vii. Such further relief that counsel may advise and that this Tribunal may deem appropriate.

DATE OF ISSUE: MARCH 25, 1999

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*New York Toronto*

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THE NORTH AMERICAN FREE TRADE AGREEMENT

CHAPTER ELEVEN

BETWEEN:

POPE & TALBOT, INC.

Claimant / Investor

- AND -

GOVERNMENT OF CANADA

Respondent / Party

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STATEMENT OF CLAIM  
SCHEDULE OF DOCUMENTS

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March 25, 1999

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**APPLETON & ASSOCIATES**

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INTERNATIONAL LAWYERS

*New York Toronto***INDEX OF SCHEDULES**

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