Public Version

INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

Koch Industries, Inc. and Koch Supply & Trading, LP

v.

Government of Canada

(ICSID Case No. ARB/20/52)

GOVERNMENT OF CANADA

REJOINDER MEMORIAL ON JURISDICTION AND THE MERITS

September 30, 2022

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I. INTRODUCTION

1. The Claimants play by their own rules. They planned to avoid regulatory disclosure obligations in California by purchasing emission allowances in Ontario and then systematically exporting allowances back to California. They expected Ontario to modify its approach to winding down the cap and trade program to suit their specific circumstances. Now, they expect this NAFTA Tribunal to award compensation, *even if* it finds (as it should) that the Claimants have not established the Tribunal's jurisdiction. The Claimants' NAFTA gambit fails at every step.

2. In late 2016, Kansas-based Koch Supply & Trading, L.P. (**KS&T**) registered in the Ontario cap and trade program as a market participant. The cap and trade program set an aggregate cap on the volume of greenhouse gases that certain large polluters could emit. Ontario created emission allowances – each representing a unit of the overall cap – and then distributed the allowances within the cap and trade program. Polluters would be required to secure and submit to regulators sufficient allowances to cover their actual emission of greenhouse gas.

3. KS&T was not itself a polluter and was not required to register in Ontario or participate in the system there. It pursued [redacted][1] California and Ontario had designed their systems to be able to harmonize, or link, which would allow participants to transfer emission allowances cross-border. If California decided to allow transfers from the Ontario system to the parallel California cap and trade system, [redacted][2] It would be able to "buy [emission allowances] wholesale in Ontario, sell retail in California".[3]

4. On May 15, 2018, KS&T bought emission allowances at auction within the Ontario cap and trade program. A provincial election campaign was underway in Ontario, and the party leading in the polls had promised to swiftly cancel the program. Given the political situation, KS&T was [redacted] of participating in the May 15 auction through its Ontario registry

[1] [redacted]

[2] [redacted]

[3] **CWS-6**, Reply Witness Statement of Frank King, 17 July 2022 ("King – Reply Witness Statement"), ¶ 21.

[4] [redacted]

account, but did so anyway. It knew that [redacted][6]

5. On June 7, 2018, as expected, the Progressive Conservative Party of Ontario (**PC Party**) won a majority of seats in the Ontario Legislature, and the swearing-in ceremony was set for June 29, 2018. The Ontario civil service mobilized to work with the transition team of the incoming government to ensure a smooth transition of power.

6. On June 11, 2018, the linked jurisdictions (including Ontario) transferred emission allowances to winning bidders' registry accounts. KS&T had planned, as with previous auctions, to move emission allowances it acquired to California "immediately".[7] [redacted]

7. [redacted] As with all prior auctions, the decision was made by a civil servant exercising delegated Ministerial authority. The incoming government had promised to cancel cap and trade as a priority; declining to set an auction date would avoid committing the new administration to selling additional emission allowances in the first months of its term.

8. After the close of business on June 15, 2018, California blocked transfers of emission allowances to and from Ontario CITSS accounts. On June 18, 2018, KS&T again attempted to move allowances to California, but the transfer was blocked because the California system no longer accepted transfers from Ontario. [redacted]

[5] [redacted]

[6] [redacted]

[7] **R-089**, Ontario Cap Trade Program - July 2018 GM changes.pdf, 31 July 2018, p. 1.

[8] [redacted]

[redacted][9]

9. On June 29, 2018, the new government took office in Ontario. As promised, it moved quickly to wind down the cap and trade program, including establishing a compensation regime based on whether or not an entity had bought emission allowances to cover its actual emissions of greenhouse gases. KS&T, as a market participant without emissions or compliance obligations, would be ineligible for compensation.

10. KS&T and affiliated Koch companies launched a lobbying campaign targeting high-level officials in the Ontario government, seeking to modify the rules in its favour. In public comments, Koch argued that although KS&T had registered as a "market participant", it was in fact acting on behalf of its affiliate companies and should be treated as a compliance entity.[10] Koch advocated for a separate sub-category of compensation for "specific market participants" – one in particular, KS&T. However, Ontario was not willing to change the rules of its principled compensation approach simply to suit KS&T.

11. Unwilling to accept the rules, the Claimants have now turned to NAFTA to air their grievances.[11]

12. In **Part III**, Canada explains that the Claimants have not discharged their burden to establish the jurisdiction of this Tribunal (**A**). They have not established that the dispute "arises directly out of an investment" under Article 25 of the ICSID Convention, (**B**) nor have they established that they had "investments" protected under NAFTA Chapter Eleven. Emission allowances were not "property" under Ontario law and therefore do not qualify as an investment under NAFTA Article 1139(g) (**C.1**). Neither the emission allowances nor KS&T's cross-border trading activity constituted

[9] [redacted]

[10] **RS-086**, Environmental Registry of Ontario, "Comment on Bill 4, Cap and Trade Cancellation Act", Comment ID 10437, 11 October 2018 ("Koch Comment on Bill 4") (also indicating that it was in favour of cancellation of the program overall given that "Koch does not support the concept of cap and trade").

[11] Canada takes note of the Claimants' statements directed personally at Canada's legal team in this arbitration (Claimants' Reply, ¶ 189). These statements are uncivil and have no place in NAFTA Chapter Eleven proceedings.

"interests arising from the commitment of capital" within the meaning of NAFTA Article 1139(h) (**C.2**). For its part, Koch Industries, Inc. (**Koch Industries**) was not even registered in the Ontario cap and trade program, and the Claimants have neither established that it held any investments relevant to the Tribunal's jurisdiction, nor alleged any damage that would be recoverable by Koch Industries (**D**). Finally, the Claimants continue to insist that a press release by a government-in-waiting amounted to a "measure" that "cancelled" the cap and trade program on June 15, 2018. That is both factually and legally incorrect: the only "measure" that was "adopted or maintained" on June 15, 2018 was Ontario's decision to decline to issue an auction notice (**E**).

13. In **Part IV.A**, Canada shows that the Claimants have not established a violation of the minimum standard of treatment under NAFTA Article 1105. The new Ontario government had a legitimate policy rationale for cancelling the cap and trade program – they believed, as did the Ontario Auditor-General at the time, that cap and trade was too costly for Ontarians. Ontario's decision to shift policies with respect to climate change falls far short of the "egregious" misconduct required to show a violation of the minimum standard of treatment under international law. The Claimants' main complaint is that KS&T did not receive compensation, but Ontario's decision with respect to eligibility for compensation was based on the purpose of the cap and trade program itself. There was nothing arbitrary, let alone manifestly arbitrary or discriminatory, about that decision.

14. In **Part IV.B**, Canada explains that the Claimants' arguments regarding expropriation under NAFTA Article 1110 are largely repetitive of their Memorial, and contain the same incoherence. Their "primary case" that Ontario indirectly expropriated KS&T's emission allowances and business on June 15, 2018 fails because KS&T did not have an investment in Ontario capable of expropriation. What is more, nothing Ontario did on June 15 substantially deprived the Claimants of their alleged investments; and its measures in winding down the cap and trade program were a valid exercise of police powers. The Claimants' alternative case of direct expropriation fails because Ontario received no benefit from the freezing of KS&T's Ontario CITSS account.

15. Finally, in **Part V**, Canada demonstrates that even if the Claimants were to establish both jurisdiction and a breach of the NAFTA, the Claimants have not proven that Ontario caused the damages they seek to recover. Even then, the Claimants would not be entitled to the full amount of damages they claim because their own negligence contributed to their alleged loss.

16. Along with its Rejoinder, Canada submits second witness statements of **Mr. Alexander Wood**, Assistant Deputy Minister of the Climate Change and Resiliency Division at the Ontario Ministry of Environment, Conservation, and Parks (**MECP**),[12] and **Ms. Nadia Ramlal**, Senior Manager Program Services and Oversight at the Financial Instruments Branch of that Division and Ministry.[13] Canada also submits second expert reports of **Professor Larissa Katz**, a leading authority on property rights under Ontario law,[14] and **Mr. Franz Litz**, an architect of the cap and trade model on which Ontario's was based.[15]

II. FACTS

A. The Claimants' Portrayal of the Ontario Cap and Trade Program Is Contradicted by the Evidence

1. Ontario's Program Was a Regulatory Regime Designed to Reduce Greenhouse Gas Emissions

17. In their Reply, the Claimants distort the nature of the regulatory regime in which KS&T participated by portraying one part – trading in emission allowances – as central, while ignoring the broader environmental purpose and functioning of the system.

18. As explained in Canada's Counter-Memorial, cap and trade programs function by setting an annual aggregate cap on emissions.[16] To implement the emissions cap, the government creates and distributes "emission allowances" – one allowance for each tonne of emissions "allowed" by the emissions cap.[17] Polluters that are covered by the system must measure, monitor and report their emissions and, at the end of a compliance period, remit allowances equal to their actual emissions.[18]

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[12] **RWS-3**, Second Witness Statement of Alexander Wood, 29 September 2022 ("Wood – Second Witness Statement").

[13] **RWS-4**, Second Witness Statement of Nadia Ramlal, 27 September 2022 ("Ramlal – Second Witness Statement").

[14] **RER-3**, Second Expert Report of Prof. Larissa Katz, 28 September 2022 ("Katz – Second Expert Report").

[15] **RER-4**, Second Expert Report of Franz Litz, 26 September 2022 ("Litz – Second Expert Report").

[16] Canada's Counter-Memorial on Jurisdiction and Merits, 17 February 2022 ("Canada's Counter-Memorial"), ¶¶ 20-21.

[17] **RER-2**, First Expert Report of Franz Litz, 15 February 2022 ("**RER-2**, Litz – First Expert Report"), ¶ 32.

[18] **R-006**, *Climate Change Mitigation and Low-carbon Economy Act*, 2016, S.O. 2016, c. 7 ("*Climate Change Act*"), ss. 9-14, **R-007**, *The Cap and Trade Program*, O. Reg. 144/16, 2016 ("Regulation 144/16"), Part III. S*ee also* **RER-4**, Litz – Second Expert Report, ¶ 5; Canada's Counter-Memorial, ¶ 28.

Emission allowances are a regulatory tool created to serve the specific and limited function of achieving the emissions reduction goal.[19]

19. Ontario's cap and trade program was created under the *Climate Change Mitigation and Low-carbon Economy Act, 2016* (***Climate Change Act*** or ***Act***). The Preamble of the legislation signals the program will "establish a broad carbon price through a cap and trade program that will change the behaviour of everyone across the Province, including spurring low-carbon innovation."[20] The regulatory purpose was clear: to "encourage Ontarians to change their behavior by influencing their economic decisions that directly or indirectly contribute to the emission of greenhouse gas."[21]

20. The "trade" in "cap and trade" refers to a market mechanism that existed in furtherance of the ultimate environmental goal of reducing greenhouse gas emissions. As cap and trade expert Mr. Litz notes in his second report: "[t]he purpose is not to create a new commodity market for allowances."[22] The design features of the program – including its restrictive rules on trading in emission allowances – exist in order to reduce emissions and facilitate compliance.

21. The *Climate Change Act* empowered the Ontario Minister of Environment, Conservation and Parks (**MECP**)[23] to create emission allowances.[24] Each emission allowance was "equivalent to one tonne of CO_2e"[25] – a unit, or fraction, of the total tonnage of greenhouse gas pollution permitted with

[19] **RER-4**, Litz – Second Expert Report, ¶ 6 ("Emission allowances are thus a regulatory tool meant to serve the specific and limited function of achieving the emissions reduction goal with flexibility.")

[20] **R-006**, *Climate Change Act*, Preamble.

[21] **R-006**, *Climate Change Act*, s. 2(2).

[22] **RER-4**, Litz – Second Expert Report, ¶ 9. Prior to this arbitration, KS&T too recognized that markets created by cap and trade systems are fundamentally different. In a publication indicating skepticism about climate change, KS&T's Executive Vice President stated: "So it's essentially a compliance market that wouldn't exist if not for government. But a second-order effect of that is government can always change the rules." *See* **R-090**, Koch Companies Quarterly Newsletter, 'Blowing Smoke", January 2010, p. 10.

[23] At the time, the Ministry was called the Ministry of the Environment and Climate Change, or MOECC.

[24] **R-006**, *Climate Change Act*, s. 30.

[25] **R-007**, Regulation 144/16, s. 10. Ontario's definition of emission allowances is consistent with WCI systems design, in which emission allowances were described as a "limited authorization to emit" one tonne of CO2e. **C-015**, WCI, Design for the WCI Regional Program, 2010, § 2.3 at p. DD-3, 4.4.6. In keeping with their nature as compliance instruments representing parts of an aggregate cap, the WCI stated that: "[e]mission allowances are not considered property rights but are a limited authorization to emit."

respect to a given year.[26] An emission allowance represented one unit of the Province's annual aggregate cap on greenhouse gas emissions.[27]

22. The function of emission allowances as compliance instruments is clear from the regulatory framework. Only registered participants were able to hold emission allowances.[28] Further, interests in emission allowances were not divisible: only one registered participant could "hold" and remit particular units of the overall cap.[29] The *Climate Change Act* went one step further still, prohibiting a participant from holding emission allowances indirectly on behalf of another entity.[30] The legislature also specified that there was no right to compensation with respect to governmental actions taken under the *Act*.[31]

2. The Evidence Confirms that Market Participants Played a Limited Role in the Ontario Cap and Trade Program

23. The *Climate Change Act* and its regulations mandated that certain large polluters participate in the cap and trade program. At the end of a compliance period, these compliance entities would be required to remit emission allowances in an amount equal to their emissions.[32] The Ontario program also allowed for the participation of entities that were not compelled to participate – "market participants"[33] like KS&T.

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[26] **R-006**, *Climate Change Act*, s. 30. "Emission allowance" was defined as an "Ontario emission allowance or an instrument created by a jurisdiction other than Ontario that, under section 38, is to be treated as an emission allowance for the purposes of this act; "quota d'emission". For its part, "Ontario emission allowance" was defined as "an emission allowance created under section 30; "quota d'émission de l'Ontario". **R-006**, *Climate Change Act*, s. 1(1). The *Climate Change Act*'s equally authoritative French definition of "emission allowance", "*quota d'émission*" supports the fact that each emission allowance was a unit of the cap. The French translation of "quota" is defined as "part" or "quota" in English. *See* **R-091**, Larousse Dictionary, translation of "quota", accessed 8 August 2022.

[27] **R-005**, WCI Design Recommendation for the WCI Regional Cap-and-Trade Program, 23 September 2008, p. 48. *See* also p. 37 ("Emission allowances from other cap-and-trade systems are regulatory instruments used to limit GHG emissions. These emission allowances are issued by appropriate government regulatory authorities and are used for compliance purposes.")

[28] **R-006**, *Climate Change Act*, s. 21.

[29] **R-006**, *Climate Change Act*, s. 28(2).

[30] **R-006**, *Climate Change Act*, s. 28(2).

[31] **R-006**, *Climate Change Act*, s. 70(1).

[32] *See* Canada's Counter-Memorial, ¶¶ 26-27.

[33] A market participant was a participant without compliance obligations that could voluntarily apply to register in the program, participate in auctions, and trade in allowances. *See* Canada's Counter-Memorial, ¶ 36. Also, as Mr. Litz noted

24. In its Counter-Memorial, Canada explained that program participants could purchase emission allowances at highly regulated auctions held four times per year.[34] These auctions were the "primary market" for emission allowances. A "secondary market" also existed, which allowed for the reallocation of emission allowances as needed between compliance entities.[35] In their Reply, the Claimants continue to distort the role of the secondary market and to exaggerate the role of market participants. The evidence is definitive: far from being essential, market participants played little to no role in the Ontario program.[36]

25. The Claimants argue that market participants were "important" and "key" because they provided efficient price discovery, market liquidity, and trading opportunities without high transaction costs.[37] However, auctions – not market participants – provided those benefits.[38] As Mr. Litz explained in his first report, in systems like Ontario's auctions "play a fundamental role in price discovery, liquidity, and the efficient, low – cost distribution of allowances to covered pollution sources that need them for compliance."[39] The Claimants incorrectly attribute the fundamental role that auctions play to market participants.

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in his first report, these entities without compliance obligations were called "voluntary associated entities" in California and "participants" in Québec. *See* **RER-2**, Litz – First Expert Report, ¶ 43. For ease of reference, Canada refers to all entities in these categories as "market participants".

[34] Canada's Counter-Memorial, ¶¶ 30-31. *See also* **R-007**, Regulation 144/16, ss. 55-57. In order to facilitate the transition to the cap and trade program, during the first compliance period Ontario distributed a significant proportion of emission allowances to compliance entities for free. *See* **R-007**, Regulation 144/16, ss. 85-90; **RS-006**, Environmental Commissioner of Ontario, "Introduction to Cap and Trade in Ontario," Appendix A to the ECO's Greenhouse Gas Progress Report 2016, November 2016 ("ECO Greenhouse Gas Report"), p. 18 and Table 4.

[35] The "secondary market" was the term used to refer to transactions that occur between registered participants after emission allowances had been auctioned or otherwise initially distributed by the government. *See* Canada's Counter-Memorial, ¶ 32; and **RER-2**, Litz – First Expert Report, ¶ 72.

[36] The Claimants insist that they were "specifically invited and encouraged through Ontario's legislative program to participate in the cap and trade program". *See* Claimants' Reply, ¶ 44. However, they have provided no evidence of such invitation or encouragement. No such evidence exists. As Canada explained in its Counter-Memorial, Ontario published general information and guidance documents on its website and the MECP Help Desk sent correspondence to all cap and trade stakeholders. *See* Canada's Counter-Memorial, ¶ 121; exhibits **C-030** through **C-035**. Given both the limited role of the secondary market and the existence of market participants on the margins of the primary and secondary markets, it would have been strange if Ontario had specifically induced their participation.

[37] Claimants' Reply Memorial on Jurisdiction and Merits, 18 July 2022 ("Claimants' Reply"), ¶¶ 37, 39, 42.

[38] **RER-2**, Litz – First Expert Report, ¶ 87.

[39] **RER-2**, Litz – First Expert Report, ¶ 69.

26. In the Ontario program, auctions took place four times a year and provided a ready, transparent source of emission allowances. Compliance entities bought the vast majority of emission allowances sold at auction. In Ontario auctions in 2017 and 2018, compliance entities bought between 91.5% and 99.1% of emission allowances sold.[40] Auctions provided efficient price discovery and market liquidity with low transaction costs.[41]

27. As for trading opportunities, these were available to compliance entities in the secondary market – without the intervention (or additional transaction costs) of third parties such as KS&T. If a compliance entity had under – or over – purchased at auction, they could acquire or sell emission allowances to other compliance entities on the secondary market.[42] [redacted]

28. The Claimants also argue that market participants reduced transaction costs for compliance entities and improved market performance overall.[44] This is nonsensical. Market participants such as KS&T increased transaction costs and introduced uncertainty in the system. Concerns about market

[40] **C-056**, Ontario Government, Summary Results Report: Ontario Cap and Trade Program Auction of Greenhouse Gas Allowances March 2017 Ontario Auction #1, 22 March 2017, p. 2 (capped participants purchased 99.1% and 100%, respectively). *See also* **C-061**, Ontario Government, Summary Results Report: Ontario Cap and Trade Program Auction of Greenhouse Gas Allowances June 2017 Ontario Auction #2, p. 2 (capped participants purchased 96.1% and 92.8%, respectively); **C-066**, Ontario Government, Summary Results Report: Ontario Cap and Trade Program Auction of Greenhouse Gas Allowances September 2017 Ontario Auction #3, p. 2 (capped participants purchased 96.4% and 96.1%, respectively); **C-069**, Ontario Government, Summary Results Report: Ontario Cap and Trade Program Auction of Greenhouse Gas Allowances November 2017 Ontario Auction #4, p. 2 (capped participants purchased 91.5% and 92.9%, respectively).

[41] The Claimants' statement that "[b]arring access to alternative sources in the secondary market, such entities would need to halt economic production once they had exhausted their initial allocation of allowances" is absurd. *See* Claimants' Reply, ¶ 32. Compliance entities were in control, via auctions, of obtaining emission allowances they required for compliance.

[42] **RER-4**, Litz – Second Expert Report, ¶ 22.

[43] [redacted]

[44] Claimants' Reply, ¶ 37.

manipulation and allowance hoarding by market participants were at the core of the decision to limit the purchasing ability of market participants,[45] as the Claimants were well aware.[46]

3. The Claimants Misidentify the Governing Legal Framework

29. In their Reply, the Claimants advance an incorrect understanding of the "legal framework" that governed Ontario's cap and trade program.[47] The Claimants assert that KS&T "participated in the market in trading Ontario allowances"[48] based on the "legal framework" of the non-binding agreement signed by the Government of California, the Government of Ontario, and the Gouvrnement du Québec in September 2017 (**Harmonization Agreement**). However, it was the *Climate Change Act*, not the Harmonization Agreement that established the legal framework for Ontario's cap and trade program.

30. As Canada explained in its Counter-Memorial, Ontario harmonized its cap and trade program with parallel programs in California and Québec starting in 2018. The three jurisdictions signed the

[45] **FL-13**, Western Climate Initiative, "Market Oversight Draft Recommendations", 1 April 2010, p. 24. Canada notes that the Claimants criticize Canada for a "selective reading" of the WCI Design Documents, and argue that Canada's explanations and Mr. Litz's firsthand recollections are not credible because ultimately market participants were allowed. *See* **CER-2**, Second Expert Report of Dr. Robert Stavins, 18 July 2022 ("Stavins – Second Expert Report"), ¶ 12. This is a straw man argument: the fact that market participants are allowed in the WCI design is not contested. As Mr. Litz stated in his first report and reiterates in his second, market participants were allowed, but "to place careful limits on participation by these entities and to make their participation as transparent as possible to allow for market oversight." *See* **RER-2**, Litz – First Expert Report, ¶ 82; **RER-4**, Litz – Second Expert Report, ¶¶ 25-33. Canada further notes that the Claimants exhibited only an excerpt of the WCI Design Recommendations with their Memorial, omitting over 100 pages of the document, including the page stating "Emission allowances are not considered property rights but are a limited authorization to emit." The Claimants are in no position to allege a "selective reading".

[46] *See* [redacted]

[47] Claimants' Reply, ¶ 65.

[48] Claimants' Reply, ¶ 64.

Harmonization Agreement to signal their intent to continue coordinating, while expressly guarding and reinforcing each jurisdiction's regulatory and participatory autonomy.[49]

31. The Ontario cap and trade program was governed entirely by the *Climate Change Act* and its regulations, both before and after harmonization with California and Québec. In Ontario, harmonization was effected through amendments to regulations that entered into force on January 1, 2018.[50] The amendments allowed for the recognition of "external accounts"[51] and for emission allowances created in other jurisdictions to satisfy compliance obligations in Ontario.[52] Regulatory amendments, not the Harmonization Agreement, "provided the basis for the mutual recognition" of each jurisdiction's compliance instruments.[53]

B. The Claimants Grossly Exaggerate KS&T's Business Activities in Ontario

32. The Claimants also overstate the extent of KS&T's business activities in Ontario. They continue to cast KS&T's limited involvement in Ontario's cap and trade program as a "business enterprise"[54] or an "emission trading business in Ontario".[55] They posit that KS&T's actions were

[49] The Harmonization Agreement specified that it "does not, will not and cannot be interpreted to restrict, limit or otherwise prevail over relevant national obligations of each Party, if applicable, and each Party's sovereign right and authority to adopt, maintain, modify, repeal or revoke any of their respective program regulations or enabling legislation". **R-025**, Ontario Newsroom, "Agreement on the Harmonization and Integration of Cap-and-Trade Programs for Reducing Greenhouse Gas Emissions between the Gouvernement du Québec, the Government of California and the Government of Ontario", 22 September 2017 ("Harmonization Agreement"), Preamble.

[50] *See* **R-013**, *The Cap and Trade Program Ontario Regulation*, O. Reg. 450/17 Amending O. Reg. 144/16 ("Regulation 450/17"), s. 46. The Harmonization Agreement itself provided that "the Parties recognize that the harmonization and integration of their greenhouse gas emissions reporting programs and their cap-and-trade programs *are to be attained by means of regulations adopted by each Party*" and that "this Agreement is intended to *facilitate continued consultation*, using and building on existing working relationships, during the implementation and the operation *of the Parties' respective programs* and supporting the development of any proposed program changes, including new offset protocols, and new program elements, with the objective of maintaining and developing harmonized and integrated approaches that may be considered by each Party." *See* **R-025**, Harmonization Agreement (emphasis added). *See also* Canada's Counter-Memorial, ¶ 55; [redacted]

[51] **R-013**, Regulation 450/17, s. 1(6).

[52] **R-013**, Regulation 450/17, s.7.

[53] Claimants' Reply, ¶ 92. Contrary to the Claimants' assertions, these amendments were not "implementing regulations" of the Harmonization Agreement. *See* Claimants' Reply, ¶ 64. Subnational entities cannot enter into treaties or create treaty obligations requiring implementation in domestic law.

[54] Claimants' Reply, ¶¶ 246, 652. *See also* Claimants' Reply, ¶¶ 67, 215, referring to "KS&T's enterprise activities".

[55] Claimants' Reply, ¶¶ 650, 652, 654-656. *See also* Claimants' Memorial, ¶ 2 and Claimants' Reply, ¶ 2, (referring to "KS&T's carbon allowance trading business in the Province"); Claimants' Memorial, ¶ 156, (referring to "KS&T's

"intrinsically linked to its ownership of an Ontario CITSS account into which it deposited and held and through which it traded in OCA allowances and related compliance instruments, as an Ontario-registered market participant",[56] and argue that that KS&T's "business in Ontario" was "part of a sustained, long-term business plan".[57] However, the Claimants' attempts to inflate their business activities in Ontario must be rejected. They have provided no contemporaneous documents evidencing either KS&T's alleged business plan or the existence of a business in Ontario at all.[58]

33. In reality, KS&T was a cross-border trader whose activities were based in the United States, and who, in their own words, [redacted] [9] At no time did it operate a business in Ontario. Canada fully explains in the sections that follow that KS&T: (1) participated in Ontario's cap and trade program from the United States; (2) established a "standard practice" to move the emission allowances it purchased in Ontario to California "immediately"; and (3) had limited involvement in the secondary market for Ontario emission allowances.

Ontario allowance trading business"); Claimants' Memorial, pp. iii and 145, subheading 5(D)(2) and ¶ 490, and Claimants' Reply, pp. iii and 227, subheading V(C) and ¶¶ 642, 649, 651, 653, (referring to "KS&T's Ontario emissions trading business"); Claimants' Memorial, ¶¶ 402, 409, 491, (referring to "KS&T's broader carbon trading business in Ontario"); Claimants' Reply, ¶¶ 4 (referring to "the Claimants' Ontario allowance trading business"), ¶ 534 (referring to the Claimants' "rights in a broader carbon trading business in Ontario"), ¶ 611 (referring to "their Ontario emission allowance trading business"), and ¶ 654 (referring to KS&T's "broader emission trading business enterprise in Ontario").

[56] Claimants' Reply, ¶ 63.

[57] Claimants' Memorial, ¶ 323(a); Claimants' Reply, ¶ 539. *See also* Claimants' Reply, ¶¶ 299, 302, 315 (emphasis added).

[58] [redacted]

[59] [redacted]

1. KS&T's Participation in Ontario's Cap and Trade Program Was Conducted from the United States, not Ontario

34. There is no dispute that KS&T is an enterprise "organized under the laws of the United States",[60] not Canada. It does not have a physical address, officers, directors, subsidiaries, personnel, infrastructure or equipment in Ontario.[61] Rather than dispute these facts, the Claimants argue that "having a physical presence or fixed place of business is irrelevant".[62] Far from being irrelevant, the absence of physical indicia indicates that KS&T did not have a business in Ontario, particularly when the Claimants allege that KS&T had a "commercial presence in the Province".[63]

35. Consistent with the absence of physical indicia, contemporaneous documentation establishes that KS&T viewed its "business in Ontario" as part of its U.S. business, and that their business activities were managed and executed from the United States. The evidence, summarized below, establishes five additional indicia that the Claimants did not have a "business in Ontario".[64]

36. First, KS&T has been registered in California's cap and trade program as a market participant, and has had a California CITSS account, since 2012.[65] KS&T viewed its registration as an Ontario market participant in 2016 as part of its already existing [redacted] for which KS&T [redacted]

[60] Claimants' Memorial, ¶¶ 301, 316.

[61] Canada's Counter-Memorial, ¶¶ 3, 119-120, 157 and fn. 302. When describing Koch's "global presence", the company's website made no mention of its "presence" in Ontario, and only listed locations in North America (Houston, Mexico, New York City, and Wichita), Europe (London, Geneva, and Rotterdam), and Asia and Middle East (Singapore and Shanghai). *See* **R-096**, Koch Supply & Trading, website screenshot as at 3 June 2017; **R-097**, Koch Supply & Trading, website screenshot as at 18 December 2018; **R-098**, Koch Supply & Trading, website screenshot as at 1 April 2018.

[62] Claimants' Reply, ¶¶ 371, 355.

[63] Claimants' Reply, ¶ 56.

[64] *See* **R-099**, California Air Resources Board, "Guidance for Registering as a Voluntary Associated Entity", June 2021, pp. 4-5 (providing indicators that a market participant in California is "located in the United States" for the purpose of the California Air Resources Board, including physical and mailing addresses, incorporation, location of directors and officers, and business numbers issued within the United States.)

[65] *See* Claimants' Memorial, ¶ 123; Canada's Counter-Memorial, ¶ 48.

[redacted] [7]

37. Second, the strategic decisions with respect to KS&T's registration as a market participant in Ontario's cap and trade program were made in the United States, not Ontario. KS&T's Vice President, Global Renewables, Mr. Graeme Martin, was responsible for "ensuring that KS&T could register as a market participant in Ontario."[68] He was based in the company's Houston, Texas office.[69] Among his strategic decisions with respect to registration in Ontario were the identification of KS&T's Primary Account Representative ("PAR") and Alternate Account Representative ("AAR").[70] His decisions provide indicia that KS&T's business was being run not from Ontario, but from Texas and Kansas:

- KS&T designated Mr. Sam Porter, based in Wichita, Kansas, as its AAR.[71] [redacted] [2] He worked closely with Mr. Martin

[66] [redacted]

[67] *See* **C-051**, KS&T, Ontario Business Relationship Disclosure Form, [redacted] **NR-12**, KS&T, Ontario Business Relationship Disclosure Form, [redacted] **NR-14**, KS&T, Ontario Business Relationship Disclosure Form, [redacted] **NR-16**, KS&T, Business Relationship Disclosure Form, [redacted] **NR-17**, KS&T, Business Relationship Disclosure Form, [redacted] **R-101**, State of Delaware, Corporate Registry Search – KS&T 3437877.

[68] **CWS-2**, Witness Statement of Graeme Martin, 4 October 2021 ("Martin – First Witness Statement"), ¶ 21.

[69] *See e.g.*, [redacted]

[70] Ontario law required each participant to appoint one PAR, who was required to be an Ontario resident, and at least one, but no more than four, AARs. A PAR or an AAR was authorized to act on behalf of the participant to perform any actions that the participant was required or permitted to take under the *Climate Change Act*. PARs and AARs were authorized, in accordance with the laws and regulations governing Ontario's cap and trade program, to bid in auctions and effect transfers in the CITSS. *See* **RWS-4**, Ramlal – Second Witness Statement, ¶¶ 26-28; **R-007**, Regulation 144/16, ss. 44, 46, 47.

[71] **NR-13**, KS&T Participant Registration Form, [redacted]

[72] [redacted] **RWS-2**, Witness Statement of Nadia Ramlal, 15 February 2022 ("Ramlal – First Witness Statement"), ¶ 41; **NR-13**, KS&T Participant Registration Form, 29 November 2016, s. 4.0.

in every aspect of KS&T's activity related to Ontario, [redacted] [3] Despite the nomenclature, the evidence establishes that Mr. Porter was KS&T's functional PAR.[74]

- KS&T selected Mr. Paul Brown as a figurehead PAR to comply with Ontario's residency requirement.[75] Mr. Brown, the only person associated with KS&T to have an address in Ontario, [redacted] [8] As discussed further below, Mr. Brown fulfilled the expectations of his role as PAR.

[73] [redacted]

[74] [redacted]

[75] [redacted]

[76] [redacted]

[77] [redacted] Having two AARs would have allowed KS&T to transfer emission allowances to and from its Ontario CITSS account without the PAR's involvement. *See* **RWS-4**, Ramlal – Second Witness Statement, ¶¶ 27-29. Had KS&T appointed one of its employees as a second AAR, it would have been able to transfer emission allowances to and from its Ontario CITSS account without involvement of any Canada-based persons. It did not do so.

[78] [redacted]

- [redacted]

38. Third, the strategic decisions with respect to the allocation of holding limits to KS&T's Ontario CITSS account were made in the United States, not Ontario. [redacted]

39. Fourth, decisions with respect to whether to register for a particular auction, overall bidding strategy, and which CITSS account to use to participate in auctions, were made in the United States:

- [redacted]

[79] **NR-13**, KS&T Participant Registration Form, [redacted] *See* **C-051**, KS&T, Ontario Business Relationship Disclosure Form, [redacted]

[80] **NR-13**, KS&T Participant Registration Form, [redacted]

[81] [redacted]

[82] **C-051**, KS&T, Ontario Business Relationship Disclosure Form, [redacted] **NR-12**, KS&T, Ontario Business Relationship Disclosure Form, [redacted] **NR-14**, KS&T, Ontario Business Relationship Disclosure Form, [redacted] **NR-16**, KS&T, Business Relationship Disclosure Form, [redacted] **NR-17**, KS&T, Business Relationship Disclosure Form, [redacted] *See also* [redacted]

[83] [redacted]

- [redacted]

- [redacted]

[redacted]

[redacted]

[84] [redacted]

[85] *See e.g.*, [redacted]

[86] [redacted]

[87] [redacted]

[redacted] [9]

40. Finally, the technical aspects of KS&T's auction participation, and the management of its bids and its Ontario CITSS account, were carried out by Mr. Porter, the functional PAR in Wichita, with oversight from Mr. Martin, the VP in Houston. In particular, Mr. Porter: [redacted] KS&T had only nominated two account representatives, meaning that Mr. Brown was technically necessary to approve transfers of emission allowances into and out of the Ontario CITSS account.[94] [redacted]

[88] This requirement became applicable starting with the November 29, 2014 auction. **R-128**, California Air Resources Board, "Chapter 5.1.5.A: Auction Application Attestation Guidance", October 2014, p. 1; **R-129**, California Air Resources Board, "Cap-and-Trade Auction Application: Auction Application Attestation Disclosure", p. 1.

[89] [redacted]

[90] *See e.g.,* [redacted]

[91] [redacted]

[92] *See e.g.* [redacted]

[93] [redacted]

[94] **RWS-2**, Ramlal – First Witness Statement, ¶¶ 35-37; **RWS-4**, Ramlal – Second Witness Statement, ¶¶ 37-41.

[redacted]

2. KS&T Confirmed Its Standard Practice Was to Move All Allowances Purchased in Ontario to California Immediately

41. Canada explained in its Counter-Memorial that KS&T purchased emission allowances almost exclusively for the purpose of [redacted][96] In their Reply, the Claimants object to this characterization, arguing that purchasing emission allowances at auctions through KS&T's Ontario CITSS account was "intrinsic to a complex business plan that involved far more than simple, immediate export to meet compliance obligations of other Koch companies."[97] Yet the Claimants failed to produce any such business plan, and KS&T's own contemporaneous documents betray their position.

42. Mr. Martin – the person responsible for strategic decisions relating to KS&T's Ontario business activities – confirmed with his track changes that KS&T's [redacted][98] In its Counter-Memorial, [redacted][9] and the Claimants provided no evidence of KS&T transferring emission allowances from

[95] [redacted]

[96] Canada's Counter-Memorial, ¶ 122.

[97] Claimants' Reply, ¶ 302.

[98] [redacted]

[99] Canada's Counter-Memorial, ¶¶ 57, 122, 298 and fns. 95, 229, 55. [redacted] *See* **RWS-2**, Ramlal – First Witness Statement, ¶ 52 and Attachment 1, [redacted] *See* **RWS-2**, Ramlal – First Witness Statement, ¶ 54 and Attachment 1, [redacted]

California to its Ontario CITSS account.[100] The fact that KS&T has not transferred any emission allowances to its related participants in Ontario – Invista or Komsa – is also not in dispute.[101]

43. In an attempt to downplay their strategy of "buy wholesale in Ontario, sell retail in California",[102] the Claimants allege that [redacted][104] These allegations not only misstate KS&T's holding limits, but confirm that KS&T was a cross-border trader.

44. A holding limit denoted the maximum number of emission allowances that a cap and trade participant, or a group of participants that are related persons ("corporate association group" or **CAG**), could hold at any point in time.[105] Members of each CAG – not the Government of Ontario – decided how to allocate the holding limit among themselves.[106] The allocation could be changed at any time by filing an updated business relationship disclosure form.[107] The evidence establishes that

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[100] The Claimants make a misleading statement that "allowances transferred to California could thereafter, and *several times* were, *transferred back* to Ontario or Québec for either physical sales (i.e. straight transfers of credits), or in connection with KS&T's ongoing futures sales." *See* **CWS-6**, King – Reply Witness Statement, ¶ 43. In reality, [redacted] *See* Canada's Counter-Memorial, ¶ 65; **RWS-2**, Ramlal – First Witness Statement, ¶ 56 and Attachment 1, [redacted] KS&T could not transfer emission allowances "back" to Québec for the sole reason that KS&T was not registered in Quebec's cap and trade program and thus did not have a Québec CITSS account. [redacted] *See* **RWS-4**, Ramlal – Second Witness Statement, ¶¶ 13, 44, fn. 47, and Attachment 2, [redacted]

[101] Canada's Counter-Memorial, ¶ 122; **RWS-2**, Ramlal – First Witness Statement, ¶ 13; Claimants' Reply, ¶ 56.

[102] Claimants' Memorial, ¶ 126; Canada's Counter-Memorial, ¶ 119. *See also* **CWS-2**, Martin – First Witness Statement, ¶ 36; **CWS-5**, Reply Witness Statement of Graeme Martin, 18 July 2022 ("Martin – Reply Witness Statement"), ¶ 15.

[103] **CWS-6**, King – Reply Witness Statement, ¶ 21.

[104] Claimants' Reply, ¶ 66; **CWS-6**, King – Reply Witness Statement, ¶ 33. *See also* **CWS-5**, Martin – Reply Witness Statement, ¶ 15 [redacted]

[105] **RWS-2**, Ramlal – First Witness Statement, ¶ 20; **RWS-4**, Ramlal – Second Witness Statement, ¶ 15.

[106] **RWS-2**, Ramlal – First Witness Statement, ¶ 23; **RWS-4**, Ramlal – Second Witness Statement, ¶ 17.

[107] *See e.g.*, **C-051**, KS&T, Ontario Business Relationship Disclosure Form, [redacted] **NR-12**, KS&T, Ontario Business Relationship Disclosure Form, [redacted] **NR-16**, KS&T, Business Relationship

KS&T was well-aware of the purpose and operation of holding limits,[108] and of participants' role in allocating them.[109]

45. [redacted] [11] Despite this fact, it was KS&T's "standard practice" to "immediately" transfer emission allowances to its California CITSS account after acquiring them at auction through its Ontario CITSS account.

3. KS&T's Alleged Secondary Market Activity in Ontario is a Smokescreen for its U.S.-Based Business

46. In its Counter-Memorial, Canada explained [redacted] [12] In their Reply, the Claimants argue that Canada's conclusions are "wrong"[113] because "KS&T's activities in tradeable

Disclosure Form, [redacted] **NR-17**, KS&T, Business Relationship Disclosure Form, [redacted]

[108] *See* [redacted]

[109] [redacted]

[110] [redacted] *See* **RWS-2**, Ramlal – First Witness Statement, ¶ 43; **NR-16**, KS&T, Business Relationship Disclosure Form, [redacted] **NR-17**, KS&T, Business Relationship Disclosure Form, [redacted]

[111] [redacted]

[112] Canada's Counter-Memorial, ¶¶ 51, 65, and 121.

[113] Claimants' Reply, ¶ 52.

compliance instruments (*i.e.*, emissions allowances and offset credits) was considerable".[114] However, the Claimants fail to identify any other transfers of emission allowances to or from KS&T's Ontario CITSS account.

47. Instead, they attempt to inflate KS&T's involvement in the secondary market in Ontario by counting activities conducted elsewhere. In the sections that follow, Canada explains that: (a) KS&T's trades in [redacted] were not business activities in Ontario; and (b) none of the Claimants' newly identified transactions had a connection to Ontario.

(a) KS&T's Trading in [redacted] Was Not a Business Activity in Ontario

48. In their Reply, the Claimants allege that KS&T [redacted] through the Intercontinental Exchange ("ICE"),[115] and that, as a result, KS&T [redacted] [16] However, these transactions cannot be considered business activity in Ontario.

49. First, trading in Ontario Carbon Allowance ("OCA") *futures* does not mean trading in Ontario *emission allowances*. Equating the two kinds of transactions is incorrect. A "futures" contract is a standardized derivative contract, traded on an exchange, in which "the parties agree to trade allowances at a certain date in the future, at a certain price".[117] Emission allowances do not change

[114] Claimants' Reply, ¶¶ 53, 4.

[115] Claimants' Reply, ¶ 53; **CWS-6**, King – Reply Witness Statement, ¶ 17 and Annex A, ¶ 1.

[116] Claimants' Reply, ¶ 53. *See also* **CWS-6**, King – Reply Witness Statement, ¶ 17 and Annex A, ¶ 1; [redacted]

[117] **CWS-4**, Witness Statement of Frank King, 6 October 2021 ("King – First Witness Statement"), ¶ 10; **CWS-6**, King – Reply Witness Statement, ¶ 16. *See also* **RS-006**, ECO Greenhouse Gas Report, p. 15 ("As in financial markets, products derived from allowances (*e.g.*, futures contracts) can also be traded. This is the case, for example, for futures contracts that allow a participant to purchase from another participant a certain quantity of emission allowances that are delivered on a given date and sold at a predetermined price. Derivative products can also be used to cover risks related to the variation of emission allowance prices.") On January 30, 2017, the ICE listed OCA futures, and options on OCA futures, for the 2017 vintage. These contracts were assigned "OC7 Vintage 2017" symbol. *See* **R-143**, ICE Futures U.S., "Exchange Notice: Listing of New Energy Futures Contracts on January 30, 2017", 30 January 2017; **R-144**, ICE Futures U.S., "Exchange Notice: Listing of New Energy Futures Contracts on January 22, 2018", 11 December 2017; **R-145**, ICE Futures U.S., "New California Carbon Allowance Vintage 2021 Future and Related Amendments Submission Pursuant to Section 5c(c)(1) of the Act and Regulation 40.2", Submission No. 18-7, 4 January 2018. *See also* **R-146**, ICE

hands until the contract's settlement date, and only physical delivery of emission allowances is recorded in the CITSS.[118] It is not necessary for a futures trader to ever hold an emission allowance. KS&T itself acknowledged the difference, [redacted] [19]

50. Second, even if somehow relevant, KS&T's trading activity in futures contracts was activity conducted in the United States, not in Ontario. KS&T's trades were executed by its Chicago-based broker, Mizuho Securities,[120] on the ICE, a commodities exchange based in the United States.[121]

51. Finally, as the Claimants themselves recognize, trading in futures is entirely anonymous and, at the contract settlement date, the ICE matches net buyers and net sellers in order to arrange physical delivery.[122] As a result, contrary to the Claimants' suggestion that futures trading was an integral part of its business activity in Ontario, it was only by chance that KS&T might be matched to a counterparty in Ontario with respect to a futures obligation.

Futures U.S., "Delisting of Ontario Carbon Allowance Futures and Options Contracts Submission Pursuant to Section 5c(c)(1) of the Act and Regulation 40.6(a)", Submission No. 18-377, 3 July 2018.

[118] **RWS-4**, Ramlal – Second Witness Statement, ¶ 42. [redacted] *See* **CWS-6**, King – Reply Witness Statement, ¶ 17 and Annex A, ¶¶ 1, 11. [redacted] *See* Canada's Counter-Memorial, ¶ 51; **RWS-2**, Ramlal – First Witness Statement, ¶ 51 and Attachment 1, [redacted]

[119] *See e.g.*, [redacted]

[120] *See e.g.*, [redacted] Only entities registered with the ICE could trade in futures *See* **R-152**, Intercontinental Exchange, U.S. Membership website, available at: https://www.theice.com/futures-us/membership

[121] The ICE is incorporated under the laws of Delaware and its full legal name is "ICE Futures U.S., Inc." The ICE is a subsidiary of Intercontinental Exchange, Inc., a company incorporated under the laws of Delaware, with its headquarters and principal executive office located in Atlanta, Georgia and New York, New York. *See* **R-153**, Intercontinental Exchange, Inc., "Form 10-K: Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2021" ("ICE Annual Report, 2021"), pp. 19, 39-40, and Exhibit 21.1.

[122] **CWS-2**, King – Witness Statement, ¶ 10; **CWS-6**, King – Reply Witness Statement, ¶ 16.

(b) Almost None of KS&T's Secondary Market Trading in Compliance Instruments Had a Connection to Ontario

52. In their Reply, the Claimants further allege that KS&T entered into [redacted] [124] After providing no evidence of these transactions in their Memorial, the Claimants submitted copies of thirty-six contracts that KS&T had concluded with various counterparties with their Reply.[125] The Claimants' late attempts to bolster KS&T's business activity in Ontario are misplaced.[126]

53. First, [redacted]

[123] Claimants' Reply, ¶ 53; **CWS-6**, King – Reply Witness Statement, ¶ 21 and Annex A, ¶ 17.

[124] Claimants' Reply, ¶¶ 53, 305; **CWS-6**, King – Reply Witness Statement, ¶ 26.

[125] The Claimants provided copies of [redacted] (**FK-6**; **FK-9**; **FK-10**; **FK-12**; **FK-14**; **FK-16**; **FK-17**; **FK-19**; **FK-21**; **FK-23**; **FK-25**); [redacted] (**FK-27**; **FK-30**; **FK-33**; **FK-35**; **FK-37**; **FK-41**); and [redacted] (**FK-44**; **FK-46**; **FK-48**; **FK-49**; **FK-51**; **FK-52**; **FK-53**; **FK-55**; **FK-57**; **FK-58**; **FK-59**; **FK-60**; **FK-61**; **FK-62**; **FK-63**; **FK-64**; **FK-66**; **FK-67**; **FK-68**).

[126] In the document production phase, Canada requested documents referring to, relating to, or concerning: [redacted] *See* Procedural Order No. 2, Annex B, Requests 8, 10, and 11. The Claimants produced documents related to [redacted] *See* [redacted]

[127] Canada's Counter-Memorial, ¶ 65; **RWS-2**, Ramlal – First Witness Statement, ¶ 56 and Attachment 1, [redacted]

[128] Several of the contracts KS&T entered into [redacted] *See* **FK-14**; **FK-19**; **FK-23**; **FK-25**. [redacted] *See* **FK-6**; **FK-9**; **FK-10**; **FK-12**; **FK-16**; **FK-17**; **FK-21**; **FK-23**; **FK-25**. [redacted]

[redacted] [130] The Claimants' reliance on these transactions is unhelpful. The fact that KS&T entered into contracts [redacted] cannot serve as evidence of KS&T's business activity in Ontario.

54. Similarly, [redacted] [31] all of the [redacted]

[redacted] *See* Claimants' Reply, ¶¶ 53, 305 and fns. 56, 442; **CWS-6**, King – Reply Witness Statement, ¶ 21 (emphasis in original).

[129] Throughout their Reply, the Claimants attempt to lump together emission allowances and offset credits. *See e.g.*, Claimants' Reply, ¶¶ 53, 305; **CWS-6**, King – Reply Witness Statement, ¶ 21. Offset credits are not relevant to this dispute. An offset credit is a compliance instrument that represents a reduction, avoidance or removal of one tonne of CO_2e achieved by a government-approved project. *See* **RS-006**, ECO Greenhouse Gas Report, p. 5. Notably, ("[r]evenues from the sale of offsets are not received by government, but rather to the project proponent.") *See* **RS-006**, ECO Greenhouse Gas Report, p. 15; **RWS-4**, Ramlal – Second Witness Statement, ¶ 13. [redacted] *See* **FK-6**; **FK-14**; **FK-19**; **FK-21**, **FK-25**.

[130] [redacted] (**FK-6**; **FK-9**; **FK-10**; **FK-12**; **FK-14**; **FK-16**; **FK-17**; **FK-19**; **FK-23**; **FK-25**). [redacted]

[131] Canada's Counter-Memorial, ¶ 65; **RWS-2**, Ramlal – First Witness Statement, ¶ 56 and Attachment 1, [redacted]

[132] [redacted] (**FK-30**; **FK-33**; **FK-35**) [redacted] *See* **CWS-6**, King – Reply Witness Statement, ¶¶ 36, 42, 44; **FK-29**, [redacted] **FK-42**, [redacted]

[133] [redacted] (**FK-27**) [redacted] (**FK-30**; **FK-35**) [redacted]

[134] [redacted]

[redacted] [35]

55. Second, [redacted] [139] KS&T's trading in [redacted] is not business activity in Ontario.

C. KS&T's Participation in the May 2018 Auction Was a Calculated Risk

56. The Claimants' documents further establish that KS&T was advised to exercise caution in purchasing emission allowances ahead of the June 2018 election, participated in the May 2018 auction anyway, and was unable to transfer its emission allowances to California because of its own poor planning.

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[135] **CWS-6**, King – Reply Witness Statement, ¶ 34. [redacted] *See* Canada's Counter-Memorial, ¶ 65; **RWS-2**, Ramlal – First Witness Statement, ¶ 56 and Attachment 1, [redacted]

[136] [redacted] *See* **R-154**, CARB, Compliance Instrument Tracking System Service Registrant Report Q1, 30 March 2018; **R-155**, CARB, Compliance Instrument Tracking System Service Registrant Report Q2, 29 June 2018; **R-156**, Quebec, Compliance Instrument Tracking System Service Registrants, 31 March 2021. [redacted]

[137] [redacted] (**FK-44**; **FK-46**; **FK-49**; **FK-53**; **FK-55**; **FK-59**; **FK-63**; **FK-64**); [redacted] (**FK-48**; **FK-57**; **FK-62**). [redacted]

[138] [redacted] (**FK-51**; **FK-52**; **FK-57**; **FK-58**; **FK-60**; **FK-66**; **FK-67**; **FK-68**) [redacted] (**FK-59**). [redacted]

[139] [redacted] (**FK-61**; **FK-62**) [redacted] (**FK-44**; **FK-46**).

57. [redacted] KS&T registered for the May 15, 2018 auction[143] and proceeded to participate in it.[144] At the same time, [redacted][145] By [redacted] KS&T's Ontario CITSS account balance was [redacted][46]

58. The emission allowances that KS&T purchased from the three jurisdictions in the auction were transferred in separate transfers from each jurisdiction on June 11, 2018.[147] True to form, [redacted]

[140] Mr. Brown "also supplied government affairs support to Koch companies across Canada", reporting "directly to Koch Companies Public Sector, LLC". *See* **CWS-3**, Brown – Witness Statement, ¶ 7.

[141] [redacted]

[142] [redacted]. Mr. Ford was the PC Party's leader at this time.

[143] **R-047**, Auction Notice, "California Cap-and-Trade Program, Quebec Cap-and-Trade System, and Ontario Cap-and-Trade Program Joint Auction of Greenhouse Gas Allowances On May 15, 2018, 16 March 2018, p. 8 of 11.

[144] [redacted] At the May 2018 auction, KS&T procured [redacted] *See* Claimants' Memorial, ¶ 178; **CWS-4**, King – First Witness Statement, ¶¶ 24-25 (emphasis added).

[145] *See e.g.*, [redacted] **RWS-2**, Ramlal – Witness Statement, ¶¶ 53-55 and Attachment 1, [redacted]

[146] *See* Canada's Counter-Memorial, fn. 553; **RWS-2**, Ramlal – Witness Statement, ¶¶ 53-55 and Attachment 1, transfers No. 126127, 126246, and 126440.

[147] Canada's Counter-Memorial, ¶ 76. KS&T understood how this worked. *See* [redacted]

[redacted]

59. As Canada has previously explained, the May 2018 auction took place during the election campaign. KS&T was well aware that the transfer of allowances into winning bidders' CITSS accounts would only occur on June 11, 2018, after the election held on June 7, 2018.[150] The evidence demonstrates that KS&T's plan to bid at the May 2018 auction and then [redacted] transfer emission allowances to California failed because of their own poor planning and miscalculated risk.[151]

D. Ontario Declined to Commit the Incoming Government to a Future Auction of Emission Allowances

60. California and Quebec planned to hold a joint auction for emission allowances on August 14, 2018. Under the Ontario rules governing auction dates, if Ontario wished to participate in the August auction it would need to give public notice on June 15, 2018. That day fell after Ontario's provincial election but prior to the swearing-in of the new government. Ontario declined to participate.

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148 [redacted]

149 [redacted]

150 Canada's Counter-Memorial, ¶¶ 72-73. *See e.g.*, [redacted]

151 [redacted]

61. The Claimants make a number of incorrect assertions about the events of June 15. First, they attempt to construe a press release by the Premier-Designate as having "cancelled" Ontario's cap and trade program. Second, they elide the actual rules applicable to auctions and auction notification in Ontario. Third, they seek to undermine the decision to decline to issue an auction notice itself, which was made in accordance with caretaker principles and delegated Ministerial authority.

1. Premier-Designate Ford's Press Release Did Not "Cancel" the Cap and Trade Program

62. The Claimants repeatedly assert that a press announcement on June 15, 2018 by the Premier-Designate, Doug Ford, "cancelled" the cap and trade program. That assertion is false. No cancellation took place on that day.

63. Premier-Designate Ford's press release was an announcement of future intent by the incoming government. Such public announcements by an incoming government are common during the transition period prior to assuming office.[152] Moreover, the press release did not even purport to cancel the cap and trade program. Premier-Designate Ford instead announced that his "cabinet's first act *following the swearing-in of his government will be* to cancel Ontario's current cap-and-trade scheme".[153] At the time, the Claimants understood that Ontario did not cancel the cap and trade program on June 15.[154]

2. The Claimants Misunderstand the Ontario Process for Auction Notification and Scheduling

64. The Claimants misrepresent the rules governing Ontario's auction process, going so far as to suggest that Ontario violated its laws by declining to issue a notice for the August 2018 joint

[152] Canada's Counter-Memorial, ¶ 78.

[153] **C-007**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Announces an End to Ontario's Cap-and-Trade Carbon Tax", 15 June 2018.

[154] *See* [redacted]

auction[155] and that public servants "usurp[ed]" decision-making power with regard to the notice.[156] The Claimants are incorrect about Ontario's auction notification process.

65. First, Ontario did not set the dates of auctions by regulation. Regulation 144/16 stated that Ontario was required to hold four auctions on separate occasions each year, but did not specify that auctions be held on a particular date.[157] Rather, under Ontario's regulations, the dates of auctions were set by issuing an auction notice that was published at least 60 days in advance of the auction date.[158]

66. Second, the MECP Minister or a civil servant with delegated Ministerial power[159] held the authority to issue auction notices.[160] In December 2017, the MECP Minister delegated such authority to the Director of the Cap and Trade Branch – a position held by Mr. Jeff Hurdman (**Minister's Delegate**).[161] This delegation remained in effect on June 15, 2018.[162]

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[155] Claimants' Memorial, ¶¶, 364, 365. *See also* Claimants' Reply, ¶ 140.

[156] Claimants' Reply, ¶ 145.

[157] *See* **R-007**, Regulation 144/16, s. 58(1) ("Each year starting in 2017, the Minister shall submit emission allowances for the purposes of an auction to be held on four separate occasions, each consisting of a single round of bidding."). *See also* **RWS-3**, Wood – Second Witness Statement, ¶ 7.

[158] The auction notice had to include certain information, including the day and time set for an auction, a summary of the auction process, and information pertaining to the number and vintage of emission allowances that would be offered for sale. *See* **R-007**, Regulation 144/16, s. 60(1); **RWS-2**, Ramlal – Witness Statement, ¶ 28. The publication of the auction notice triggered key dates for entities that wished to participate in the auction, including dates for applying for permission to register in the auction and dates for the provision of financial guarantees. *See* **R-007**, Regulation 144/16, ss. 67(1)(2) and 67(1)(3). Under section 60(3), the Minister or Minister's Delegate could modify the notified date by up to four days.

[159] Section 74(1) of the *Climate Change Act* permitted the Minister to delegate any powers or duties assigned under the *Climate Change Act* or its regulations to a public servant or other person. *See* **R-006**, *Climate Change Act*, s. 74(1).

[160] **R-007**, Regulation 144/16, s. 60(1). The timing of auctions was discretionary. *See* [redacted]

[161] **RWS-3**, Wood – Second Witness Statement, ¶ 10; **R-167**, Ministry of the Environment and Climate Change, "Delegation of Certain Minister's Powers and Duties", 4 December 2017. These powers and duties had previously been delegated to the Director, Program Management Branch of the MEOCC. The 2017 delegation was issued because the title "Director, Program Management Branch, Environmental Programs Division" was changed to "Director, Cap and Trade Branch, Climate Change Directorate". *See* **RWS-4**, Ramlal – Second Witness Statement, fn. 13; **R-168**, Decision/Approval Note, "Cap and Trade Program – Delegation of Minister's Authorities for Auction Activities", 28 October 2016.

[162] **RWS-3**, Wood – Second Witness Statement, ¶ 10. Under Section 81 of Ontario's *Legislation Act*, 2006, any delegation of a power or duty remains valid until it is revoked or amended. *See* **R-169**, *Legislation Act*, S.O. 2006, c.21, s. 81.

67. Third, Ontario's participation in auctions was not a "historical, ministerial decision" that was made once.[163] A separate decision was required for each auction. In 2017 and 2018, the Minister's Delegate issued separate auction notices, and separate Decision/Approval Notes were prepared for each auction.[164] After harmonization with Québec and California, Ontario retained control over the timing of auctions and whether it would participate in joint auctions, and followed the same internal process.[165]

3. Ontario's Decision to Decline to Issue an Auction Notice Was in Keeping with Established Principles

68. If Ontario wished to participate in the August 2018 joint auction, an auction notice was required by June 15 – during the transition period after Ontario's election, but prior to the swearing in of Mr. Ford's government.[166] On June 15, 2018, the Minister's Delegate declined to issue an auction notice committing Ontario to offer emission allowances for auction in August 2018. There was nothing improper, let alone "*ultra vires*", about that decision.

69. In Canada, a government enters a "caretaker period" from the moment an election is called until "a new government is sworn-in" or "an election result returning an incumbent government is clear."[167] During a caretaker period, government activity does not halt; the incumbent government

[163] Claimants' Reply, ¶ 145.

[164] *See* [redacted]

[165] As noted in Part II.A.3, the *Climate Change Act* and its regulations continued to govern Ontario's cap and trade program after harmonization. [redacted] Given that Ontario's participation in joint auctions was discretionary, Ontario's cap and trade webpage publicized the anticipated dates for joint auctions, but indicated that anticipated auction dates "are subject to change and will be confirmed through the official Auction Notice." *See* **R-171**, Ontario, Cap and Trade Summary (Archived), last updated 12 July 2021, fn. 1.

[166] The Progressive Conservative Party won a majority in Ontario's June 7 election and would be sworn in on June 29, 2018. *See* **C-102**, Ontario News Release, "Doug Ford to Become Ontario's 26th Premier", 8 June 2018.

[167] **C-201**, Government of Canada, Guidelines on the conduct of Ministers, Ministers of State, exempt staff and public servants during an election, August 2021. *See also* **R-053**, Memo to Deputy Ministers from Secretary Steve Orsini, "Public Service Responsibilities and Procedures Leading To and During the Election Period", 28 February 2018.

retains legal authority to govern but is expected to act with restraint.[168] This balances the need for the continuation of routine government operations and necessary business while respecting the principle of responsible government.[169] The decision about whether or not to issue an auction notice on June 15 would need to be made in light of caretaker principles, including the principle of acting with restraint.[170]

70. The Progressive Conservative Party had just won a clear majority after campaigning on cancelling the cap and trade program.[171] In this context, participation in the August 2018 auction was not "routine".[172] Issuing an auction notice would commit the incoming government to the continued distribution of allowances in a regulatory system it had pledged to unwind. In addition, Regulation 144/16 did not provide any mechanism to allow for withdrawal from an auction after one had been notified – meaning that a notice was not easily "reversible" by the new government.[173]

71. Where a decision must be made concerning a controversial matter, caretaker principles encourage the outgoing government and public service to consult with and consider the views of

[168] The principle of restraint is a political rule rather than law, and gives officials flexibility to respond to circumstances arising during the caretaker period. As Canada's Privy Council Office notes, in determining what activity is necessary for continued governance, "the Government must inevitably exercise judgement, weighing the need for action and the restraint called for by convention." *See* **C-201**, Government of Canada, Guidelines on the conduct of Ministers, Ministers of State, exempt staff and public servants during an election, August 2021.

[169] **C-201**, Government of Canada, Guidelines on the conduct of Ministers, Ministers of State, exempt staff and public servants during an election, August 2021.

[170] **R-053**, Memo to Deputy Ministers from Secretary Steve Orsini, "Public Service Responsibilities and Procedures Leading To and During the Election Period", 28 February 2018.

[171] *See e.g.*, **R-032**, PC Party of Ontario, "People's Guarantee", p. 25; **R-034**, PC Party of Ontario, "Doug Ford Will Fight a Carbon Tax and Scrap Kathleen Wynne's 'Cap and Trade' Slush Fund", 23 April 2018; **R-077**, Ontario PC Party, "Statement from Ontario PC Leader Doug Ford on the Carbon Tax", 25 April 2018; **R-078**, Ontario PC Party, "Doug Ford will Cut Gas Taxes by Ten Cents Per Litre", 16 May 2018; **R-079**, Ontario PC Party, Doug Ford Formally Commits to Reducing Taxes for Ontario Families, 24 May 2018; and **R-080**, Ontario PC Party, "NDP Will Increase Gas & Hydro Bills, Ontario PCs Will Reduce Them", 30 May 2018; and **R-172**, "Doug Ford says he stands with PM in U.S. trade dispute", 8 June 2018.

[172] The public service in Ontario had been taking steps to prepare CITSS for possibly participating in the August 2018 auction. As Mr. Wood explains, the public service was prepared for either option. **RWS-3**, Wood – Second Witness Statement, fn. 10.

[173] The Claimants suggest that issuing the notice "would not have limited or impaired the decision-making freedom of the Ford Government" because the "OQC Agreement would have encompassed the auction scheduled for at least 12 months." *See* Claimants' Reply, ¶ 150. This relies on a flawed understanding of the legal framework for cap and trade and the legal effect of the *Harmonization Agreement*, including its withdrawal provisions. As demonstrated in Part II.A.3, Ontario's cap and trade system was governed by Ontario law and regulations, not the *Harmonization Agreement*.

opposition parties or the incoming government.[174] As is typical and appropriate, senior members of the public service briefed the incoming government's transition team and sought their views on the decision pertaining to the next joint auction notice.[175] In fact, given the sensitivity of the issue, it would have been inappropriate under caretaker principles for the public service not to seek the views of the incoming government's transition team. [redacted][176]

72. Moreover, contrary to the Claimants' accusations of unelected bureaucrats "usurp[ing]" decision-making functions and taking decisions "contrary to the position of the sitting government,"[177] the Minister's Delegate, in consultation with senior officials and the MECP Deputy Minister, simply declined to issue the auction notice, in accordance with properly delegated authority and caretaker principles.[178] The incumbent Minister could have intervened and notified Ontario's participation in the August 2018 auction; he did not do so.[179]

73. Finally, the Claimants repeatedly point to the Premier-Designate's statement that he had "directed" officials not to participate in future auctions – while acknowledging that its legality is "moot".[180] On that point at least, they are correct. It is undisputed that Ontario declined to issue an auction notice on June 15, 2018.

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[174] **C-202**, Philippe Lagassé, Clarifying the Caretaker Convention (Policy Options Politiques), 9 October 2015.

[175] **RWS-1**, Wood – First Witness Statement, ¶¶ 14-15; **RWS-3**, Wood – Second Witness Statement, ¶ 11.

[176] **RWS-3**, Wood – Second Witness Statement, ¶ 12.

[177] Claimants' Reply, ¶ 145.

[178] In addition, the Claimants' allegations that Ontario "blindsided" California and Québec on June 15 are incorrect, as Mr. Wood explains. *See* **RWS-3**, Wood – Second Witness Statement, ¶¶ 13-17.

[179] Section 80 (Powers and duties remain despite delegation) of Ontario's *Legislation Act* provides "A person on whom an Act confers a power or imposes a duty may exercise it even if it has been delegated to another person." *See* **R-169**, *Legislation Act,* s. 80.

[180] Claimants' Reply, ¶ 156.

E. California De-linked its CITSS Registry from Ontario's

74. At 8 p.m. on June 15, California issued a "market notice" advising participants that it was prohibiting incoming transfers to Ontario accounts, as well as outgoing transfers to Ontario accounts.[181]

75. The Claimants argue that the "trigger" for California de-linking that day was "the *ultra vires* actions of the Premier-elect."[182] Leaving aside the fact that the June 15, 2018 announcement was not "*ultra vires*" as Canada explained above, California's motives do not matter.[183]

76. In addition, de-linking was not the only option available to California to protect the integrity of its system. As Mr. Litz explains, California could have taken the same approach as the RGGI states did when New Jersey announced its plan to withdraw in 2018, and Virginia announced its plan to withdraw in 2021. In both cases, the remaining RGGI states kept the connection with the departing state intact, and honoured all emission allowances. Similarly, California could have maintained the connection with Ontario intact continued to honour allowances sold at joint auctions with Ontario. They could then have made adjustments to their program to absorb the extra Ontario allowances.[184]

77. Another option available to California would have been to selectively honour emission allowances based on their date or origin. As Mr. Litz explains, California could have decided to honour only those allowances that were sold in the first two auctions of 2018, in which all three jurisdictions participated.[185] Or, California could have selectively honoured its connection with certain account holders and certain account types. For example, California could have permitted

[181] **C-104**, California Air Resources Board, Market Notice, 15 June 2018. After the Premier-Designate's announcement but prior to California's notice, an Ontario cap and trade participant made three separate transfers from its Ontario CITSS to its California CITSS account. **C-200**, Email from Jeff Hurdman to Alex Wood, "Preventing Auction Registration", 15 June 2018, p. 1. *See also* [redacted]

[182] Claimants' Reply, ¶ 160; Claimants' Reply, ¶ 156.

[183] The Harmonization Agreement, on which the Claimants rely, expressly protected each party's regulatory autonomy. Each party retained sovereign rights over its program, including the right to withdraw from the linked system. *See* Canada's Counter-Memorial, ¶ 55.

[184] **RER-4**, Litz – Second Expert Report, ¶¶ 40-45.

[185] **RER-4**, Litz – Second Expert Report, ¶¶ 47-49.

participants in Ontario to apply to have the allowances in their Ontario holding accounts transferred to California, provided that the applicant could prove that the emission allowances had been purchased to meet a compliance obligation in California.[186]

78. While these examples are merely illustrative, they discredit the Claimants' arguments that California de-linking was an inevitable result of the Premier-Designate's June 15 press release.[187]

F. Ontario's Winding Down of the Cap and Trade Program Was Based on Legitimate Policy Goals

1. The Policy Goals of the New Government Dictated the Options for Winding Down the Program

79. After the new government was sworn in on June 29, it made winding down the cap and trade program a priority.[188] Guided by the new government's policy goals of winding down the system as soon as possible without imposing additional costs, Ontario public servants identified certain policy options that were no longer viable. For example, Mr. Wood explains that continuing the program until the end of the first compliance period in 2020 was not an option given the policy goal of winding down the program as soon as possible. Moreover, any options that would have resulted in additional costs for Ontarians, for instance by requiring entities who were short to buy additional emission allowances, either by purchasing them from entities who had excess allowances or by holding an extraordinary Ontario auction, were rejected as incompatible with the policy goals of the new government.[189]

[186] **RER-4**, Litz – Second Expert Report, ¶¶ 50-52.

[187] While the Claimants accuse Ontario of trying to "shift the blame" to California, their protestations are undermined by their own contemporaneous documents. Internal briefing materials state: "it was California who ran the Red light and blindsided us." [redacted]

[188] **R-054**, ipolitics, "Ford to recall Ontario legislature on July 11", 29 June 2018.

[189] **RWS-3**, Wood – Second Witness Statement, ¶ 20.

2. Ontario's Wind-Down of its Cap and Trade Program Was Lawful and Legitimate

80. The Claimants attempt to characterize the process of winding down Ontario's cap and trade program as "illegal" and "reckless".[190] In reality, the process followed the well-established normal legislative process in Ontario.[191]

81. As described in Canada's Counter-Memorial, the first step to wind-down Ontario's cap and trade was the making of Regulation 386/18, which came into force on July 3, 2018.[192] Regulation 386/18 was made under the *Climate Change Act*. It had the effect of prohibiting cap and trade participants with Ontario CITSS accounts from purchasing, selling, trading or otherwise dealing with emission allowances. The Government of Ontario had expressed its intention of winding down cap and trade as soon as possible and the making of Regulation 386/18 gave effect to this policy intent. The Claimants' attempts to attack Regulation 386/18 as hasty and illegitimate because it "was not

[190] Claimants' Reply, ¶¶ 202, 203.

[191] In footnote 183 of their Reply, the Claimants suggest that the Tribunal "is entitled to draw an adverse inference" as a result of domestic access to information requests made by Mr. Jonathan McGillivray under Ontario's *Freedom of Information and Protection of Privacy Act* (***FIPPA***) in December 2019 (*see also* Claimants' Reply, ¶¶ 153-154). This suggestion should be rejected. The Ontario *FIPPA* process is extraneous to this arbitration. The Claimants have not requested, nor has the Tribunal called upon, Canada to produce documents with respect to domestic FIPPA requests. Canada responded to the Claimants' document requests in this arbitration. *See* [redacted] In any event, Ontario responded to the access to information requests, and documents were disclosed or withheld in accordance with *FIPPA* procedures and rules. The requests made to MECP did not proceed to the disclosure of documents stage because the requestor declined to pay the fee estimate required to proceed. *See* **JMG-18**, Ministry of the Environment, Conservation and Parks Decision, A-2020-00203, 6 April 2021; **JMG-19**, Ministry of the Environment, Conservation and Parks Decision, A-2020-00204, 6 April 2021; **CWS-8**, Witness Statement of Jonathan McGillivray, 17 July 2022, ¶¶ 28-31. The requestor's requests to other Ministries were either allowed, resulting in the disclosure of documents, or denied in accordance with *FIPPA*. The requestor also appealed to the Information and Privacy Commissioner of Ontario. Those appeals have been resolved and the files are now closed. *See* Claimants' Reply, fn. 183; **CWS-8**, Witness Statement of Jonathan McGillivray, 17 July 2022, ¶ 31; **R-178**, Closing Letter 203 from Soo Kim to Ryan Gunn, 12 August 2022; **R-179**, Closing Letter 204 from Soo Kim to Ryan Gunn, 12 August 2022; **R-180**, Closing Letter from Soo Kim to Nadia Williams, 12 August 2022.

The Claimants also appear to suggest that an adverse inference is warranted with respect to one of the Claimants' document requests (No. 11), which sought "documents relating to any distribution of the allowances or funds amongst the linked jurisdictions". *See* Claimants' Reply, ¶ 126 and fn. 182. This too is baseless and should be ignored. In joint auctions, participating jurisdictions only received payment, via the Financial Services Administrator in New York, for the emission allowances that they had created and offered for auction. *See* Canada's Counter-Memorial, ¶ 46. KS&T understood this at the time. *See* [redacted] Canada did not produce documents regarding transfer of funds between the jurisdictions following the May 2018 auction because no such documents exist.

[192] Canada's Counter-Memorial, ¶ 85.

accompanied by any explanation or assurances […] as to the government's plan for an 'orderly' wind down" must be rejected.[193]

82. After the coming into force of Regulation 386/18, Ontario's public servants started working on draft legislation that would repeal the cap and trade program. The *Cap and Trade Cancellation Act* ("Bill 4") was introduced in the Ontario Legislative Assembly on July 25, 2018. From July to September 2018, the Ontario Legislature debated Bill 4 on seven separate occasions, prior to the Bill being referred to a legislative Standing Committee. The Standing Committee considered the Bill in three sessions in October, after which the Bill returned to the full Legislature and was carried on October 31, 2018.[194] Bill 4 received Royal Assent the same day.[195] In addition to the legislative process, Ontario undertook stakeholder briefings and public consultations on the Bill.

83. In their Reply, the Claimants attack the consultation process for Bill 4, essentially arguing that this process had no legitimacy and that "Ontario was simply 'going through the motions' to give the appearance of legitimate, democratic process".[196] They also argue that only two "administrative" errors were changed following the public consultation on Bill 4. The Claimants are incorrect.

84. As Mr. Wood explains, as soon as Bill 4 was introduced in the Ontario Legislative Assembly on July 25, 2018, the Ontario government informed stakeholders on both the content of the Bill and on the steps that would be taken to wind-down the cap and trade program in an orderly fashion.[197] Mr. Wood led two one-hour technical briefings on July 25 and July 27, 2018. During these webinars, he discussed Bill 4, provided an opportunity for participants to ask questions, and responded to numerous stakeholder questions. All of the concerns raised and responses given were then summarized in an internal document prepared by the MECP.[198] In addition to these technical briefings, stakeholders were encouraged to contact the Cap and Trade Help Desk for any further

[193] Claimants' Reply, ¶ 200.

[194] **R-181**, Bill 4, *Cap and Trade Cancellation Act*, 2018, Legislative History.

[195] **R-181**, Bill 4, *Cap and Trade Cancellation Act*, 2018, Legislative History.

[196] Claimants' Reply, ¶ 201.

[197] **RWS-3**, Wood – Second Witness Statement, ¶ 27.

[198] **RWS-3**, Wood – Second Witness Statement, ¶ 27; **R-182**, "Summary of Cap and Trade Cancellation Act, 2018 Stakeholder webinars".

questions or concerns they might have had with respect to the wind-down of Ontario's cap and trade program.[199]

85. Ontario also posted Bill 4 for public comment on the Environmental Registry of Ontario on September 11, 2018.[200] As Canada explained in its Counter-Memorial, Ontario received voluminous comments, and followed its usual process for considering and publishing comments, including a consultation summary.[201] As Mr. Wood explains, Ontario received and considered over 11,000 comments.[202] The Claimants appear to suggest that the publication date of the consultation summary (November 15) indicates that the consultation process was not meaningful.[203] That is incorrect. Following standard practice and in line with the requirements of the *Environmental Bill of Rights*, Ontario published the consultation summary after the Bill was implemented.[204]

3. Ontario Adopted a Principled Approach to Compensation

86. The Claimants allege that Ontario's approach to compensation was "non-sensical" and [redacted] [205] The Claimants are incorrect.

[199] **R-182**, "Summary of Cap and Trade Cancellation Act, 2018 Stakeholder webinars", pp. 1 and 3.

[200] Several weeks after its initial decision that a separate consultation process was not required in light of the recent election, Ontario agreed to post Bill 4 on the Environmental Registry of Ontario. In the *Greenpeace* decision, which was rendered a year *after* the public consultation took place, Justice Myers emphasized that Greenpeace was not challenging the validity of the *Cancellation Act*, but was rather looking for an "academic determination that the interim freezing of the marketplace in cap and trade credits by the repeal of the cap and trade regulation did not meet the public participation requirements of the *Environmental Bill of Rights*." The Court dismissed Greenpeace's application. *See* **R-058**, *Greenpeace Canada v. Minister of the Environment (Ontario)*, 2019 ONSC 5629, ¶ 91.

[201] Canada's Counter-Memorial, ¶¶ 87, 90. *See also* **C-012**, Environmental Registry of Ontario, "Bill 4, Cap and Trade Cancellation Act, 2018", 15 November 2018 ("Environmental Registry – Bill 4").

[202] **RWS-1**, Wood – First Witness Statement, ¶ 26. Public consultations led to a number of substantive amendments to Bill 4. *See* **RWS-3**, Wood – Second Witness Statement, ¶ 28.

[203] Claimants' Reply, ¶ 201.

[204] **AW-29**, Environmental Bill of Rights, 1993, s. 36. Sub-section 36(1) provides that: ("As soon as reasonably possible after a proposal for a policy, Act or regulation in respect of which notice was given under section 15 or 16 is implemented, the minister shall give notice to the public of the implementation.") The consultation summary is considered as a "brief explanation of the effect, if any, of public participation on decision-making on the proposal" under ss. 36(3) of the Environmental Bill of Rights. Under section 1(6) of the EBR, "implementation" means when a Bill receives third reading in the Legislature.

[205] Claimants' Reply, ¶¶ 202, 207.

87. Ontario's compensation approach was tied to the function that compliance entities fulfilled in the cap and trade program. The cap and trade program was created to help reduce greenhouse gas emissions and to create incentives for compliance entities to rely on greener technologies. The Ontario Government decided to compensate compliance entities that had bought emission allowances in excess of their actual emissions. As Mr. Wood explains, "[u]nlike compliance entities, market participants did not have any compliance obligations to meet as part of the program and were not compelled to participate or to purchase emission allowances. As a result, compliance entities and market participants were treated differently under the cap and trade program."[206]

88. Nor were market participants singled out for ineligibility; other categories of participants were also excluded from compensation. For example, fuel suppliers and natural gas distributors were excluded from compensation because they were able to pass on the cost of compliance directly to Ontario consumers.[207]

89. Finally, the Claimants' reliance on a $5 million figure that was used in internal documents when the government was drafting the *Cancellation Act* is misplaced. As Mr. Wood explains, this $5 million figure was an estimated compensation amount, it was not a "goal" that Ontario wanted to meet in order to minimize payment of compensation. Ontario could not have precisely determined the final compensation amount as it did not have the entities' final emissions reports and could not have known the exact result of the matching of emissions.[208]

4. Ontario Began Work on a New Environment Plan as Early as the Fall of 2018

90. The Claimants argue that Ontario's cancellation of the cap and trade program was not taken for environmental purposes, but rather so that it could "crow to Ontario suburbanites that they have reduced the cost of gas by 10 cents a liter"[209] and that it "was undertaken […] primarily for arbitrary

[206] **RWS-3**, Wood – Second Witness Statement, ¶ 22. In keeping with their non-compliance role, market participants were treated differently from compliance entities under the Ontario cap and trade program. For example, market participants were unable to open compliance accounts in the CITSS registry system, and also faced strict purchase limits at auctions for emission allowances. *See e.g.*, **R-007**, Regulation 144/16, s. 69 ("Purchase limits").

[207] *See* Canada's Counter-Memorial, ¶¶ 97, 205, 276.

[208] **RWS-3**, Wood – Second Witness Statement, ¶ 24.

[209] Claimants' Reply, ¶ 191.

political reasons".[210] They also make a number of unsubstantiated allegations about how Ontario cancelled its cap and trade program despite knowing the federal backstop program would replace it and "impose[] a higher cost on Ontario taxpayers"[211] and about how the "gap of over three and a half years between the enactment of the Cancellation Act and the operation of the new 'Made-in-Ontario' environmental plan is absurd and strains credulity."[212]

91. All of these allegations are incorrect. First, early in its new term the new Ontario government announced its intention to challenge the constitutionality of the federal backstop program before Canadian courts.[213] As a result, it was far from certain in July 2018 that Ontario "knew" that the federal backstop program would apply in the stead of the cancelled cap and trade program.

92. Second, as explained in Canada's Counter-Memorial, one of the main reasons the Progressive Conservative Party wanted to wind down Ontario's cap and trade program was that it was imposing an inefficient economic burden on Ontarians.[214] Tellingly, the Claimants agree that cap and trade [redacted] and [redacted][215]

93. Third, the *Cancellation Act* required Ontario to establish a new environmental plan and report on progress.[216] Ontario's public servants started working on such plan as early as the fall of 2018.[217] The plan was meant to address environmental issues, including climate change, without imposing undue financial burdens on Ontarians. In July 2019, Ontario made the Greenhouse Gas Emissions Performance Standards regulation that detailed how the EPS program would work and which entities

[210] Claimants' Reply, ¶ 190.

[211] Claimants' Reply, ¶ 190.

[212] Claimants' Reply, ¶ 193.

[213] **R-183**, Government of Ontario News Release, "Ontario Announces Constitutional Challenge to Federal Government's Punishing Carbon Tax Scheme", 2 August 2018.

[214] Canada's Counter-Memorial, ¶ 205.

[215] [redacted]

[216] **R-059**, *Cancellation Act*, c. 13, ss. 4 and 5.

[217] **RWS-1**, Wood – First Witness Statement, ¶ 34; **RWS-3**, Wood – Second Witness Statement, ¶ 31.

would be covered.[218] On September 21, 2020, following extensive discussions with the federal government, Ontario announced that Ontario's EPS program would be accepted as an alternative to the federal output-based pricing system ("OBPS").[219] Ontario's EPS program came into force in January 2022.[220]

III. THE TRIBUNAL DOES NOT HAVE JURISDICTION OVER THE CLAIM

94. The Claimants' claim must be dismissed for lack of jurisdiction. Contrary to the Claimants' suggestion, the Tribunal's jurisdiction cannot be presumed; the Claimants bear the burden of establishing that the Tribunal has jurisdiction to hear its claim (**Section A**). The Claimants have failed to meet their burden because they have not established: that the dispute arises directly out of an "investment" under Article 25 of the ICSID Convention (**Section B**); that KS&T held qualifying "investments" under NAFTA Articles 1139(g) or (h) (**Section C)**; that Koch Industries either holds any "investment" in Canada relevant to this Tribunal's jurisdiction under NAFTA Articles 1101, 1116, and 1139, or has made a *prima facie* damages claim under NAFTA Article 1116 (**Section D**). The Claimants have also failed to established that the Premier-Designate's announcement of June 15, 2018 was a "measure" under NAFTA Article 1101 (**Section E**).

A. The Tribunal's Jurisdiction Cannot be Presumed

95. A mere assertion by a claimant that the jurisdictional requirements of NAFTA Chapter Eleven are met is insufficient to establish the Tribunal's jurisdiction. A claimant must present sufficient evidence of the alleged facts on which jurisdiction rests to prove that a tribunal has jurisdiction. It is well established in international arbitration that, "if jurisdiction rests on the existence of certain facts, they have to be *proven* at the jurisdictional stage."[221]

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[218] **AW-30**, Greenhouse Gas Emissions Performance Standards, O. Reg. 241/19 ("Regulation 241/19").

[219] **AW-12**, Ontario, "Province Welcomes Federal Government's Decision to Accept Made-in-Ontario Emissions Performance Standards", 21 September 2020.

[220] **RWS-3**, Wood – Second Witness Statement, ¶ 33.

[221] **CL-047**, *Phoenix Action, Ltd. v. Czech Republic* (ICSID Case No. ARB/06/5) Award, 15 April 2009 ("*Phoenix Action – Award*"), ¶ 61 (emphasis added).

96. Despite this, the Claimants argue that they "demonstrated that – legally and factually – the Tribunal has *prima facie* jurisdiction."[222] However, a *prima facie* standard does not apply to factual issues upon which a tribunal's jurisdiction depends.[223] As the tribunal in *Phoenix Action v. Czech Republic* stated, "when a particular circumstance constitutes a critical element for the establishment of the jurisdiction itself, such fact must be proven".[224] Thus, the Claimants' attempt to rely on a *prima facie* case for establishing this Tribunal's jurisdiction is incorrect. The Claimants must "positively establish key jurisdictional facts."[225]

97. The Claimants also incorrectly argue that "it is for a respondent to adduce evidence in order to challenge the claimant's substantiated assertion [*sic*] that a tribunal has jurisdiction."[226] A claimant bringing a claim under NAFTA Chapter Eleven bears the burden of proving that it has satisfied the conditions precedent to commencing arbitration and that the tribunal has jurisdiction over the dispute.[227] As the tribunal in *National Gas, S.A.E. v. Egypt* explained, even where a jurisdictional objection is raised by a respondent, "it is not for the Respondent to disprove the Tribunal's

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[222] Claimants' Reply, ¶ 241.

[223] **CL-047**, *Phoenix Action – Award*, ¶ 61. *See also* **RL-132**, *Pac Rim Cayman LLC v. Republic of El Salvador* (ICSID Case No. ARB/09/12) Decision on the Respondent's Jurisdictional Objections, 1 June 2012, ¶ 2.8 ("The application of that 'prima facie' or other like standard is limited to testing the merits of a claimant's case at a jurisdictional stage; and it cannot apply to a factual issue upon which a tribunal's jurisdiction directly depends.")

[224] **CL-047**, *Phoenix Action – Award*, ¶ 64. *See also* **RL-030**, *Apotex Inc. v. United States of America* (ICSID Case No. UNCT/10/2) Award on Jurisdiction and Admissibility, 14 June 2013 ("*Apotex – Award on Jurisdiction and Admissibility*"), fn. 29 (citing *Phoenix Action*, summarising previous decisions, and concluding that "if jurisdiction rests on the existence of certain facts, they have to be proven [rather than merely established prima facie] at the jurisdictional phase.") The NAFTA tribunal in *Gallo* also confirmed that "[i]f jurisdiction rests on the existence of certain facts, these must be proven at the jurisdictional stage - only the alleged violations of the treaty affording jurisdiction (in this case the NAFTA) can be accepted pro tem." *See* **RL-003**, *Vito G. Gallo v. The Government of Canada* (UNCITRAL) Award, 15 September 2011, ¶ 277. *See also* **RL-006**, *Spence International Investments, LLC, Berkowitz, et al. and others) v. Republic of Costa Rica* (ICSID Case No. UNCT/13/2) Interim Award (Corrected), 30 May 2017 ("*Spence – Corrected Interim Award*"), ¶ 239 ("the Tribunal observes that it is for a party advancing a proposition to adduce evidence in support of its case. This applies to questions of jurisdiction as it applies to the merits of a claim, notably insofar as it applies to the factual basis of an assertion of jurisdiction that must be proved as part-and-parcel of a claimant's case.")

[225] **RL-133**, *Nova Scotia Power Incorporated v. Bolivarian Republic of Venezuela* II (ICSID Case No. ARB(AF)/11/1) Excerpts of Award, 30 April 2014 ("*Nova Scotia Power – Excerpts of Award*"), ¶ 50. *See also* **RL-134**, *Air Canada v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB(AF)/17/1) Award, 13 September 2021, ¶ 302 ("At the outset, the Tribunal considers that Claimant must *positively establish* the facts which are intended to prove that an investment has been made in Respondent's territory, while facts which are part of the merits may be provisionally "*accepted at face value*" for the purposes of jurisdiction.") (emphasis added).

[226] Claimants' Reply, ¶ 241.

[227] *See* Canada's Counter-Memorial, ¶¶ 109-111.

jurisdiction."[228] The Claimants must "discharge the burden of proving all essential facts required to establish jurisdiction".[229]

B. The Claimants Have Not Established Jurisdiction Under Article 25 of the ICSID Convention

98. In their Reply, the Claimants deny that they must separately prove that they made an investment under Article 25 of the ICSID Convention, and continue to posit that they have established that they had an "investment" in Ontario. The Claimants' arguments must be rejected because: (1) jurisdiction cannot be presumed under the ICSID Convention; and (2) the Claimants' activities in Ontario do not bear the commonly accepted indicators of an "investment". Accordingly, the Tribunal does not have jurisdiction *ratione materiae* under the ICSID Convention.

1. The Claimants Must Independently Establish that their Activities Meet the Objective Criteria of Article 25

99. Canada and the Claimants agree that the Tribunal's jurisdiction must be established under both Article 25 of the ICSID Convention and NAFTA Chapter Eleven.[230] However, the Claimants argue that the ICSID Convention "does not add any binding requirement regarding the existence of an investment additional to those set out in the NAFTA,"[231] and that "jurisdiction will be presumed to

[228] **RL-005**, *National Gas S.A.E. v. Arab Republic of Egypt* (ICSID Case No. ARB/11/7) Award, 3 April 2014, ¶ 118. *See also* **CL-010**, *Emmis International Holding, B.V., Emmis Radio Operating, B.V., and MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. Hungary* (ICSID Case No. ARB/12/2) Award, 16 April 2014 ("*Emmis – Award*"), ¶ 171 ("If the Claimants' burden of proving [jurisdiction] is not met, the Respondent has no burden to establish the validity of its jurisdictional defences."); **RL-004**, *Tulip Real Estate Investment and Development Netherlands B.V. v. Republic of Turkey* (ICSID Case No. ARB/11/28) Decision on Bifurcated Jurisdictional Issue, 5 March 2013, ¶ 48 ("the Parties agree that whilst the Article 8(2) Objection was raised by Respondent, the onus remains on Claimant to establish that the requirements of Article 8(2) have been satisfied, and that the Tribunal has jurisdiction."); **RL-135**, G Born, 'On Burden and Standard of Proof', in M Kinnear et al (eds), (*Building International Investment Law: The First 50 Years of ICSID*) (Kluwer/ICSID 2016), p. 49 ("Although challenges to the tribunal's jurisdiction will have been initiated by the respondent, it is for the claimant affirmatively to prove that the tribunal has jurisdiction.")

[229] **RL-005**, *National Gas S.A.E. v. Arab Republic of Egypt* (ICSID Case No. ARB/11/7) Award, 3 April 2014, ¶ 118.

[230] Claimants' Memorial, ¶¶ 1, 295, 296 (referring to "[t]he requirement of jurisdiction … *ratione materiae* set out in Article 25(1) of the ICSID Convention"), ¶¶ 318, 328, 335; Claimants' Reply, ¶¶ 234, 243 (alleging that the Claimants made "qualifying investments under the USMCA, and Article 25(1) of the ICSID Convention"), ¶ 357; Canada's Counter-Memorial, ¶ 112.

[231] Claimants' Reply, ¶ 359.

exist" under the ICSID Convention if a claimant has an "investment" within the meaning of the investment agreement under which a claim is brought.[232] Both of these propositions must be rejected.

100. Arbitral tribunals have broadly confirmed that Article 25 is part of a "double barrelled" or "double keyhole" approach to the *ratione materiae* jurisdiction of the Tribunal.[233] For instance, in *Postova Banka v. Greece*, the tribunal observed that tribunals "[i]n a number of well-known cases" have articulated "objective criteria" that "flow from the object and purpose of the ICSID Convention" and that "cannot be set aside by a consent that may have been given in another legal instrument," such as a bilateral investment treaty.[234] Commentators have made similar observations.[235]

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[232] Claimants' Memorial, ¶ 329; Claimants' Reply, ¶ 357.

[233] Canada's Counter-Memorial, ¶¶ 112-115 and fns. 212, 216. *See also* **RL-009**, Christoph Schreuer, "The ICSID Convention: A Commentary", 2nd ed (Cambridge University Press, 2009) ("Schreuer"), p. 117, ¶ 124; **CL-154**, *Československá Obchodní Banka A.S. v. Slovak Republic* (ICSID Case No. ARB/97/4) Decision on Objections to Jurisdiction, 24 May 1999 ("*CSOB – Decision on Jurisdiction*"), ¶ 68; **RL-021**, *Global Trading Resource Corp. and Globex International, Inc. v. Ukraine* (ICSID Case No. ARB/09/11) Award, 1 December 2010, ¶ 43; **RL-136**, *Alps Finance and Trade AG v. Slovak Republic* (UNCITRAL) Award, 5 March 2011 ("*Alps Finance – Award*"), ¶¶ 229, 240; **CL-049**, *KT Asia Investment Group B.V. v. Republic of Kazakhstan* (ICSID Case No. ARB/09/8) Award, 17 October 2013 ("*KT Asia – Award*"), ¶¶ 160, 168; **CL-106**, *Vestey Group Limited v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB/06/4) Award, 15 April 2016 ("*Vestey Group – Award*"), ¶ 187 ("A majority of ICSID tribunals hold that the term 'investment' in Article 25 of the ICSID Convention has an independent meaning."); **RL-137**, *Krederi Ltd. v. Ukraine* (ICSID Case No. ARB/14/17) Excerpts of Award, 2 July 2018, ¶ 243; **RL-138**, *Standard Chartered Bank (Hong Kong) Limited v. United Republic of Tanzania II* (ICSID Case No. ARB/15/41) Award of the Tribunal, 11 October 2019 ("*Standard Chartered Bank – Award*"), ¶¶ 194-195.

[234] **RL-014**, *Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic* (ICSID Case No. ARB/13/8) Award, 9 April 2015 ("*Poštová banka – Award*"), ¶ 353 (emphasis added). *See also* Canada's Counter-Memorial, ¶ 114. The Claimants are incorrect that the tribunal in *Postova Banka v. Greece* "expressly refused to endorse" imposing "objective criteria" additional to the definition in the investment treaty. Claimants' Reply, fn. 528. The tribunal did not "expressly refuse" to apply the objective approach (¶ 351). Instead, it was clear that it "[did] not need to choose" between the approaches because it had decided that the claimants' interests in Greek Government Bonds (GGBs) did not qualify as an "investment" under the BIT (¶ 359). The tribunal thus exercised judicial economy in deciding whether the interests also qualified as an investment under the ICSID Convention. *See generally* ¶¶ 276-277, 349-350. Canada agrees that, if this Tribunal concludes that the Claimants did not hold "investments" in the territory of Canada within the meaning of NAFTA Article 1139, it need not consider the Claimants' claims any further and may exercise judicial economy with respect to the Claimants' allegations under Article 25 of the ICSID Convention. Conversely, if the Claimants did not own "investments" within the meaning of Article 25, the Tribunal need not consider whether the Claimants held investments within the meaning of NAFTA Article 1139.

[235] *See e.g.*, **RL-009**, Schreuer, p. 117, ¶ 124 ("In examining whether the requirements for an 'investment' have been met, *most tribunals* apply a dual test: whether the activity in question is covered by the parties' consent and whether it meets the Convention's requirements.") (emphasis added); **CL-181** Michael Waibel, Subject Matter Jurisdiction: The Notion of Investment, 19 ICSID Reports (2021), p. 28, ¶ 6 ("Investment tribunals have increasingly accepted that the meaning of investment in Article 25 ICSID Convention is objective and cannot be varied by the two parties to a bilateral investment treaty. … Accordingly, ICSID tribunals assess whether a transaction falls within Article 25 ICSID Convention's own notion of 'investment'.")

101. Nor is the existence of an "investment" established under the ICSID Convention simply because a tribunal has found that an investment exists under the investment agreement at issue. The tribunal in *CSOB v. Slovakia* made precisely this point, finding that the parties' agreement that their transaction was an investment in that case was not conclusive for the purposes of deciding whether the dispute involves an investment under Article 25.[236] The parties could not submit a dispute to ICSID that did not arise directly out of an investment. Accordingly, the Claimants must independently establish that they hold an "investment" within the meaning of Article 25 of the ICSID Convention.

2. The Claimants' Activities Do Not Meet the Objective Criteria of Article 25

102. In their Memorial, the Claimants put forward four "commonly-accepted requirements for an 'investment' under the ICSID Convention": (1) contribution of money or assets; (2) of a certain duration; (3) an element of risk; and (4) a contribution to the economic development of the host State.[237] In their Reply, the Claimants argue that these characteristics are not "relevant".[238] However, arbitral tribunals "have applied these criteria in numerous cases", referring to them as "basic features", "characteristics", "hallmarks" or "indicative elements" of an "investment".[239] Tribunals

[236] **CL-154**, *CSOB – Decision on Jurisdiction*, ¶ 68: ("[A]n agreement of the parties describing their transaction as an investment is not, as such, conclusive in resolving the question whether the dispute involves an investment under Article 25(1) of the Convention. The concept of an investment as spelled out in that provision is objective in nature in that the parties may agree on a more precise or restrictive definition of their acceptance of the Centre's jurisdiction, but they may not choose to submit disputes to the Centre that are not related to an investment.") *See also* **CL-041**, *Joy Mining Machinery Limited v. The Arab Republic of Egypt* (ICSID Case No. ARB/03/11) Award on Jurisdiction, 6 August 2004, ¶ 50; **RL-139**, *RSM Production Corporation v. Grenada I* (ICSID Case No. ARB/05/14) Award, 13 March 2009, ¶ 235.

[237] Claimants' Memorial, ¶ 330, citing **CL-039**, *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco [I]* (ICSID Case No. ARB/00/4) Decision on Jurisdiction, 23 July 2001 ("*Salini – Decision on Jurisdiction*"), ¶ 52. *See also* Claimants' Reply, ¶¶ 357, 364.

[238] Claimants' Reply, ¶¶ 365-366 ("[E]ven if such criteria were binding or even relevant (they are not), the Claimants' investments meet the 'Salini characteristics'").

[239] **CL-152**, Dolzer, pp. 91-92. *See* **RL-015**, *Patrick Mitchell v. Democratic Republic of Congo* (ICSID Case No. ARB/99/7) Decision on the Application for Annulment of the Award, 1 November 2006, ¶ 27; **CL-046**, *Saipem S.p.A. v. The People's Republic of Bangladesh* (ICSID Case No. ARB/05/07) Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007 ("*Saipem – Decision on Jurisdiction*"), ¶ 99; **RL-016**, *Ioannis Kardassopoulos v. The Republic of Georgia* (ICSID Case No. ARB/05/18) Decision on Jurisdiction, 6 July 2007, ¶ 116. Even in *Biwater Gauff v. Tanzania*, a decision cited in the Claimants' Reply, ¶ 361, the tribunal opted for an approach that "takes into account the features identified in *Salini*, but along with all the circumstances of the case". ***See*** **RL-121**, *Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania* (ICSID Case No. ARB/05/22) Award, 24 July 2008 ("*Biwater Gauff – Award*"), ¶ 316.

have repeatedly concluded that the term "investment" has an inherent meaning[240] that differentiates it from other commercial transactions, such as cross-border sale of goods.[241] The Claimants have failed to establish that their activities possess the inherent characteristics of an "investment" under Article 25 of the ICSID Convention.[242]

(a) KS&T Did Not Contribute Money or Assets to an Economic Venture in Ontario

103. KS&T's activities do not qualify as a contribution of money or assets to an economic venture in Ontario.[243] The evidence establishes that KS&T, a Delaware entity with no presence in Canada and whose business decisions were taken in the United States, merely paid money in exchange for emission allowances that were repeatedly transferred to KS&T's California CITSS account for resale.[244]

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[240] **RL-140**, *Raymond Charles Eyre and Montrose Developments (Private) Limited v. Democratic Socialist Republic of Sri Lanka* (ICSID Case No. ARB/16/25) Award, 5 March 2020 ("*Eyre – Award*"), ¶ 293; **RL-141**, *Masdar Solar & Wind Cooperatief U.A. v. Kingdom of Spain* (ICSID Case No. ARB/14/1) Award, 16 May 2018 ("*Masdar Solar – Award*"), ¶ 196; **RL-142**, *MNSS B.V. and Recupero Credito Acciaio N.V. v. Montenegro* (ICSID Case No. ARB(AF)/12/8) Award, 4 May 2016 ("*MNSS – Award*"), ¶ 189; **RL-133**, *Nova Scotia Power – Excerpts of Award*, ¶¶ 81, 84; **RL-136**, *Alps Finance – Award*, ¶ 241.

[241] **CL-151**, Rudolf Dolzer and Christoph Schreuer, "Principles of International Investment Law", OUP, 2nd ed (2012), pp. 75-76 ("[T]he ordinary meaning of 'investment' refers to an economic transaction which is different from a trade transaction, both from the viewpoint of general usage and from the vantage point of international legal terminology."); **RL-143**, Nigel Blackaby et al., "Redfern and Hunter on International Arbitration", 6th ed (Kluwer Law International, 2015) ("Blackaby"), ¶ 8.38 ("[I]t is often noted that a simple contract for the sale of goods, without more, could not qualify as an investment under Article 25 of the Convention, even if this were the subject of an agreement by the parties."); **CL-159**, *SGS Société Générale de Surveillance SA v. The Republic of Paraguay* (ICSID Case No. ARB/07/29) Decision on Jurisdiction, 12 February 2010, ¶ 93; **RL-138**, *Standard Chartered Bank – Award*, ¶ 194; **CL-130**, *Tenaris S.A. and Talta - Trading e Marketing Sociedade Unipessoal Lda. v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB/11/26) Award, 29 January 2016, ¶ 291; **RL-133**, *Nova Scotia Power – Excerpts of Award*, ¶¶ 82, 113; **CL-156**, *Ambiente Ufficio SPA and Others (Case formerly known as Giordano Alpi and Others) v. Argentine Republic* (ICSID Case No. ARB/08/9) Decision on Jurisdiction and Admissibility, 8 February 2013, ¶ 470; **RL-136**, *Alps Finance – Award*, ¶¶ 231-232, 238 and 245.

[242] Canada's Counter-Memorial, ¶¶ 117-130.

[243] Canada explained in its Counter-Memorial that, in order to constitute an "investment", a contribution of money or assets must be "to an economic venture" in the host State. *See* Canada's Counter-Memorial, ¶ 118, citing **RL-014**, *Poštová banka – Award – Award*, ¶ 361 ("If an 'objective' test is applied, in the absence of a contribution to an economic venture, there could be no investment. An investment, in the economic sense, is linked with a process of creation of value, which distinguishes it clearly from a sale") and fn. 506 ("In a sale there is also a contribution of goods or services by the seller and a contribution of money by the buyer, but this is different from the contribution to an economic venture required in order to find an investment.").

[244] Canada's Counter-Memorial, ¶¶ 119-122; Canada's Rejoinder, Sections II.B and II.C.

104. The Claimants object to this conclusion, claiming that the *Postova Banka v. Greece* tribunal's differentiation between a contribution to an economic venture and a sale, on which Canada relies, was "*obiter dicta*".[245] However, several tribunals, citing *Postova Banka v. Greece*, have drawn this distinction, and held that the term "investment" presupposes "a contribution *to an economic venture* of a certain duration implying an operational risk".[246] The tribunal in *MNSS v. Montenegro* further recognized that, while reciprocal commitments in a sales contract "can, strictly speaking, be classified as contributions; some more precision needs to be given to the kind of contribution that qualifies as an investment for purposes of the ICSID Convention."[247] The Claimants have failed to establish that KS&T's activities constitute the kind of contribution that qualifies as an investment under the ICISD Convention.

105. While the Claimants argue that it is "simply incorrect" that KS&T was "simply a cross-border trader",[248] their own documents belie their position.[249] KS&T consistently transferred the emission allowances it purchased through its Ontario CITSS account to its California account [redacted] [50] KS&T's Vice President confirmed that [redacted][251] KS&T similarly intended to transfer all of the emission allowances it acquired in the May 2018 joint auction to California. The fact that [redacted]

[245] Claimants' Reply, ¶¶ 369-370.

[246] **RL-140**, *Eyre – Award*, ¶¶ 293-294 (emphasis added); **RL-141**, *Masdar Solar – Award*, ¶ 199 (emphasis added); **RL-142**, *MNSS – Award*, ¶ 189 (emphasis added); all citing **RL-014**, *Poštová banka – Award – Award*, ¶¶ 361 or 371. *See also* **RL-138**, *Standard Chartered Bank – Award*, ¶ 220 (holding that "loans and financial instruments standing alone without any link to some economic venture intended to provide for the improvement of the State's development would not be considered an 'investment.'"); **RL-142**, *MNSS – Award*, ¶ 196.

[247] **RL-142**, *MNSS – Award*, ¶ 196.

[248] Claimants' Reply, ¶ 371.

[249] *See* Canada's Rejoinder, Sections II.B and II.C.

[250] Canada's Rejoinder, ¶¶ 39-43, 5-56. KS&T participated in four auctions in 2017, [redacted] *See* Canada's Counter-Memorial, ¶ 57. [redacted]

[251] [redacted]

[redacted][252] does not change the nature of KS&T's activities in Ontario, and does not make KS&T's purchase of emission allowances [redacted] the kind of contribution contemplated by Article 25 of the ICSID Convention.

106. Contrary to the Claimants' arguments,[253] the absence of a physical presence or business infrastructure in Ontario further confirms that KS&T was not contributing to an economic venture in Ontario. The evidence is also clear that KS&T's business model was to regularly and promptly transfer emission allowances from Ontario to California for subsequent resale, and all decisions regarding KS&T's "business in Ontario" were made and implemented from the United States.[254] KS&T had no expectations for the only Ontario resident involved in its alleged "business in Ontario".[255] KS&T's alleged "emission allowances business" was thus not in Ontario, and the Claimants have not provided evidence of any other kind of economic venture in Ontario.

107. The Claimants' final efforts to overcome the evidence that KS&T was not contributing to an economic venture in Ontario overstate its role as a market participant in Ontario's cap and trade program[256] and KS&T's secondary market activity in Ontario.[257] Not only is their emphasis on the role of market participants rejected by a leading expert in cap and trade design,[258] but the Claimants have not identified any transfers of compliance instruments that KS&T made in its capacity as an Ontario-registered market participant beyond the [redacted] that Canada discussed in its Counter-

[252] Canada's Rejoinder, ¶¶ 5, 56.

[253] Claimants' Memorial, ¶ 371. *See also* Claimants' Reply, ¶ 371, acknowledging that KS&T did not have "a 'bricks and mortar' presence in Ontario"; **CWS-2**, Martin – First Witness Statement, ¶ 20 (referring to KS&T "establishing the necessary infrastructure to acquire Ontario allowances by registering a CITSS account in Ontario and complying with all procedural mandates required by the Province"), and ¶ 30 (referring to "the significant amount of time KS&T spent building the infrastructure necessary to participate in the Ontario Program".).

[254] Canada's Rejoinder, ¶¶ 32-38; Canada's Counter-Memorial, ¶¶ 119-120.

[255] Canada's Rejoinder, ¶ 35. Indeed, KS&T's Vice President Mr. Martin anticipated that Mr. Brown, KS&T's nominal PAR, [redacted]

[256] Claimants' Reply, ¶¶ 368, 371 (alleging that KS&T made "vital contributions" to the "effective" and "smooth" functioning of Ontario's cap and trade program).

[257] Claimants' Reply, ¶ 371 (arguing that they have "completely discredited" Canada's conclusion that KS&T's participation in the secondary market in Ontario amounted to [redacted]. *See* Canada's Counter-Memorial, ¶¶ 51, 64, 121.

[258] Canada's Counter-Memorial, ¶¶ 37-39, 121-122; **RER-2**, Litz – First Expert Report, ¶ 66, 69, 77-83, 87, 89, 117; Canada's Rejoinder, ¶¶ 21-26; **RER-4**, Litz – Second Expert Report, ¶¶ 23-24.

Memorial.[259] KS&T's activity on the secondary market outside of Ontario – [redacted] – is not evidence of KS&T's "investment" in Ontario.[260] To the contrary, its transaction in compliance instruments and [redacted] which did not generate revenue for Ontario, do not constitute contributions to an economic venture in Ontario.[261]

(b) KS&T's Activities in Ontario Were Inherently Short-Term

108. The Claimants have not established that KS&T's activities in Ontario were of a "certain duration".[262] To the contrary, KS&T's activities in Ontario were inherently short-term and did not constitute an "investment". [263] The Claimants attempt to downplay the duration criterion by arguing that "no investment tribunal thus far has ever found that a transaction does not qualify as an investment based solely on the absence of a long-term transfer of financial resources."[264] But several tribunals have concluded that the transaction at issue did not constitute an "investment" because, among other factors, it lacked the requisite duration.[265]

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[259] Canada's Counter-Memorial, ¶¶ 47, 51, 65; Canada's Rejoinder, ¶¶ Section II.B.3.

[260] Canada's Rejoinder, Section II.B.3. The Claimants try to distinguish this case from *Postova Banka v. Greece*, where the dispute concerned "sovereign bonds that were purchased on the secondary market, outside of the territory of the respondent State, with payments made only to third parties rather than to the respondent State". *See* Claimants' Reply, ¶ 370. At the same time, the Claimants argue that KS&T had an "investment" in Ontario because it [redacted] and traded in compliance instruments on the secondary market [redacted]

[261] *See e.g.*, **RL-136**, *Alps Finance – Award*, ¶ 236. *See also* ¶¶ 229, 238, 243 (referring to a dispute as "being based on a purely speculative transaction deprived of any significant economic activity in the host country"), and concluding that (the claimant's acquisition of receivables from a Slovak business was "a private, neutral and speculative business, having no impact on the State economy" and thus did not constitute an "investment" in Slovakia.)

[262] Claimants' Memorial, ¶ 330(2); Claimants' Reply, ¶¶ 357(2), 364(2).

[263] Canada's Counter-Memorial, ¶¶ 123-124. Several tribunals and commentators have indicated that an "investment" requires a duration of two to five years. *See* Canada's Counter-Memorial, ¶ 123 and fns. 232 and 235-236.

[264] Claimants' Reply, ¶ 375 (emphasis added).

[265] *See e.g.*, **CL-049**, *KT Asia – Award*, ¶¶ 210 and 215-216 (agreeing that "no matter how long the duration is in practice, the investment must be held with the expectation of some long-term relationship" and concluding that the claimant's "alleged investment did not involve the kind of duration envisaged within the meaning of an 'investment' under the ICSID Convention". In that case, "the investment was supposed to last a very short period of time" as the claimant "was to hold the shares of BTA for a period of weeks ('at least 3/4') before they were sold on to investors in a private placement."); **RL-020**, *Romak S.A. (Switzerland) v. The Republic of Uzbekistan* (UNCITRAL) Award, 26 November 2009, ¶ 227 (finding that the duration of the claimant's wheat deliveries, which spanned a five-month period, "does not reflect a commitment on the part of [the claimant] beyond a one-off transaction, and is not of the sort normally associated with 'investments' according to the common understanding of the term."). In *Bayindir v. Pakistan*, a case relied on by

109. The Claimants' attempts to cast KS&T's "investment" in Ontario as occurring "over a period of three years (2016 to 2018, well within the 'two to five years' Canada asserts)"[266] must also be rejected. The first auction in which KS&T participated – and paid a purchase price for emission allowances – took place on March 22, 2017; the last – on May 15, 2018 – was less than 14 months later.[267] Each auction was a separate event; participating in one did not entitle or require KS&T to participate in any subsequent auctions, nor was it a guarantee of success.[268]

110. KS&T's "standard practice" of moving the emission allowances it purchased in individual auctions from its Ontario CITSS account to its California CITSS account [redacted] confirms the short-term nature of its cross-border trading activity.[269] The joint auction of May 2018 was no exception. [redacted][270] This short duration is indicative of KS&T's involvement in cross-border trading, not making an "investment" in Ontario.

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the Claimants (*see* Claimants' Memorial, fn. 424; Claimants' Reply, fn. 567), the tribunal emphasized that ("[t]he element of duration is the *paramount factor* which distinguishes investments within the scope of the ICSID Convention and ordinary commercial transactions.") *See* **CL-045**, *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan* (ICSID Case No. ARB/03/29) Decision on Jurisdiction, 14 November 2005 ("*Bayindir – Decision on Jurisdiction*"), ¶ 132 (emphasis added). In *Bayindir*, the impugned contract had an initial duration of three years followed by a defect liability period of one year and a maintenance period of four years. The tribunal concluded that the duration requirement was met as the respondent "ha[d] not contended that the project was not sufficiently extended in time to qualify as an investment". *See* **CL-045**, *Bayindir – Decision on Jurisdiction*, ¶ 133.

[266] Claimants' Reply, ¶ 376 (emphasis added). Throughout their Reply, the Claimants describe the duration of their alleged investment as "two years" (¶¶ 4, 51), "full two years" (¶¶ 62, 321) "several years" (¶¶ 18, 62, 315, 373, 539), or as a "two-year" (¶¶ 301, 383), "three-year" (¶ 48) or "multi-year" period (¶¶ 4, 47).

[267] Canada's Rejoinder, ¶ 55. *See also* **CL-049**, *KT Asia – Award*, ¶ 214 (pointing out that the time from the acquisition of the shares until the request for arbitration "would only be 16 months, which is a very short time if one remembers the five years tentatively put forward in the course of the elaboration of the ICSID Convention.")

[268] **RWS-4**, Ramlal – Second Witness Statement, ¶¶ 32-34. [redacted] *See* Claimants' Memorial, ¶ 148; [redacted]

[269] Canada's Rejoinder, ¶¶ 39-43; [redacted]

[270] Canada's Rejoinder, ¶ 56; [redacted]

111. The Claimants assert that, but for Ontario's cancellation of its cap and trade program, KS&T's alleged investment would have "continued for at least a decade longer, until at least 2030, and possibly even further to 2050"[271] and that KS&T's activities were part of a "complex", "sustained", "long-term business plan".[272] However, the Claimants produced neither the alleged business plan nor any evidence to support their alleged intention to continue trading in emission allowances "until at least 2030".

(c) KS&T's Activities in Ontario Involved Risks Inherent in Cross-Border Sales Transactions, Not Risks Inherent in Operating an Economic Venture in Ontario

112. In their Reply, the Claimants try to downplay the importance of "risk", and present a circular argument that "ICSID tribunals have been clear that an element of risk is inherent in any long-term investment."[273] Because "any long-term investment" inherently involves "an element of risk", they claim, it is an "investment" for the purposes of Article 25 of the ICSID Convention. The cases the Claimants cite[274] merely found that long-term *construction projects* may constitute an "investment".[275] KS&T's alleged "business in Ontario" involved no physical presence in Ontario, and thus did not carry the types of risk inherent in construction contracts due to the presence of materials, equipment and personnel in the host State and the inherently illiquid nature of construction projects.[276]

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[271] Claimants' Reply, ¶¶ 301, 377.

[272] Claimants' Memorial, ¶ 323(a); Claimants' Reply, ¶ 299, 302, 315, 539.

[273] Claimants' Memorial, ¶ 333; Claimants' Reply, ¶ 381 (emphasis added).

[274] Claimants' Memorial, fn. 424; Claimants' Reply, fn. 567.

[275] In *Salini v. Morocco*, the dispute concerned a three-year highway construction contract and thus involved "construction that stretches out over many years, for which the total cost cannot be established with certainty in advance". **CL-039**, *Salini – Decision on Jurisdiction*, ¶ 56. The total duration for the performance of the contract was fixed at 32 months, later extended to 36 months. *See* **CL-039**, *Salini – Decision on Jurisdiction*, ¶ 54. In *Bayindir v. Pakistan*, a highway construction contract had an initial duration of three years followed by a one-year defect liability period and a four-year maintenance period. *See* **CL-045**, *Bayindir – Decision on Jurisdiction*, ¶¶ 133, 136. In *Saipem v. Bangladesh*, the dispute concerned a pipeline construction project that lasted two and a half years. *See* **CL-046**, *Saipem – Decision on Jurisdiction*, ¶¶ 7, 11-12, 100, 109.

[276] Had KS&T been building a highway or a pipeline in Ontario, it would not have been able to move its construction project to California. In contrast, it was KS&T's standard practice to transfer allowances from its Ontario CITSS account to its California CITSS account.

113. This case is more analogous to the situation that arose in *NSPI v. Venezuela*, where the dispute concerned the claimant's contractual rights to receive coal from a mine in Venezuela.[277] There, the tribunal considered that "the type of risk required for an investment" was not present because the claimant had not "established lasting infrastructure in Venezuela that was at the mercy of the government" and could manage the risks by, for instance, invoking the force majeure clause in the contract.[278] Similarly, it is clear that KS&T: (1) had no "lasting infrastructure" in Ontario; (2) decided to participate in the May 2018 auction as an Ontario-registered market participant rather than as a California-registered market participant [redacted] [79] (3) intended to promptly transfer the emission allowances it acquired at the May 2018 auction to California;[280] and (4) could manage, through contractual means, the risks involved in its cross-border sales transactions – such as the risk that KS&T would be unable to deliver compliance instruments under the contract due to a termination of a cap and trade program.[281]

114. Nonetheless, in their Reply, the Claimants allege that they "exposed themselves to financial risk" in four ways.[282] None withstands scrutiny. First, there is no evidence that KS&T was exposed to significant "financial risk" when it took "all steps necessary to open a CITSS account and qualify as an Ontario-registered market participant".[283] [redacted] KS&T was not required to pay annual fees, bid at auctions, or enter into any transactions on the secondary market.

[277] **RL-133**, *Nova Scotia Power – Excerpts of Award*, ¶¶ 1, 90.

[278] **RL-133**, *Nova Scotia Power – Excerpts of Award*, ¶ 111.

[279] Canada's Rejoinder, Sections II.B and II.C.

[280] Canada's Counter-Memorial, ¶¶ 322-324; Canada's Rejoinder, Section II.C.

[281] For instance, the [redacted] contemplated a situation where KS&T is unable to deliver compliance instruments to FHR "due to a change in Applicable Law that terminates or suspends indefinitely the Program". *See* **C-073**, [redacted] The Claimants have not provided a convincing explanation as to why KS&T did not invoke this provision in the [redacted] *See also* Canada's Counter-Memorial, fn. 572.

[282] Claimants' Reply, ¶ 383.

[283] Claimants' Reply, ¶ 383.

115. Second, the only risk involved in KS&T's secondary market transactions[284] was that its counterparty would not perform the contract. This is a "pure commercial, counterparty risk",[285] and not the type of risk involved in operating an economic venture in Ontario.[286]

116. Third, the Claimants' reliance on KS&T's participation in six emission allowance auctions[287] fails to identify any risks beyond those inherent in a sale and purchase transaction. KS&T freely chose how it would bid at auctions (i.e. the purchase price and the number of allowances it wished to acquire) and, once auction results were certified, the participating jurisdictions delivered emission allowances to successful bidders. KS&T repeatedly moved the emission allowances it purchased at auction to its California CITSS account, and intended to do so again after the May 2018 auction.

117. Fourth, the Claimants' allegation that KS&T [redacted] again exaggerates KS&T's involvement in Ontario's cap and trade program. The "gains" [redacted] The Claimants cannot claim both that "the price of emissions allowances is expected to increase over time"[290] and that their strategy of purchasing allowances for transfer to California involved the types of risk inherent in an "investment" in Ontario.

[284] Claimants' Reply, ¶ 383 (claiming that KS&T "transact[ed] on the secondary market using its Ontario CITSS account").

[285] Canada's Counter-Memorial, ¶¶ 126-127, and fn. 239.

[286] Moreover, between January 1, 2017 and July 3, 2018, KS&T made only *two* transfers of emission allowances from its Ontario CITSS account (excluding transfers from KS&T's Ontario CITSS account to California). Canada's Counter-Memorial, ¶¶ 47, 51, 65; Canada's Rejoinder, Section II.B.3.

[287] Claimants' Reply, ¶ 383.

[288] Claimants' Reply, ¶ 383, citing **CWS-2**, Martin – First Witness Statement, ¶ 17, and **CWS-4**, King – First Witness Statement, ¶ 20.

[289] **CWS-4**, King – First Witness Statement, ¶ 20.

[290] Claimants' Memorial, ¶ 27. *See* **CER-2**, Stavins – Second Expert Report, fn. 55.

(d) KS&T Did Not Make a "Substantial" Contribution to the Economic Development of Canada

118. Finally, the Claimants continue to argue that KS&T "contributed substantially to Canada's economic development" because "investments like KS&T's raised a total of CAD 2.9 billion for Ontario."[291] In their Reply, they also refer repeatedly to "USD 368 million" that Ontario received in proceeds from the sale of all of the emission allowances it offered for sale in the May 2018 joint auction.[292] The Claimants' attempts to establish *KS&T*'s alleged contribution to the economic development in Ontario on the basis that *others* (mostly capped participants)[293] bought emission allowances through auctions must be rejected. KS&T knew that successful bidders in a joint auction would acquire a mixture of each jurisdiction's emission allowances in proportion to each jurisdiction's contribution to the auction.[294] Ontario received only [redacted] for the emission allowances that KS&T purchased in the May 2018 auction – [redacted] of Ontario's share of the proceeds from the May 2018 auction.[295]

119. More importantly, KS&T's transfers of [redacted] allowances *to California* in January-May 2018,[296] with an intention to transfer an additional [redacted] allowances in June 2018, did not contribute substantially to economic development *in Ontario*. Nor did KS&T's [redacted] transactions on the secondary market in Ontario over the period of 18 months ([redacted]

[291] Canada's Counter-Memorial, ¶ 128; Claimants' Memorial, ¶ 334.

[292] Claimants' Reply, ¶¶ 14, 228, 232, 328, 388. Canada does not contest the accuracy of the figures cited in Ontario's post-auction public proceeds reports. Claimants' Reply, ¶ 388 and fn. 580.

[293] **RWS-4**, Ramlal – Second Witness Statement, ¶¶ 35-36.

[294] Canada's Counter-Memorial, ¶ 61; Canada's Rejoinder, Section II.C.

[295] Canada's Counter-Memorial, ¶ 64.

[296] Claimants' Memorial, ¶ 9, 183, 287, and Claimants' Reply, ¶¶ 48, 51, 301, 368, 383, refer to KS&T paying "a total of USD [redacted]" for the emission allowances in purchased at auctions in 2017-2018. The Claimants, however, ignore the fact that KS&T moved to its California CITSS account all of these emission allowances with the exception of [redacted] *See* **RWS-2**, Ramlal – First Witness Statement, Attachment 1, [redacted]

[redacted]

make a considerable contribution to "increased fluidity"[297] of the cap and trade program.

120. In sum, the Claimants have not established that their business activities bear the characteristics of an "investment" under Article 25 of the ICSID Convention: (1) KS&T did not contribute money or assets to an economic venture in Ontario; (2) its activities in Ontario were inherently short-term; (3) its activities involved risks characteristic of cross-border sales transactions rather than of an investment; and (4) KS&T's alleged contribution to economic development of Ontario was far from "substantial". As a result, this Tribunal does not have jurisdiction *ratione materiae* and the Claimants' claim must be dismissed.

C. The Claimants Have Not Established Jurisdiction with Respect to KS&T Under NAFTA Chapter Eleven

121. The Claimants have also failed to meet their burden to establish that the Tribunal has jurisdiction *ratione materiae* with respect to KS&T's alleged investments under NAFTA Chapter Eleven. Canada explains in the sections that follow that the Tribunal does not have jurisdiction over KS&T's claims because: (1) the emission allowances KS&T held in its Ontario CITSS account do not qualify as "property" under NAFTA Article 1139(g); and (2) despite the shifting parameters of KS&T's alleged "investment", neither the emission allowances nor KS&T's alleged "trading business in Ontario" qualify as interests arising from the commitment of capital or other resources in the territory of Ontario under NAFTA Article 1139(h).

1. Emission Allowances Held by KS&T Were Not "Property" Under NAFTA Article 1139(g)

122. In order for them to qualify as an "investment" under NAFTA Article 1139(g), the Claimants must establish that emission allowances constitute "real estate or other property, tangible or intangible property, acquired in the expectation or used for the purposes of economic benefit or other business purposes".[298] The disputing parties agree that what constitutes "property" for the purposes of

[297] Claimants' Reply, ¶ 389.

[298] Canada's Counter-Memorial, ¶¶ 133-138; Claimants' Reply, ¶ 247.

Article 1139(g) must be determined by reference to the relevant domestic law, in this case Ontario,[299] and that no Ontario court has confronted the question of whether emission allowances constitute property in Ontario.[300]

123. Nonetheless, the Claimants merely asserted that the emission allowances KS&T held constituted "property", and referred to a single domestic law case from a foreign jurisdiction in its Memorial.[301] With their Reply, the Claimants have filed two expert reports they view as bearing on the question of whether emission allowances are property in Ontario. Each is flawed. Professor de Beer purports to predict with certainty what a hypothetical Ontario court would decide,[302] and presents an oversimplified "legal test" that he draws from only two Canadian cases in which the interests in question were found to constitute property.[303] Mr. Mehling's report is based on an incorrect instruction about the role of "international practice" in an Ontario court's analysis and draws incorrect or speculative conclusions about the intention of Ontario's legislators.[304]

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[299] Claimants' Reply, ¶ 248. *See also* Canada's Counter-Memorial, ¶ 136; **RL-024**, *Lion Mexico Consolidated L.P. v. United Mexican States* (ICSID Case No. ARB(AF)/15/2) Decision on Jurisdiction, 30 July 2018 ("*Lion Mexico – Decision on Jurisdiction*"), ¶¶ 231-234 (finding that mortgages qualified as an investment under NAFTA Article 1139(g) by examining the municipal law of the host state and concluding that the municipal law "explicitly and unequivocally" included the impugned interests as "intangible real estate.") Despite the Claimants' agreement that the Tribunal must look to Ontario law to answer this question, they propose that "international law has considered that 'property' should be given expansive content." *See* Claimants' Reply, ¶ 248. Their position is unsupported. Each of the cases referred to by the Claimants (**CL-020**, *Grand River Enterprises Six Nations, Ltd., et al. v. United States of* America (UNCITRAL) Award, 12 January 2011 ("*Grand River – Award*"); **CL-148**, *Starrett Housing Corp. v. Islamic Republic of Iran*, 4 Iran-U.S. Cl. Trib. Rep. 122 (1983); **CL-096** *Amoco International Finance Corp v Iran* (1987) 15 Iran-USCTR 189, 220; and **CL-147** *Phillips Petroleum Iran v. Islamic Republic of Iran and National Iranian Oil Company*, 21 Iran-U.S. Cl. Trib. Rep. 106 (1989) ("*Phillips Petroleum*")), involved a locally established enterprise with a physical presence in the host state, which is not the case here. Furthermore, in the Iran-US claims context, as relevant to *Starett, Amoco, and Phillips Petroleum*, the tribunals considered a distinct treaty text that, unlike NAFTA Article 1139(g), refers to both "property" and "interests in property", and that directly informed the tribunals' decisions (*see e.g.*, **CL-147**, *Phillips Petroleum*, ¶¶ 104-105, finding that a contractual right qualified as "interests in property", rather than "property").

[300] Claimants' Reply, ¶ 248.

[301] Claimants' Memorial, ¶ 323 (c) (referring exclusively to the UK High Court decision, **R-072**, *Armstrong DLW GmbH v Winnington Networks Ltd*, decided in a non-analogous context). *See also* Claimants' Reply, ¶ 261.

[302] **CER-3**, Expert Report of Prof. Jeremy de Beer, 15 July 2022 ("Prof. de Beer – Expert Report"), ¶¶ 30, 213.

[303] *See* **RER-3**, Katz – Second Expert Report, ¶ 14. Professor de Beer fails to acknowledge the significance of the specific and limited contexts of the property analyses carried out in those cases, as answering the question for specific statutory purposes. *See* **CER-3**, Prof. de Beer – Expert Report, ¶¶ 34-35, 88-89, **RER-3**, Katz – Second Expert Report, ¶¶ 14; 17-18. Professor Katz sets out a number of additional flaws in Profesor de Beer's methodology in her second expert report. *See* **RER-3**, Katz – Second Expert Report, ¶¶ 13-24.

[304] **CER-4**, Expert Report of Prof. Michael Mehling, 15 July 2022, ¶¶ 7, 9, 65.

124. Ontario property law expert, Professor Katz, sets out in her first and second reports the proper approach that an Ontario court would follow when confronted with a novel property claim like this one. Despite the Claimants' attempt to portray Professor Katz's approach as "an idiosyncratic theoretical framework,"[305] her approach is firmly grounded in the applicable case-law,[306] which, unlike Professor de Beer's, draws from the full range of relevant cases.[307] An Ontario court approaching a novel claim to property would proceed through three stages of analysis:[308]

> **Stage One:** A court would determine if there is a legislative declaration or judicial decision that adds the interest at issue to the category of property rights.
>
> **Stage Two:** A court would examine the nature and character of the interest in question. If it is a statutorily created interest, the court would consider the statutory and regulatory context in which the interest is created to determine its core characteristics.
>
> **Stage Three:** A court would consider whether the interest, given its nature and character, has the common law characteristics of property in common law or sufficient attributes of property in common law for the purposes of a particular statute that expands or narrows the common law definition.

125. Below, Canada demonstrates at Stage One that emissions allowances do not currently have the legal status of property in Ontario.[309] This should settle the matter for the Tribunal. However, should the Tribunal find it necessary to proceed further, Stage Two requires an accurate description of the nature and character of emission allowances. A review of their creating statute demonstrates that emission allowances were non-compensable regulatory interests, intended to accomplish the

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[305] Claimants' Reply, ¶ 250. *See also* Claimants' Reply, ¶¶ 17, 23, 249, 253, 263, 295. The Claimants argue that Professor Katz's "chosen theoretical framework" is "Hofeldian analysis." (*See* Claimants' Reply, ¶¶ 255-257, 265). Despite the Claimants' mischaracterization, Professor Katz's analysis is not based on a "Hohfeldian analysis", but on the practical approach an Ontario court would employ, as drawn from the relevant case-law authorities. To the extent Professor Katz refers to "Hofeldian" concepts, she does so to demonstrate their use as helpful analytical "tools." She explains that, "Hohfeldian concepts are analytical tools adopted by Canadian property scholars and courts in analyzing legal interests." *See* **RER-3**, Katz – Second Expert Report, fn. 56. Such tools are well accepted by courts and respected property scholars in Canada, the US and the UK (*See* **RER-3**, Katz – Second Expert Report, fn. 68.)

[306] **RER-3**, Katz – Second Expert Report, ¶ 12.

[307] This includes cases that address novel property claims in both statutory and non-statutory contexts. *See* **RER-3**, Katz – Second Expert Report, ¶¶ 13-24; 82-90.

[308] **RER-3**, Katz – Second Expert Report, ¶¶ 4, 12.

[309] **RER-3**, Katz – Second Expert Report, ¶ 35.

purposes of the *Climate Change Act*.[310] Finally, under a hypothetical Stage Three analysis, given their nature and character, the interests created by Ontario as emission allowances lacked hallmark indicia of common law property, most notably exclusive control and use.[311] As a result, the Claimants have failed to establish that emission allowances created under the *Climate Change Act* are "property" under the relevant municipal law, and KS&T's "investment" in emission allowances falls outside the scope of NAFTA Article 1139(g).[312]

(a) Emission Allowances Are Not Property Rights in Ontario Because They Have Not Been Added to the Category of Property

126. The Claimants and Professor de Beer agree that the *Climate Change Act* did not declare emission allowances to be property and that there has not been judicial recognition of emission allowances as property rights in Ontario.[313] These facts bear on the current legal status of emission allowances: they are not currently property, because they have not yet been added to the category of property in Ontario.[314] The Claimants' attempts to avoid this conclusion are unavailing.

127. First, Professor de Beer asserts that the legal status of an interest is "conferred" by its creating statute, and that courts merely "confirm such status which already did or did not exist."[315] However, his position denies the important judicial role in determining the legal status of novel interests as property rights.[316] Absent a legislative declaration, an Ontario court's role is to determine "whether to add a statutorily created interest to the category of property rights."[317] Novel claims to property

[310] **RER-3**, Katz – Second Expert Report, ¶¶ 36-51.

[311] **RER-3**, Katz – Second Expert Report, ¶¶ 9, 54-64.

[312] Canada's Counter-Memorial, ¶¶ 133-151.

[313] Claimants' Reply, ¶ 248, **CER-3**, Prof. de Beer – Expert Report, ¶¶ 31, 51, 80. *See also* **RER-3**, Katz – Second Expert Report, ¶¶ 6; 11-12; 25-28. This is what makes a property claim "novel".

[314] **RER-3**, Katz – Second Expert Report, ¶ 6.

[315] **CER-3**, Prof. de Beer – Expert Report, ¶ 32.

[316] **RER-3**, Katz – Second Expert Report ¶ 35.

[317] **RER-3**, Katz – Second Expert Report, ¶ 34 (emphasis in original).

must be vetted by courts or legislatures before they are admitted to the category of property in Ontario.[318]

128. Second, the Claimants and Professor de Beer incorrectly infer that the Ontario legislature intended to create property rights in the *Climate Change Act* because it did not include an "express disclaimer" of emission allowances' proprietary status.[319] The creation of property rights in Ontario law cannot be presumed, and certainly not from the absence of a disclaimer. In this case, it is more significant that the statute did not use the nomenclature of "property" at all.[320] Canadian courts have found such omissions to be significant in bearing on the non-proprietary status of an interest.[321]

129. Nor can the intention of the Ontario legislature be inferred based on consideration of "international practice", as Mr. Mehling and the Claimants claim.[322] The answer to the novel question of emission allowances' proprietary status in Ontario is jurisdiction-specific. It depends on what the Ontario legislature did and what an Ontario court would find based on the *Climate Change Act* and its regulations, not on "international practice."[323]

130. Based on the absence of a legislative declaration and a decision by an Ontario court that emission allowances are property in Ontario, the Tribunal can appropriately conclude that emission allowances currently lack the legal status of property in Ontario.[324] It need not pursue the issue any further.

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[318] *See* **RER-3**, Katz – Second Expert Report, ¶ 35 ("[t]here is a clear "before" and "after" quality to a court's ruling that affects the legal status of the interest.").

[319] *See* Claimants' Reply, ¶¶ 273-290; **CER-3**, Prof. de Beer – Expert Report, ¶ 199-201, 212; **RER-3**, Katz – Second Expert Report, ¶¶ 30-33.

[320] **RER-3**, Katz – Second Expert Report, ¶ 32.

[321] *See* **RER-3**, Katz – Second Expert Report, ¶ 32. Legislators also know how to declare proprietary interests, having done so in other cases. *See* **RER-3**, Katz – Second Expert Report, ¶ 31.

[322] *See* Claimants' Reply, ¶¶ 250, 260; **CER-4**, Expert Report of Prof. Michael Mehling, 15 July 2022, ¶¶ 9, 65.

[323] *See* **RER-3**, Katz – Second Expert Report, ¶ 23.

[324] **RER-3**, Katz – Second Expert Report, ¶ 35.

(b) Emission Allowances are Non-Proprietary, Non-Compensable Regulatory Interests

131. Given a lack of legislative declaration or judicial determination, it is "not a matter of fact but a matter of speculation whether a court in Ontario might in future admit a new interest like emission allowances to the category of property rights in Ontario."[325] Stage Two of the exercise would require an Ontario court to identify the nature and character of the interest in question.[326] Where an interest is created by statute, an Ontario court would assess its nature and character within the framework of the creating statute, including its overall purpose.[327]

132. The purpose of the *Climate Change Act* was to establish a regulatory scheme to reduce greenhouse gas emissions to respond to climate change.[328] Emission allowances were regulatory tools created under the *Act* to facilitate meeting that objective, including by encouraging Ontarians to modify their behaviour.[329]

133. Within the cap and trade system, behaviour modification was effectuated through compliance obligations.[330] Emitters would be obliged to submit emission allowances equal to their total emissions for a given compliance period, or face penalties for non-compliance.[331] As such, emission allowances were compliance instruments, representing units of an overall "cap" on emissions.[332] While they provided a flexible way for compliance entities to meet their obligations, emission allowances derived

[325] **RER-3**, Katz – Second Expert Report, ¶ 25.

[326] **RER-3**, Katz – Second Expert Report, Section III(B). The resulting picture of an interest's nature and character is static and does not vary with context. *See* **RER-3**, Katz – Second Expert Report, ¶ 12.

[327] **RER-3**, Katz – Second Expert Report, ¶¶ 36-37.

[328] **R-006**, *Climate Change Act*, ss. 2(1), 2(2).

[329] **RER-3**, Katz – Second Expert Report, ¶ 39.

[330] **RER-3**, Katz – Second Expert Report, ¶¶ 39-43; 47. *See also* **R-006**, *Climate Change Act*, s. 14.

[331] **RER-3**, Katz – Second Expert Report, ¶¶ 8; 47.

[332] As noted above, emission allowances were to be submitted in the amount of one emission allowance per tonne of CO2 emitted. *See* **R-007**, Regulation 144/16, s. 10. The French term for "emission allowance" in the *Climate Change Act* – "quota d'emission" – confirms that emission allowances are akin to parts of an overall quota on emissions. See footnote 22 above.

their purpose and value as immunities from penalty for emitting an equivalent amount of greenhouse gas.[333]

134. In addition to their statutory purpose, a number of statutory provisions shape the nature and character of emission allowances as "non-proprietary, non-compensable regulatory interests."[334] Notably, the government retained discretion to act with respect to emission allowances without an obligation to compensate in section 70 of the Act.[335] The inclusion of section 70 in the creating statute for emission allowances signals the Legislature's clear intention not to create a property right.[336]

135. Section 28(2) of the *Act* further provides that emission allowances were not able to be fragmented by way of a trust.[337] They could only be held and submitted by one participant at any given time and could not be held beneficially on behalf of another. This prohibition on beneficial holding, indicates that the Legislature specifically did not grant emission allowances a proprietary nature and character.[338]

136. The Claimants and their experts argue that policy reasoning – including what they believe would be preferable for the effectiveness of the system – dictates that emission allowances should have the legal status of property.[339] However, an Ontario court would be concerned with what the legislature actually *did* in creating emission allowances under the relevant statutes, rather than with free-standing policy thinking. Nothing in the cap and trade program, including trading in emission allowances, depended on the creation of property rights. Rather, in examining the specific provisions

[333] **RER-3**, Katz – Second Expert Report, ¶ 41.

[334] **RER-3**, Katz – Second Expert Report, ¶¶ 46-51.

[335] Section 70 of the *Act* provided that emission allowances could not be the subject of any expropriation action. *See* **R-006**, *Climate Change Act*, s. 70; **RER-3**, Katz – Second Expert Report, ¶ 47; **RER-1**, First Expert Report of Prof. Larissa Katz, 16 February 2022 ("Katz – First Expert Report"), ¶ 59 ("s. 70 of the Climate Change Act indicates an intention that emission allowances exist as non-proprietary compliance instruments, with broad latitude reserved by the legislature to make policy decisions that may affect their value".)

[336] **RER-3**, Katz – Second Expert Report, ¶ 47.

[337] **RER-3**, Katz – Second Expert Report, ¶ 47.

[338] **RER-3**, Katz – Second Expert Report, ¶ 47.

[339] *See e.g.*, Claimants' Reply, ¶ 275; **CER-3**, Prof. de Beer – Expert Report, ¶ 185.

of the *Act* and its regulations, in light of their statutory purpose, the Legislature intended to create emission allowances as non-proprietary regulatory interests.[340]

(c) Emission Allowances Lack the Core Common Law Characteristics of Property, Most Notably Exclusive Control and Use

137. The Third Stage of an Ontario court's analysis would involve determining whether the interest has the common law characteristics of property rights or sufficient common law characteristics in the legal context in which the question arises.[341] Given their nature and character, emission allowances lack essential common law characteristics of property,[342] especially exclusive control and use.[343]

138. Exclusive control and use is the ability to exclude interference by others, including the government, and to determine on what terms others are included in property rights.[344] Professor Katz explains that emission allowances lacked this fundamental characteristic of property because they were subject to the discretion of the Minister to pursue its policy objectives, without being subject to claims for compensation.[345] This is a significant limitation on the right to exclude others, specifically the government. Section 70 of the *Act* indicates that emission allowances lacked this important indicium of common law property rights.[346]

139. Emission allowance holders also lacked the power to fragment their interests under section 28(2) of the *Act*. The power to fragment is a fundamental and basic feature of property rights that emission allowances lacked.[347]

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[340] **RER-3**, Katz – Second Expert Report, ¶ 8.

[341] **RER-3**, Katz – Second Expert Report, ¶ 52-53, 83-90.

[342] **RER-3**, Katz – Second Expert Report, ¶¶ 9-10, 52-91.

[343] **RER-3**, Katz – Second Expert Report, ¶¶ 9, 54-81. For a discussion of further core common law criteria that emission allowances lacked, *see* **RER-1**, Katz – First Expert Report, Section 6.

[344] **RER-3**, Katz – Second Expert Report, ¶ 55.

[345] **RER-3**, Katz – Second Expert Report, ¶¶ 54-80.

[346] **RER-3**, Katz – Second Expert Report, ¶¶ 55, 61-64.

[347] **RER-3**, Katz – Second Expert Report, ¶¶ 66-69.

140. Professor de Beer misunderstands the common law meaning of exclusivity, focusing instead on the things that "only a registered participant" may do with emission allowances.[348] But as Professor Katz explains, exclusive control in the common law tradition has "never … meant restricting owners to the solitary enjoyment of a thing."[349] Rather, it is concerned with "the ability to control the actions of others with respect to a thing".[350] There were significant limitations on a registered participant's ability to control the actions of others, particularly the government, with respect to emission allowances. Professor de Beer's misunderstanding extends throughout his analysis and undermines his conclusion that emission allowances would be found to be property in Ontario.[351]

141. Given the absence of a legislative declaration or judicial determination that emission allowances are property in Ontario, emission allowances currently lack the status of property under the relevant municipal law. As emission allowances lack the requisite common law characteristic of exclusive control of use, among other common law indicia of property, an Ontario court would also likely not find that emission allowances constitute property.[352] As such, emission allowances are not property under the relevant domestic law and fall outside of the scope of NAFTA Article 1139(g).

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[348] *See e.g.*, **CER-3**, Prof. de Beer – Expert Report, ¶ 140.

[349] **RER-3**, Katz – Second Expert Report, ¶ 67 (emphasis in original). *See also* ¶¶ 65-71.

[350] **RER-3**, Katz – Second Expert Report, ¶ 67.

[351] **RER-3**, Katz – Second Expert Report, ¶¶ 66-76; 144; 210; Claimants' Reply, ¶¶ 266-272. Professor Katz explains further that Professor de Beer misidentifies "tradability" as evidence of exclusivity (*see* **RER-3**, Katz – Second Expert Report, ¶¶ 77-80). Both Canada's and the Claimants' expert agree that tradability and value as understood in a "commercial realities" approach is not determinative of an interest's proprietary status in Ontario. *See* **CER-3**, Prof. de Beer – Expert Report, ¶¶ 78, 106, 186; **RER-1**, Katz – First Expert Report, ¶ 19; **RER-3**, Katz – Second Expert Report, ¶¶ 27, 86.

[352] Professor Katz explains that, given that emission allowances lack the core indicia of common law property, notably exclusive control of use, they would neither qualify as property for the purposes of the common law generally, as in the expropriation context, nor in the hypothetical statutory context identified by the Claimants. *See* **RER-3**, Katz – Second Expert Report, ¶ 92. However, should an analogous domestic legal context be useful, the most analogous legal context for an Ontario court in which the present question arises is that of expropriation, rather than the hypothetical statutory context selected by Professor de Beer, the *Ontario Rules of Civil Procedure*. *See* **RER-3**, Katz – Second Expert Report, ¶¶ 81-90.

2. KS&T Did Not Hold "Interests Arising from the Commitment of Capital or Other Resources in the Territory of a Party to Economic Activity in Such Territory" Under NAFTA Article 1139(h)

(a) The Claimants Have Failed to Articulate a Cohesive Theory of KS&T's Alleged Investment under Article 1139(h)

142. In their Memorial, the Claimants did not clearly articulate what "interests" they alleged qualified as investments under Article 1139(h). They appeared to allege that KS&T held two distinct investments under Article 1139(h): "interests arising from the commitment of capital and other resources in Canada, including: (a) business development, marketing and trading activities", which "included KS&T's broader carbon trading business", and "(b) commitment of capital through the purchases of carbon allowances from public auctions through KS&T's Ontario CITSS accounts".[353] While the language with respect to (b) was unclear, the Claimants had alleged in their Notice of Arbitration that the "Purchase Price KS&T invested in Ontario to purchase the Purchased allowances also constituted a protected investment under the NAFTA."[354] Canada demonstrated in its Counter-Memorial that neither KS&T's "carbon trading business" nor the purchase price of emission allowances was the type of interest contemplated by NAFTA Article 1139(h).[355]

143. In their Reply, the Claimants still cannot decide what their alleged investment is. In their arguments on jurisdiction, the Claimants appear to have abandoned any claim that KS&T's alleged "carbon trading business" is a standalone investment under Article 1139(h). They assert instead that Canada's understanding that this was one of its alleged "interests" under Article 1139(h) was "inaccurate and misleading,"[356] and focus exclusively on "the emission allowances", not their purchase price, as the relevant "interest".[357]

144. However, in their arguments on the merits, the Claimants assert that they "held rights in a broader carbon trading business in Ontario under Article 1139(h) of the NAFTA, investments which

[353] Claimants' Memorial, ¶¶ 323(a) and (b).

[354] Claimants' Request for Arbitration, 7 December 2020, ¶ 64.

[355] Canada's Counter-Memorial, ¶¶ 152-164, including fn. 302.

[356] Claimants' Reply Memorial, fn. 459.

[357] Claimants' Reply, ¶ 314. *See also* Claimants' Reply, Section III.B.2 ("The Respondent's Assertion that the Emission Allowances Held by KS&T Were Not Investments Under Article 1139(h) of the NAFTA is Unsupported").

were expropriated by Ontario."[358] They further state, "for the avoidance of any doubt", that, if the Tribunal agrees with Canada that the emission allowances purchased by KS&T in the May 2018 auction are not "property" under Article 1139(g), "they *together with the Claimants' broader trading business* in any event also constitute 'interest*s* arising from the commitment of capital' under 1139(h)."[359] They do not explain anywhere what these alleged "rights in a broader carbon trading business" are, or how their purported "interest" in a "broader trading business" qualifies as an investment under Article 1139(h).

145. The Claimants' failure to articulate a cohesive theory of their investment in Ontario is telling. Their attempts to fit their nebulous cross-border business activity into the specific category of investment captured by Article 1139(h) must be rejected. The following sections demonstrate: first, that NAFTA Article 1139(h) is not the catch-all category of investment the Claimants hope it to be; and second, when considered against the properly interpreted provision, KS&T's alleged investments are not interests protected by Article 1139(h).

(b) Article 1139(h) Is Not a Catch-All Category of Investment

146. In their Reply Memorial, the Claimants rely heavily on their broad notion of the term "interest",[360] standing on its own, and an allegation that Article 1139(h) is "understood to operate as a 'catch-all' category of investment."[361] Contrary to the principles of proper treaty interpretation,[362] the Claimants ignore the context in which the term "interest" appears. As a result, they overlook the specific requirements that must be met for an interest to qualify for protection under Article 1139(h).

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[358] Claimants' Reply, ¶ 534.

[359] Claimants' Reply, fn. 849 (emphasis added).

[360] Claimants' Reply, ¶¶ 313-315, 345, and 348.

[361] Claimants' Reply, ¶ 313. The Claimants point to an UNCTAD paper to support the "catch-all" point; however, that paper also erroneously refers to NAFTA Article 1139 as containing "an illustrative list" of investments. NAFTA Article 1139, including paragraph (h), fits more appropriately in the subsequent section of the paper, which discusses "closed list" approaches. *See* **CL-172**, UNCTAD, Scope and Definition, UNCTAD Series on Issues in International Investment Agreements II, U.N. Doc. No. UNCTAD/DIAE/IA/2010/2 (2011), p. 34.

[362] **RL-029**, *Vienna Convention on the Law of Trea*ties, 23 May 1969 (entered into force 27 January 1980) 1155 U.N.T.S. 331 ("Vienna Convention on the Law of Treaties"), Art. 31(1).

147. As Canada explained in its Counter-Memorial,[363] the definition of "investment" in NAFTA Article 1139 provides an exhaustive list of the eight types of interest that qualify as "investments" under the treaty.[364] Each sub-paragraph in the list refers to a different kind of interest, specifically defined and featuring particular requirements. Accordingly, the mere identification of an alleged "interest" does not suffice to qualify the interest as an investment; the "interest" must also meet the particular requirements of the category at issue. NAFTA Article 1139(h) is no exception.[365]

148. The requirements of Article 1139(h) are gleaned from both the *chapeau* and its illustrative sub-paragraphs. The Claimants' attempt to read out the sub-paragraphs[366] is contrary to the principles of treaty interpretation. The sub-paragraphs constitute highly relevant context that elucidates the kind of interest captured by Article 1139(h). Prior NAFTA tribunals have dismissed similar attempts to focus exclusively on the *chapeau* of Article 1139(h), explaining:

> The *chapeau* cannot be read by itself. The NAFTA does not extend protection to any "commitments of capital", but only to those which exhibit certain features so as to give rise to "interests". These features are defined through two illustrative examples in subparagraphs (h.i) and (h.ii).[367]

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[363] Canada's Counter-Memorial, ¶ 132.

[364] *See e.g.*, **RL-024**, *Lion Mexico – Decision on Jurisdiction*, ¶ 182 (describing Article 1139 as "offer[ing] a sophisticated and precise definition of protected investments: the provision lists eight categories of 'interests' which are considered as investments, and two categories which are excluded."); **CL-020**, *Grand River – Award*, ¶ 82. All three NAFTA Parties agree. *See e.g.*, **RL-198**, *B-Mex, LLC and Others v. United Mexican States* (ICSID Case No. ARB(AF)/16/3) Third Article 1128 Submission of Canada, 13 June 2022 ("*B-Mex – Canada's Third 1128 Submission*"), ¶ 9; **RL-144**, *Lone Pine Resources Inc., v. Government of Canada* (UNCITRAL) Article 1128 Submission of the United States, 16 August 2017 ("*Lone Pine – 1128 Submission of the United States*"), ¶ 2; **RL-199**, *B-Mex, LLC and Others v. United Mexican States* (ICSID Case No. ARB(AF)/16/3) Fourth Article 1128 Submission of the United States, 13 June 2022 ("*B-Mex – Fourth US Article 1128 Submission*"), ¶ 2; **RL-145**, *Methanex Corporation v. United States of America* (UNCITRAL) Second Article 1128 Submission of the Government of Mexico, 15 May 2001, ("*Methanex – Mexico's Second 1128 Submission*"), ¶ 19.

[365] The NAFTA Parties have been clear that not all "interests" arising from the commitment of capital qualify as an "investment" under Article 1139(h). *See e.g.*, **RL-198**, *B-Mex – Canada's Third 1128 Submission*, ¶ 17; **RL-199**, *B-Mex – Fourth US Article 1128 Submission*, ¶ 6; **RL-146**, *Apotex Holdings Inc. and Apotex Inc. v. United States of America* (ICSID Case No. ARB(AF)/12/1) Counter-Memorial on Merits and Objections on Jurisdiction of Respondent United States of America, 14 December 2012, ¶ 245; **RL-147**, *Apotex Holdings Inc. and Apotex Inc. v. United States of America* (ICSID Case No. ARB(AF)/12/1) Mexico Article 1128 Submission, 8 February 2013, ¶ 6. Were Article 1139(h) designed as a "catch-all" category of investment, as the Claimants allege, the drafters would have chosen more open-ended language.

[366] Claimants' Reply Memorial, ¶¶. 342-348.

[367] **RL-024**, *Lion Mexico – Decision on Jurisdiction*, ¶¶ 203-205.

149. The Claimants incorrectly argue that the "emission allowances do not need to correspond to either such illustrative examples in order to fall within the scope of Article 1139(h)."[368] Sub-paragraphs (h)(i) and (h)(ii) help to define the features of an investment that qualifies under Article 1139(h). While an alleged interest need not fall squarely within one of the illustrative examples, it must exhibit similar features.[369]

150. The common features of the illustrative examples include references to contracts;[370] the presence of an investor's property or an enterprise in the territory of the host Party; and economic activities in the territory of the host Party (*e.g.* turnkey or construction contracts or concessions; or production, revenue or profits of an enterprise). The types of contractual interests illustrated in subparagraphs (h)(i) and (h)(ii) thus confirm that, for an interest to meet the requirements of Article 1139(h), it must be longer-term and include an important commitment of capital contributing to the economic development of the host State.

151. Articles 1139(i) and (j) further confirm that more is required under Article 1139(h) than "claims to money" (as opposed to capital) arising from cross-border sales agreements for goods or services (1139(i)(i)), the extension of credit in connection with a commercial transaction (1139(i)(ii)), or any other claims to money that do not otherwise fall within the specifically enumerated categories of investment in Article 1139. The Claimants do not dispute that cross-border trading interests do not qualify as investments under Article 1139(h).[371]

(c) KS&T's Alleged Investments Do Not Satisfy the Requirements of Article 1139(h)

152. The Claimants have not established that KS&T's "interests" meet the specific requirements of Article 1139(h). To the contrary, KS&T's alleged interests bear no similarity to the illustrative examples that help to define the category of interest that is protected.

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[368] Claimants' Reply, ¶ 346.

[369] *See* Canada's Counter-Memorial, ¶¶ 160-162.

[370] **RL-024**, *Lion Mexico – Decision on Jurisdiction*, ¶ 205.

[371] Claimants' Reply, ¶¶ 317-318 (attempting to distinguish the *facts* of the cases Canada cited in its Counter-Memorial in support of this point, arguing that their interests are not cross-border trading interests as a matter of fact).

153. First, KS&T had no business infrastructure in Ontario. Despite the Claimants' assertions that KS&T was engaging in a "long-term enterprise in Ontario",[372] it did not have any physical or corporate presence in Ontario consistent with Articles 1139(h)(i) or (ii). There is no dispute that KS&T was solely incorporated in the United States, and that it had no subsidiary, business address, employees, officers, directors, personnel, infrastructure or equipment in Ontario. The Claimants attempt to minimize the importance of a "physical presence or fixed place of business",[373] but a physical or established corporate presence in the host State's territory is indicative of the kind of economic activity necessary to give rise to a qualifying interest. Business infrastructure in the United States, and an Ontario CITSS account used to make transfers to California, do not.

154. Second, the economic activities that KS&T undertook in Ontario were not in support of any "business in Ontario", but of its business in the U.S. The evidence is clear that KS&T's purchases of emission allowances through its Ontario CITSS account were orchestrated and executed in the United States, primarily by Mr. Martin in Houston and Mr. Porter in Wichita. Mr. Martin further confirmed that it was the company's [redacted] to move all emission allowances it purchased through its Ontario account to its California account [redacted] [374] Mr. King – another KS&T employee based in the United States – also explained that KS&T used its California account to [redacted] emission allowances it purchased at auction through its Ontario account.[375] Prior to the May 2018 auction, in which KS&T was not obligated to participate, [redacted]

155. The Claimants' attempts to play up their "economic activities" in Ontario by reference to KS&T's secondary market activity similarly confirm that KS&T's "broader carbon trading business" was in the United States. As set out above, apart from the [redacted] transactions Canada identified in its Counter-Memorial, none of the other transactions they cite used KS&T's Ontario CITSS account were with Ontario counterparties, or referenced any other connection to Ontario.[376] They all [redacted]

[372] Claimants' Memorial, ¶¶ 49, 246, 379, 383

[373] Claimants' Reply, ¶ 371.

[374] [redacted]

[375] **CWS-6**, King – Reply Witness Statement, ¶ 21.

[376] Canada's Rejoinder, Section II.B.

[redacted] [77]

156. While KS&T may have expended funds to purchase emission allowances in Ontario auctions, the mere expenditure of funds, even in connection with an "interest", does not suffice to qualify as an investment under Article 1139(h). A more lasting connection to the territory of the host State is required than a cross-border trading business centered in the United States, and the prompt transfer of emission allowances to California. The Claimants assert that KS&T's participation in Ontario's cap and trade program was part of a "long-term business strategy".[378] Not only did they not produce any contemporaneous evidence of a long-term business plan or strategy, but this statement is contradicted by KS&T`s own internal documents stating that their core strategy is to [redacted] [79]

157. The evidence is conclusive that KS&T's "carbon trading business" was located in the United States, not Ontario, and that it only participated in auctions in Ontario to support its cross-border trades. As a result, neither the alleged interest in emission allowances nor its unidentified "rights in a broader carbon trading business" arise from the commitment of capital or other resources in Ontario to the kind of economic activity contemplated by NAFTA Article 1139(h).

158. Anticipating this conclusion, the Claimants suggest that the Tribunal can exercise jurisdiction even if it finds that KS&T did "not conduct sufficient economic activity in the Respondent's territory in order to establish jurisdiction *ratione materiae* under the NAFTA".[380] There is no basis in NAFTA

[377] **CWS-6**, King – Reply Witness Statement, ¶ 34.

[378] Claimants' Reply, ¶ 302.

[379] [redacted]

[380] Claimants' Reply, ¶ 341. The Claimants argue that Canada is estopped from "denying jurisdiction under NAFTA Article 1139" because Ontario linked its cap and trade program with those of California and Quebec, and "expressly represented" that their emission allowance markets "had become a seamless single market". *See* Claimants' Reply, ¶ 330. In addition to the Claimants' argument being legally unsound, the mere fact that an emission allowance created by one jurisdiction could be used for compliance obligations in another does not eviscerate borders for other purposes. KS&T's participation in this "single market" demonstrates that location continued to matter after linkage. KS&T registered as a market participant in *both* California and Ontario, and made choices about where it would participate in auctions based on the territorially-bound regulations [redacted] Taken to its

Chapter Eleven to permit this result. The Tribunal must be satisfied that the jurisdictional requirements of NAFTA have been met, and the Claimants have failed to establish that KS&T held an investment under Article 1139(h).

D. The Claimants Have Not Established Jurisdiction with Respect to Koch Industries Under NAFTA Chapter Eleven

159. The Claimants have not established that the Tribunal has jurisdiction with respect to Koch Industries. In the sections that follow, Canada explains that: (1) Koch Industries does not hold any investments in Ontario relevant to the Tribunal's jurisdiction to hear this claim under NAFTA Articles 1101, 1116, and 1139; and (2) Koch Industries has failed to make a *prima facie* claim for damages under NAFTA Article 1116.

1. Koch Industries Does Not Hold Any "Investments" Relevant to the Tribunal's Jurisdiction Under NAFTA Articles 1101, 1116 and 1139

(a) The Claimants Have Failed to Articulate a Cohesive Theory of Koch Industries' Alleged Investments

160. The Claimants' theory of alleged Koch Industries investments that are relevant to this Tribunal's jurisdiction has also shifted. In their Memorial, the Claimants made bare assertions about their "investments" as follows:

- "its 100 percent shareholding in KS&T and INVISTA", pointing to Article 1139(a);[381]
- unspecified "interests in enterprises entitling Koch to the income or profits of these enterprises", pointing to Article 1139(e);[382] and
- "real estate or other property, tangible or intangible, that was acquired in the expectation or used for the purposes of economic benefit or other business purposes", pointing to Article 1139(g), and "a range of other bricks-and-mortar investments in Ontario, as well as intangible investments". The Claimants alleged that the brick-and-mortar investments

logical conclusion, the Claimants' position would count any participant holding "fungible" emission allowances in a California CITSS account as an investor *in Ontario*.

[381] Claimants' Memorial, ¶ 322(a) and fn. 409. NAFTA Article 1139(a) refers to "an enterprise".

[382] Claimants' Memorial, ¶ 322(b) and fn. 410. NAFTA Article 1139(e) refers to ("an interest in an enterprise that entitles the owner to share in income or profits of the enterprise")

> in Ontario that qualified under Article 1139(g) included "Koch subsidiaries INVISTA and Georgia Pacific."[383]

161. Canada established in its Counter-Memorial that the Claimants' bare assertions – often unaccompanied by even the most basic identification of the alleged interest in question – did not satisfy their burden to establish the Tribunal's jurisdiction over Koch Industries' alleged investments.[384]

162. In their Reply, the Claimants make at least three new attempts to establish the Tribunal's jurisdiction. First, they allege that Koch Industries has an indirect interest in the emission allowances that separately qualify as investments under both NAFTA Articles 1139(g) and 1139(h).[385] Second, they allege that Koch Industries' "indirect ownership of [the] emission allowances from the May 2018 auction" is an "interest in an enterprise" that qualifies as an investment under Article 1139(e).[386] Third, they have newly identified Koch Industries' 100 percent shareholding in both INVISTA and Georgia Pacific as "interests in enterprises that entitle Koch to the income or profits of those enterprises" under Article 1139(e).[387] The Claimants' late attempts to articulate a basis for the Tribunal's jurisdiction evince a misunderstanding of both the categories of investment protected by NAFTA Article 1139 and the facts. They must be rejected.

(b) Koch Industries' Alleged Interests in the Emission Allowances Purchased by KS&T Do Not Qualify as Protected Investments

163. Canada maintains that Koch Industries' ownership of KS&T, a U.S. entity, cannot qualify as an investment in Ontario under NAFTA Article 1139(a) that could ground the Tribunal's jurisdiction.[388] The Claimants appear to agree, since they now focus on Koch Industries' indirect ownership of KS&T's alleged interests in the emission allowances that KS&T purchased in the May

[383] Claimants' Memorial, ¶ 322(c) and fns. 411-412.

[384] Canada's Counter-Memorial, ¶¶ 165-171.

[385] Claimants' Reply, ¶ 352.

[386] Claimants' Reply, ¶ 353.

[387] Claimants' Reply, ¶ 354.

[388] Canada's Counter-Memorial, ¶¶ 166-167.

2018 auction, rather than the entity itself. The Claimants' arguments under Articles 1139(e), (g), and (h) must all be rejected.

164. First, the Claimants mischaracterize the nature of interests captured by NAFTA Article 1139(e).[389] Paragraphs (a) through (f) refer to enterprises and the types of interests one can have with respect to an enterprise, not merely to interests in things held by an enterprise. For example, paragraphs (b) and (c) refer to equity security and debt security interests "of an enterprise". Paragraphs (e) and (f) similarly refer to "interest[s] in an enterprise".[390] An emission allowance that was purchased by an enterprise is not an interest in that enterprise. The emission allowances thus cannot qualify as an "interest in [KS&T] that entitles [Koch Industries] to share in income or profits of [KS&T]".

165. Second, the Claimants ignore that emission allowances could not be indirectly "owned" as a matter of fact. Section 28(2) of the *Climate Change Act* prohibited a registered participant from holding an emission allowance that was indirectly owned by another person:

> No registered participant shall hold in the participant's cap and trade accounts an emission allowance that is owned, directly or indirectly, by another person.[391]

166. Section 21 of the *Climate Change Act* further mandated that only registered participants were permitted to deal in any way with emission allowances.[392] There is no dispute that Koch Industries was not a registered participant in any of the prescribed jurisdictions. Accordingly, if Koch Industries did indirectly own emission allowances, the Claimants were in violation of Ontario law.[393]

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[389] NAFTA Article 1139(e) reads ("investment means […] (e) an interest in an enterprise that entitles the owner to share in income or profits of the enterprise").

[390] Canada recalls that the definition of "enterprise" in NAFTA Articles 1139 and 201 is broad, and refers to many ways of forming an enterprise, including incorporation and partnership.

[391] **R-006**, *Climate Change Act*, s. 28(2).

[392] **R-006**, *Climate Change Act*, s. 21.

[393] Indeed, both of KS&T's PAR and AAR certified that they would "comply with the *Climate Change Mitigation and Low-Carbon Economy Act, 2016* and the Cap-and-Trade Regulation". *See* **R-050**, KS&T Participant Registration Form, 29 November 2016, pp. 5 and 9 of the PDF. The President of KS&T, LP, Frans Pettinga, further certified his responsibility for the conduct of KS&T's account representatives. *See* **R-050**, p. 13 of the PDF.

167. Finally, even if it were possible for Koch Industries to have an indirect interest in the emission allowances themselves, Canada has demonstrated that the allowances do not qualify as investments under Article 1139(g), because they are not property under Ontario law,[394] or under Article 1139(h), because they do not comprise an interest that meets the requirements of that sub-paragraph.[395]

(c) Koch Industries' Alleged Interests in INVISTA and Georgia Pacific Cannot Ground the Tribunal's Jurisdiction Over This Claim

168. Canada maintains that none of Koch Industries' alleged interests with respect to INVISTA or Georgia Pacific are relevant to the Tribunal's jurisdiction because they are not the "investment" in dispute.[396] Although they are Canadian enterprises, they are not at issue in this dispute. In their Reply, the Claimants add to their list of alleged interests in these two enterprises,[397] and reiterate their allegation that the Tribunal has jurisdiction over Koch Industries' "investments" in these enterprises[398] because, "in accordance with NAFTA Article 1101(1)(b), INVISTA and Georgia Pacific are investments of Koch in Canada's territory 'relating to' Ontario's measures that are at issue in the present dispute."[399] The Claimants' arguments must be rejected.

169. First, the Claimants rely on an incorrect reversal of the order of analysis under Article 1101(1). It is not an alleged investment that must "relate to" a measure, but the reverse.

170. Second, the Claimants overlook the importance of Article 1116(1), read together with Article 1101(1), in circumscribing the parameters of a tribunal's jurisdiction to hear a particular claim. Article 1116(1) permits an investor of a Party to submit to arbitration a claim that another Party has: (1) breached an obligation under Section A, and (2) that the investor has suffered damage by reason

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[394] *See* Section III.C.1; Canada's Counter-Memorial, ¶¶ 131-151.

[395] *See* Section III.C.2; Canada's Counter-Memorial, ¶¶ 152-164.

[396] Canada's Counter-Memorial, ¶¶ 168, 170-171.

[397] In their Memorial, the Claimants alleged that Koch Industries had an "enterprise" in INVISTA under Article 1139(a), and property interests under Article 1139(g) in "Koch subsidiaries INVISTA and Georgia Pacific." Claimants' Memorial, ¶¶ 322(a) and (c). The Claimants have added to their allegations that Koch Industries' ownership interests in INVISTA and Georgia Pacific are "are interests in enterprises that entitle Koch to the income or profits of those enterprises." *See* Claimants' Reply, ¶ 354.

[398] Claimants' Reply, ¶¶ 354-356, 393-398.

[399] Claimants' Reply, ¶ 394.

of, or arising out of, that breach. NAFTA tribunals have consistently held that the investment an investor invokes under Article 1101(1) must be "the very investment in respect of which it makes its claims."[400]

171. The Claimants chose to bring their claim under Article 1116, and were free to define its parameters. The Claimants did not, and have not, alleged the breach of an obligation or any damage suffered with respect to Koch Industries' interests in INVISTA or Georgia Pacific. Indeed, even as they allege in their Reply that the impugned measures "relate to" INVISTA, the Claimants acknowledge that it was only KS&T that was left "exposed to the measures at issue in this claim."[401] Accordingly, even if the impugned measures could be viewed as "relating to" these Canadian enterprises as a matter of fact – which the Tribunal need not decide here – no claim of breach or damage has been brought with respect to them under Article 1116. There is no basis for the Tribunal's jurisdiction.

2. Koch Industries Has Failed to Plead a *Prima Facie* Damages Claim Under NAFTA Article 1116

172. Canada maintains that the Tribunal does not have jurisdiction *ratione personae* over Koch Industries because it has failed to plead a cognizable *prima facie* damages claim under Article 1116.[402] The Claimants do not contest that they must make a *prima facie* damages claim as a matter of law. Instead, their Reply focuses on whether they have in fact met that threshold.[403] On their case, Koch Industries' alleged loss or damage is comprised of "the drop in value of its 100%-owned affiliate KS&T and the latter's directly-held investment in Ontario".[404] However, neither category of alleged loss meets the low threshold to make a *prima facie* damages claim because they are inherently losses that, if established, belong to KS&T.

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[400] *See e.g.*, **CL-059**, *Mesa Power Group, LLC v. Government of Canada* (UNCITRAL) Award, 24 March 2016 ("*Mesa – Award*"), ¶ 330; **RL-131**, *Westmoreland Mining Holdings LLC v. Government of Canada* (UNCITRAL) Final Award, 31 January 2022 ("*Westmoreland – Final Award*"), ¶¶ 199-200 (reaching the same conclusion with respect to the "investor" referenced in Articles 1116(1) and 1101(1)).

[401] Claimants' Reply, ¶ 356.

[402] Canada's Counter-Memorial, ¶¶ 172-174.

[403] Claimants' Reply, ¶ 392.

[404] Claimants' Reply, ¶ 392.

173. Article 1116 does not permit for recovery of reflective losses – that is, losses belonging to a subsidiary enterprise.[405] Instead, Article 1116 exists for direct harm to an investor's interests in an enterprise.[406] The NAFTA Parties purposefully included Article 1117 to permit investors of another Party to claim damages on behalf of a local enterprise – damages to which they would not otherwise be entitled under international law.[407] The NAFTA Parties have consistently interpreted Article 1116 as precluding recovery for reflective loss.[408] A claimant cannot bypass the specific structure of Articles 1116 and 1117 to claim the losses of an enterprise – properly the subject of an Article 1117 claim – as its own losses under Article 1116.

174. The Claimants have not brought an Article 1117 claim in this case because they did not have an enterprise in Canada on whose behalf they could claim the damages they allege. KS&T is not an investment in Canada. It is an enterprise that is organized under the laws of the United States. There is no basis in NAFTA Chapter Eleven for a U.S. enterprise (*i.e.* Koch Industries) to claim loss

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[405] *See e.g.*, **CL-136**, *Bilcon of Delaware et al v. Government of Canada* (UNCITRAL) Award on Damages, 10 January 2019, ¶¶ 369-389: (concluding, at ¶ 389, that "Articles 1116 and 1117 are to be interpreted to prevent claims for reflective loss from being brought under Article 1116. This follows from the wording of Article 1116 in its context, which includes Articles 1121 and 1135. Moreover, the Tribunal takes account of the common position of the NAFTA Parties in their submissions to Chapter Eleven tribunals.")

[406] The text of Article 1116 reflects one of the core principles of corporate law recognized by advanced domestic legal systems and customary international law: that a corporation has separate legal personality from its shareholders and that, as a result, shareholders are precluded from personally recovering damages in respect of wrongs done to the corporation. *See e.g.*, **RL-148**, D. Gaukrodger, Investment treaties as corporate law: Shareholder claims and issues of consistency. *A preliminary framework for policy analysis*, OECD Working Papers on International Investment, No. 2013/3, OECD Investment Division, pp. 15-17, 21-23; **RL-149**, *Case Concerning the Barcelona Traction, Light and Power Company, Limited (Belgium v. Spain)* (I.C.J. Reports 1970) Second Phase, Judgment, 5 February 1970 ("*Barcelona Traction*"), ¶¶ 41, 44, and 46.

[407] *See* **RL-149**, *Barcelona Traction*, ¶ 46; **RL-150**, *Case Concerning Ahmadou Sadio Diallo (Republic of Guinea v. Democratic Republic of the Congo)* Judgment on Preliminary Objections, 24 May 2007, ¶¶ 61-64 (distinguishing between admissible claims based on direct rights as shareholder and inadmissible claims based on reflective loss); **RL-151**, *Case Concerning Ahmadou Sadio Diallo (Republic of Guinea v Democratic Republic of the Congo)* (I.C.J. Reports 2010) Judgement, 30 November 2010, ¶ 105 (reaffirming the distinction).

[408] *See e.g.*, **RL-152**, M. Kinnear, A. Bjorklund and J. Hannaford, "Investment Disputes under NAFTA: An Annotated Guide to NAFTA Chapter 11", (Kluwer, 2006) [Excerpt], pp. 1116-6 - 1116-7; **RL-153**, *William Ralph Clayton, William Richard Clayton, Douglas Clayton, Daniel Clayton, and Bilcon of Delaware, Inc. v. Government of Canada* (UNCITRAL) Submission of the United States of America, 29 December 2017, ¶¶ 2-22; **RL-154**, *GAMI Investments Inc. v. United Mexican States* (UNCITRAL) Submission of the United States, 30 June 2003, ¶¶ 8-18; **RL-155**, *GAMI Investments Inc. v. United Mexican States* (UNCITRAL) Mexico's Statement of Defence, 24 November 2003, ¶¶ 166-167; **RL-156**, *S.D. Myers v. Government of Canada* (UNCITRAL) Submission of the United Mexican States (Damages Phase), 12 September 2001, ¶¶ 41-45; **RL-157**, *William Ralph Clayton, William Richard Clayton, Douglas Clayton, Daniel Clayton, and Bilcon of Delaware, Inc. v. Government of Canada* (UNCITRAL) Government of Canada Counter-Memorial on Damages, 9 June 2017, ¶¶ 13-28.

allegedly suffered to the value of another U.S. enterprise (*i.e.* KS&T) in a claim against Canada. The Claimants' first category of alleged loss thus fails to meet the *prima facie* damages threshold.

175. The only other alleged loss to Koch Industries is a "drop in value of … [KS&T's] directly-held investment in Ontario".[409] This is a clear case of reflective loss – or alleged loss belonging to, and properly asserted by, KS&T. The Claimants' recognition that the damages they allege with respect to Koch Industries "overlap" with those they allege with respect to KS&T confirms that they are seeking recovery for reflective loss.[410] The Claimants submit that an overlapping damages claim is not problematic, so long as there is no double recovery at the merits stage.[411] That may be the case if the alleged overlapping damages are cognizable for both claimants under NAFTA Chapter Eleven. But if, as here, one claimant has asserted loss or damage to which it cannot be entitled under NAFTA Chapter Eleven, it fails to meet the jurisdictional threshold contained in NAFTA Article 1116.

176. In this case, because reflective loss is not cognizable under Article 1116, the Claimants have failed to plead a *prima facie* damages claim on behalf of Koch Industries. The Tribunal does not have jurisdiction over it or its claims.

E. The Claimants Have Not Established That the Premier-Designate's Announcement of June 15, 2018 was a "Measure" Within the Scope of NAFTA Chapter Eleven

177. The Claimants insist that the Premier-Designate "cancelled" the cap and trade program through a news release issued on June 15, 2018. In addition to the factual inaccuracy of this claim, the news release is not a "measure" that was "adopted or maintained" by Canada and is therefore outside the scope of the Tribunal's jurisdiction.

178. The Claimants allege that Canada has taken the following measures within the meaning of NAFTA Articles 201 and 1101:

a. The Premier-elect's announcement of 15 June 2018;

[409] Claimants' Reply, ¶ 392.

[410] Claimants' Reply, ¶ 392.

[411] Claimants' Reply, ¶ 392.

b. Ontario Regulation 386/18 of 3 July 2018;

c. Bill 4 submitted to the Ontario Legislature on 25 July 2018, and adopted as the *Cap and Trade Cancellation Act*, 2018 (enacted on 31 October 2018);

d. Ontario's formal denial of compensation on 14 March 2019.[412]

179. Canada accepts that items b), c), and d) constitute measures within the scope of NAFTA Chapter Eleven. Canada also accepts that Ontario adopted a "measure" attributable to Canada on June 15, 2018: the decision of the Minister's Delegate not to issue an auction notice.[413] However, the Premier-Designate's announcement[414] identified by the Claimants does not constitute a "measure[] adopted or maintained" by a Party under NAFTA Article 1101 that is subject to the jurisdiction of the Tribunal.[415]

180. Article 1101 establishes the scope of Chapter Eleven's coverage. The *chapeau* to Article 1101(1) sets out the criteria that must be satisfied in order for NAFTA Chapter Eleven to apply: the conduct in question must be a "measure"; that measure must be "adopted or maintained by a Party"; and that measure must "relat[e] to" one or more of the enumerated subparagraphs of Article 1101(1).[416]

[412] Claimants' Memorial, ¶ 336; Claimants' Reply, ¶ 402.

[413] [redacted]

[414] Referring to the news release issued by the Office of the Premier-Designate on June 15. *See* **C-007**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Announces an End to Ontario's Cap-and-Trade Carbon Tax", 15 June 2018.

[415] Canada's Counter-Memorial, fn. 245. Canada maintains that the Claimants must demonstrate that the elements of NAFTA Article 1101 have been satisfied. *See* Canada's Counter-Memorial, ¶ 131. Despite the jurisdictional issues raised by Canada with regard to the Office of the Premier-Designate's June 15 news release, the Claimants have provided no explanation of how this alleged "measure" was "adopted or maintained" by Canada.

[416] NAFTA Article 1101(1). **RL-023**, Meg Kinnear, Andrea Kay Bjorklund, et al., "Investment Disputes under NAFTA: An Annotated Guide to NAFTA Chapter 11, Supplement No. 1", (Kluwer Law International; Kluwer Law International 2006) ("Kinnear: Investment Disputes under NAFTA") [Revised Excerpt], p. 1101-28c.

181. The Office of the Premier-Designate's June 15 news release contains:

- prospective statements concerning the incoming government's policy intentions for when it assumes office; and
- a short statement indicating that the Premier-Designate "confirmed that he has directed officials to immediately take steps to withdraw Ontario from future auctions."

182. The June 15 news release fails to satisfy the requirements of NAFTA Article 1101.

183. First, the news release does not constitute a "measure" within the meaning of NAFTA. Article 201 defines "measure" to include "any law, regulation, procedure, requirement or practice."[417] While tribunals have noted that the definition of "measure" is broad,[418] it is not so broad as to encompass prospective statements concerning the incoming government's policy intentions for when it assumes office.[419] Each of the concepts used to illustrate the meaning of the term – "law", "regulation", "procedure", "requirement" and "practice" – require an identifiable governmental act that imposes requirements or discipline within a Party's jurisdiction.[420] The Premier-Designate's announcement fails this basic test. The prospective statements had no effect. They did not bind Ontario – or even the Ford administration itself after it took office – to specific action.

184. Second, the news release was not "adopted or maintained by a Party". Article 1101(1) excludes potential or proposed measures.[421] This is apparent from the ordinary meaning of the terms "adopted"

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[417] NAFTA Article 201.

[418] *See* **CL-059**, *Mesa – Award*, ¶ 256.

[419] These statements include: a pledge to cancel cap and trade as a "first act following the swearing in" of Mr. Ford's government; an indication that Ontario "would be" notifying its withdrawal from the Harmonization Agreement and WCI and that it "will provide" clear rules for an orderly wind down of cap and trade; and an indication that Premier Ford "will be issuing" directions to the incoming attorney general to challenge the federal carbon tax. *See* **C-007**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Announces an End to Ontario's Cap-and-Trade Carbon Tax", 15 June 2018.

[420] As noted by the Claimants (Claimants' Reply, ¶ 406, citing to **CL-187**, *Ethyl Corporation v. Government of Canada* (UNCITRAL) Award on Jurisdiction, 24 June 1998 ("*Ethyl – Award on Jurisdiction*"), ¶ 66), Canada's view is that the NAFTA's definition of "measure" is a "non-exhaustive definition of the ways in which governments impose discipline in their respective jurisdictions."

[421] **RL-023**, Kinnear: Investment Disputes under NAFTA, pp. 1101-31-1101-33.

and "maintained."[422] Context also supports the conclusion that Article 1101 only extends to measures *actually taken* by a Party.[423] The Premier-Designate's prospective statements of intended action or policy are plainly not "adopted or maintained" by Canada – indeed, they are so vague as to be unlikely to rise even to the level of a "proposed" measure.[424]

185. The "direction" of the Premier-Designate – which the Claimants repeatedly decry as "*ultra vires*" despite acknowledging that the issue of its legality is "clearly moot"[425] – is also not a "measure" that was "adopted or maintained" by Canada. The "direction" was not legally binding on the decision-makers responsible for the August 2018 auction notice determination; the incumbent government retained authority until its resignation and the swearing in of the new government.[426] As explained in Section II.D.3, the Minister's Delegate made the decision declining to issue an auction notice on June 15.

186. Accordingly, the Claimants have failed to establish that the Premier-Designate's June 15, 2018 announcement falls within the scope of Article 1101.

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[422] The Oxford English Dictionary (OED) defines "adopt" as "[t]o take up (an opinion, attitude, course of action, etc.)" or "[t]o approve or accept (a report, proposal, resolution, etc.) formally; to ratify". Meanwhile, the OED defines "maintain" as "[t]o (cause to) continue, keep up, preserve […] To keep up, preserve, cause to continue in being (a state of things, a condition, an activity, etc.). *See* **RL-158**, *Oxford English Dictionary Online* (Oxford University Press, June 2022), definitions of "adopt .v" and "maintain, v." These definitions suggest that a measure is "adopted" when it is taken, approved, or formally accepted and a measure is "maintained" when it is continued.

[423] NAFTA Article 2004 explicitly subjects "actual" and "proposed measure[s]" to the Agreement's State-to-State dispute settlement mechanism. NAFTA Article 2004 provides; "the dispute settlement provisions of this Chapter shall apply with respect to the avoidance or settlement of all disputes between the Parties regarding the interpretation or application of this Agreement or wherever a Party considers that *an actual or proposed measure* of another Party *is or would be inconsistent* with the obligations of this Agreement" (emphasis added). *See also* NAFTA Article 1803, which, in certain circumstances, requires notification and the provision of information concerning "actual or proposed measure[s]." If the Parties also intended NAFTA Chapter Eleven to apply to "proposed measures" – and if they intended to consent to the arbitration of claims concerning "proposed measures" – they would have stated so explicitly in Article 1101(1).

[424] The Claimants rely on *Ethyl Corporation v. Canada* in an attempt to establish the scope of the term "measures". *See* Claimants' Reply, ¶ 406. In that case, the tribunal dismissed a jurisdictional objection maintaining that legislation awaiting Royal Assent did not fall within the scope of NAFTA Chapter Eleven. While Canada disagrees with the *Ethyl* tribunal's reasoning, the policy announcements in the news release (which provide no clear information on how the Premier-Designate's policy intentions would be implemented) stand in stark contrast to the legislation at issue in that case which had been debated, passed and was simply awaiting Royal Assent. *See* **C-187**, *Ethyl – Decision on Jurisdiction*, ¶¶ 68-69.

[425] Claimants' Reply, ¶ 156.

[426] **C-201**, Government of Canada, Guidelines on the conduct of Ministers, Ministers of State, exempt staff and public servants during an election, August 2021.

IV. CANADA HAS NOT VIOLATED ITS NAFTA OBLIGATIONS

A. The Claimants Have Not Established a Violation of NAFTA Article 1105

187. In their Reply, the Claimants criticize Canada's articulation of the minimum standard of treatment, the applicable standard for a denial of justice, and Canada's response to the Claimants' arguments on "arbitrary and discriminatory" conduct and legitimate expectations.[427] Once again, the Claimants rely on an overly broad interpretation of the minimum standard of treatment under NAFTA Article 1105 **(section 1**). They do so despite the NAFTA Parties' repeated and consistent statements that the threshold for finding a breach of NAFTA Article 1105 is high **(a)** and that it is not meant to protect investors against all forms of differential treatment **(b)**. NAFTA Article 1105 only protects against measures that are "manifestly arbitrary" **(c)**.

188. None of the measures challenged by the Claimants amount to a breach of NAFTA Article 1105 (**section 2**). The Claimants cannot use NAFTA Article 1105 to second-guess Ontario's policy rationale for winding down its cap and trade program **(a)**. None of the measures challenged by the Claimants meet the high threshold of arbitrariness **(b)**; and Ontario's implementation of the wind-down, including its approach to compensation, was not "manifestly arbitrary or discriminatory" **(c)**. The NAFTA Parties have confirmed that the minimum standard of treatment under Article 1105 does not protect "legitimate expectations" **(d)**. Finally, the Claimants have failed to establish a denial of justice **(e)**.

1. The Minimum Standard of Treatment Under NAFTA Article 1105 Does Not Provide the Sweeping Guarantee of Protection the Claimants Portray

189. The Claimants argue that Canada "ignores the weight of authority supporting the Claimants' articulation of the FET standard."[428] To the contrary, the Claimants impermissibly attempt to broaden the customary international law minimum standard of treatment of aliens.

[427] Claimants' Reply, ¶ 413.

[428] Claimants' Reply, ¶ 413.

(a) **The Threshold for a Violation of Article 1105 is High**

190. The NAFTA Parties have repeatedly confirmed that the threshold for a violation of NAFTA Article 1105 is high.[429] NAFTA Article 1105 only protects against acts that are "sufficiently egregious and shocking – a gross denial of justice, manifest arbitrariness, a complete lack of due process, evident discrimination, or a manifest lack of reasons."[430] NAFTA Chapter Eleven tribunals have concluded that there must be evidence of egregious conduct or manifestly arbitrary behaviour by the State before the minimum standard of treatment under customary international law is engaged.[431]

191. Further, the NAFTA Parties agree,[432] and NAFTA Chapter Eleven Tribunals have confirmed, that tribunals must afford a high level of deference to a NAFTA Party to make policy decisions and not second-guess the rationale behind those decisions, even if the investor may have preferred a

[429] **RL-159**, *Vento Motorcycles Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/17/3) Canada's Article 1128 Submission, 23 August 2019, ¶ 20; **RL-071**, *Odyssey Marine Exploration, Inc. v. United Mexican States* (ICSID Case No. UNCT/20/1) Non-Disputing Party Submission of the Government of Canada pursuant to NAFTA Article 1128, 2 November 2021 ("*Odyssey Marine – Canada's Article 1128 Submission*"), fn. 22; **RL-160**, *Alicia Grace et al., v. United Mexican States* (ICSID Case No. UNCT/18/4) Article 1128 Submission of the Government of Canada, 24 August 2021 ("*Alicia Grace – Canada's Article 1128 Submission*"), fn. 49. *See also* **RL-161**, *Bilcon et al v. Government of Canada* (UNCITRAL) Counter Memorial of Canada, 9 December 2011, ¶ 321 ("[T]he threshold for proving a violation of that standard is extremely high."); **RL-162**, *Mesa Power Group, LLC v. Government of Canada* (UNCITRAL) Second Article 1128 Submission of Mexico, 12 June 2015 ("*Mesa – Second Article 1128 Submission of Mexico*"), ¶ 8; **RL-163**, *Mesa Power Group, LLC v. Canada* (UNCITRAL) Second Article 1128 Submission of the United States, 12 June 2015 ("*Mesa – Second Article 1128 Submission of the U.S.*"), citing the *Bilcon* award, ¶ 20. As recently confirmed by a NAFTA tribunal in *Westmoreland Mining Holdings LLC v. Canada*, "significant weight" should be given to the views of the NAFTA Parties as articulated in non-disputing party submissions under NAFTA Article 1128 because the NAFTA Parties "have a unique perspective on how the NAFTA should be interpreted and also in recognition of the systemic interests of States in ensuring consistency of interpretation." *See* **RL-131**, *Westmoreland – Final Award*, ¶ 214.

[430] **CL-018**, *Glamis Gold Ltd. v. United States of America* (UNCITRAL) Final Award, 8 June 2009 ("*Glamis Gold – Award*") ¶ 616.

[431] **CL-018**, *Glamis Gold – Award*, ¶ 627. *See also* **CL-017**, *International Thunderbird Gaming Corporation v. United Mexican States* (UNCITRAL) Award, 26 January 2006, ¶¶ 194, 197, 200; **CL-054**, *Cargill, Incorporated v. The United Mexican States* (ICSID Case No. ARB(AF)/05/2) Award, 18 September 2009 ("*Cargill – Award*"), ¶ 286; **RL-044**, *Mobil Investments Canada Inc. v Canada* (ICSID Case No ARB(AF)/07/4) Decision on Liability and on Principles of Quantum, 22 May 2012 ("*Mobil – Decision on Liability*"), ¶ 152; **CL-190**, *Eli Lilly and Company v. Government of Canada* (UNCITRAL) Final Award, 16 March 2017 ("*Eli Lilly – Final Award*"), ¶ 222. *See also* **RL-006**, *Spence – Corrected Interim Award*, ¶ 282.

[432] *See e.g.*, **RL-160**, *Alicia Grace – Canada's Article 1128 Submission*, ¶ 29; **RL-164**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL) Article 1128 Submission of Mexico, 12 January 2016 ("*Windstream – Mexico's Article 1128 Submission*"), ¶ 6; **RL-165**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL) Article 1128 Submission of the United States of America, 18 March 2016, ¶ 21.

different outcome.[433] Where there are rational policy objectives underlying a State's measure, in the absence of some other egregious or manifestly arbitrary behaviour, NAFTA Article 1105 does not protect foreign investors from regulatory changes, even if those changes cause an economic loss to their investments.[434]

(b) The Claimants' Concept of "Discrimination" is Not Protected Under the Minimum Standard of Treatment at Customary International Law

192. In their Memorial, the Claimants alleged that Ontario "targeted a specific class of investors" by not compensating market participants, and that this amounted to a violation of Article 1105 because it lacked a "legitimate justification".[435] Canada responded that the Claimants had not established the existence of any additional elements of the minimum standard of treatment,[436] and explained that Ontario's compensation approach was based on legitimate distinctions between different types of participants in the cap and trade program.[437] The Claimants have not established that the minimum standard of treatment prohibits a State from drawing distinctions based on "classes" of investors or different types of participants in a regulatory regime.

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[433] **CL-064**, *S.D. Myers, Inc. v. Government of Canada* (UNCITRAL) Partial Award, 13 November 2000, ¶ 263 (noting the "high measure of deference that international law generally extends to the right of domestic authorities to regulate within their own borders."); **CL-059**, *Mesa – Award*, ¶ 553 ("In reviewing this alleged breach, the Tribunal must bear in mind the deference which NAFTA Chapter 11 tribunals owe a state when it comes to assessing how to regulate and manage its affairs").

[434] The Claimants' allegation that Canada's position on the content of the minimum standard of treatment under customary international law contradicts its "own practice on this issue" (pointing to Canada's 2021 Model FIPA) is a distraction. *See* Claimants' Reply, ¶¶ 417-418. The treaty at issue here is the NAFTA. Canada's 2021 Model FIPA is not a "subsequent agreement between the parties regarding the interpretation of the [NAFTA] or the application of its provisions", a "subsequent practice in the application of the [NAFTA] which establishes the agreement of the [NAFTA] parties regarding its interpretation", or a "relevant rule[] of international law applicable in the relations between the [NAFTA] parties". *See* VCLT Article 31(3). All NAFTA Parties agree that the burden is on a claimant to demonstrate that the content of the minimum standard of treatment has evolved to include the protections it alleges: **RL-144**, *Lone Pine – 1128 Submission of the United States*, ¶ 30; **RL-162**, *Mesa – Second Article 1128 of Mexico*, ¶ 9. *See also* **CL-018**, *Glamis Gold – Award*, ¶ 601; **CL-054**, *Cargill – Award*, ¶ 273; **CL-057**, *ADF Group, Inc. v. United States of America* (ICSID Case No. ARB(AF)/00/1) Award, 9 January 2003 ("*ADF – Award*"), ¶ 185.

[435] Claimants' Memorial, ¶¶ 369-370.

[436] Canada's Counter-Memorial, ¶¶ 185-186.

[437] Canada's Counter-Memorial, ¶ 205.

193. First, as general matter, customary international law does not preclude a State from treating its own investors more favourably than foreign investors. The *Grand River* Tribunal noted that "neither Article 1105 nor the customary international law standard of protection generally prohibits discrimination against foreign investments."[438] The three NAFTA Parties agree.[439]

194. In any event, there is no evidence that the Claimants were targeted on the basis of their nationality, or any other invidious ground of discrimination. The Claimants rely on [redacted][441] Koch's proposed amendments would have required Ontario to compensate "any market participant related to and acting for, or on behalf of, or in relation to a mandatory participant" – a transparent effort to change the rules specifically for KS&T.[442] [redacted][43]

195. [redacted]

[438] **CL-020**, *Grand River – Award*, ¶ 209; **CL-089**, *Methanex Corporation v. United States of America* (UNCITRAL) Final Award on Jurisdiction and Merits, 3 August 2005, ("*Methanex – Final Award*"), Part IV, Chapter C, p. 7, ¶ 14; **RL-169**, *Mercer International Inc. v. Government of Canada* (ICSID Case No. ARB(AF)/12/3) Award, 6 March 2018 ("*Mercer – Award*"), ¶ 7.60.

[439] **RL-167**, *Mercer International v. Government of Canada*, (ICSID Case No. ARB(AF)/12/3) Submission of the United States, 8 May 2015, ¶ 21)"State practice confirms that there is no 'categorical rule' under customary international law requiring non-discrimination."); **RL-168**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL) Canada's Reply to the 1128 Submissions of the United States and Mexico, January 2016, ¶ 27 ("[a]ll three NAFTA Parties agree that no established rule of customary international law has emerged that generally prohibits any nationality-based discrimination against foreign investors."); **RL-164**, *Windstream – Mexico's Article 1128 Submission*, ¶ 20 ("Mexico also agrees with Canada that Article 1105(1) does not provide a blanket prohibition on discrimination against foreign investors or their investments. Nationality-based discrimination falls under the purview of NAFTA Articles 1102 and 1103, and not Article 1105.")

[440] [redacted]

[441] **RS-086**, Koch Comment on Bill 4.

[442] **RS-086**, Koch Comment on Bill 4.

[443] [redacted]

[redacted][444] There is no discrimination here, let alone the type of egregious and manifestly arbitrary behavior prohibited by customary international law.

(c) NAFTA Article 1105 Only Protects Against Manifestly Arbitrary Measures That Bear No Connection to Reason or Fact

196. The Claimants appear to accept that in order to violate the customary international law minimum standard of treatment, a measure must objectively be "manifestly arbitrary".[445] Measures that are rationally connected to legitimate policy goals will not meet this test.[446]

197. Tribunals have also confirmed that measures adopted by States are not manifestly arbitrary merely because they are based on political reasons. As noted by the tribunal in *Electrabel v Hungary*; "[p]olitics is what democratic governments necessarily address; and it is not, *ipso facto*, evidence of irrational or arbitrary conduct for a government to take into account political or even populist controversies in a democracy subject to the rule of law."[447]

198. In addition, even if Ontario's measures were "illegal" or "*ultra vires*" under domestic law – which they were plainly not – that would not automatically render them manifestly arbitrary under

[444] [redacted]

[445] Claimants' Reply, ¶ 417; Claimants' Memorial, ¶ 352. The Claimants now also agree that Article 1105 does not incorporate "an obligation of regulatory stability". Claimants' Reply, ¶ 436. *See also* **RL-044**, *Mobil – Decision on Liability*, ¶ 153; **RL-090**, *Marvin Roy Feldman Karpa v. United Mexican States* (ICSID Case No ARB(AF)/99/1) Award, 16 December 2002 ("*Feldman – Award*"), ¶ 103.

[446] **CL-190**, *Eli Lilly – Final Award*, ¶ 423 ("The relevant point is that, in the Tribunal's view, the promise doctrine *is rationally connected to these legitimate policy goals*.") (emphasis added); **CL-018**, *Glamis Gold – Award*,, ¶ 803; **CL-069**, *Joshua Dean Nelson v. United Mexican States* (ICSID Case No. UNCT/17/1), Award, 5 June 2020 ("*Nelson – Award*"), ¶ 325. *See also* **RL-099**, *LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. Argentine Republic* (ICSID Case No. ARB/02/1) Decision on Liability, 3 October 2006 ("*LG&E – Decision on Liability*"), ¶ 157, citing *Lauder v. Czech Republic* and Black's Law Dictionary. *See also* **RL-106**, *Lauder (U.S.) v. Czech Republic* (UNCITRAL) Final Award, 3 September 2002.

[447] **CL-085**, *Electrabel S.A.* v. *Republic of Hungary* (ICSID Case No. ARB/07/19) Decision on Jurisdiction, Applicable Law and Liability, 30 November 2012 ("*Electrabel – Decision on Jurisdiction*"), ¶ 8.23 ("In brief, the Tribunal considers that Electrabel's criticism of Hungary's political motives is factually mistaken, particularly in alleging that Hungary's conduct towards the Generators (especially Dunamenti) was induced solely by malign populist pressures, now falsely camouflaged with other ostensibly more rational factors for the purpose of Hungary's defence in these arbitration proceedings.")

NAFTA Article 1105.[448] As the *ADF* tribunal stated, "something more than simple illegality or lack of authority under the domestic law of a State is necessary to render an act or measure inconsistent with the customary international law requirements of Article 1105(1)."[449]

199. NAFTA tribunals have clearly articulated that a measure must be objectively egregious and manifestly arbitrary before it rises to the level of a breach of NAFTA Article 1105. Ontario changing its regulatory framework to accomplish legitimate policy goals and making distinctions between different categories of entities based on their regulatory status simply does not rise to that level.

2. The Claimants Have Not Established a Breach of the Minimum Standard of Treatment under NAFTA Article 1105

200. The Claimants state that they do not challenge Ontario's decision to wind-down its cap and trade program *per se*, but rather the "*manner*" in which it was done.[450] Their Reply indicates otherwise. The Claimants attempt to draw an artificial line between Ontario's decision to wind-up its cap and trade program, on the one hand, and the execution of that decision, on the other. The Claimants are, in fact, challenging Ontario's decision to wind down the cap and trade program and to provide compensation as set out in the *Cancellation Act*.

(a) Ontario's Measures Were Not Manifestly Arbitrary

201. First, the Claimants assert that the challenged measures were "not rationally connected to any legitimate policy objective, and were based on prejudice and bias rather than on reason or fact"

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[448] This has been the consistent position of all three NAFTA Parties. *See* **RL-170**, *Mesa Power Group, LLC v. Canada* (UNCITRAL) Canada's Response to 1128 Submissions, 26 June 2015, ¶ 14; **RL-162**, *Mesa – Second Article 1128 Submission of Mexico*, ¶ 22; **RL-163**, *Mesa – Second Article 1128 Submission of the U.S.*, ¶ 11.

[449] **CL-057**, *ADF – Award*, ¶ 190. *See also* **CL-069**, *Nelson – Award*, ¶ 325 ("The implication of the ELSI standard is that arbitrariness requires more than a showing of illegality under domestic law"); **CL-018**, *Glamis Gold – Award*, ¶ 626 ("a finding of arbitrariness requires a determination of some act far beyond the measure's mere illegality, an act so manifestly arbitrary, so unjust and surprising as to be unacceptable from the international perspective.".) Similarly, tribunals in non-NAFTA cases have also confirmed that illegality under the domestic law of a State is not sufficient in itself to establish a breach of the fair and equitable treatment at customary international law. For instance, in *Saluka v. Poland*, the tribunal confirmed that "something more than simple illegality or lack of authority under the domestic law of a State is necessary to render an act or measure inconsistent with the customary international law requirements." *See* **RL-033**, *Saluka Investments B.V. (The Netherlands) v. The Czech Republic* (UNCITRAL) Partial Award, 17 March 2006, ¶¶ 442-443. *See also* **RL-046**, *Parkerings-Compagniet AS* v. *Republic of Lithuania* (ICSID Case No. ARB/05/8), Award, 11 September 2007, ¶ 315.

[450] Claimants' Reply, ¶ 432 (emphasis in original).

because Ontario did not compensate market participants.[451] As explained in Canada's Counter-Memorial, the newly elected government's decision to cancel Ontario's cap and program was based on the policy objective of removing economically inefficient burdens on Ontarians.[452] In addition, Ontario's decision to compensate capped participants but not market participants had a rational basis premised on *bona fide* distinctions between categories of participants in the regulatory system. As Mr. Wood explains, Ontario's compensation approach was based on legitimate policy grounds informed by the regulatory purpose of the cap and trade system.[453] It does not matter that the Claimants might believe these decisions were "unwise, inefficient or not the best course of action in the circumstances".[454]

202. Second, the Claimants cast Ontario's policy-based compensation rationale as "purely political" and serving "no public purpose" because Ontario would become subject to the federal backstop program.[455] Ontario's compensation approach was based on rational policy distinctions.[456] Differences in social or economic views do not render a policy objective illegitimate, such that a measure is "manifestly arbitrary".[457] As the Claimants know, at the time of the contested measures, Ontario intended to (and then did) challenge the constitutionality of the backstop program in Canadian courts.

203. Third, the Claimants posit that cancellation was "manifestly arbitrary" because of the "clear legal framework" requiring Ontario to "endeavor to provide" 12 months' notice of its intention to

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[451] Claimants' Reply, ¶ 440.

[452] Canada's Counter-Memorial, ¶ 205.

[453] **RWS-3**, Wood – Second Witness Statement, ¶¶ 21-22.

[454] **CL-074**, UNCTAD, Fair and Equitable Treatment 7 (UNCTAD Series on Issues in International Investment Agreements II, United Nations, 2012), p. 78.

[455] Claimants' Reply, ¶ 440.

[456] **RWS-3**, Wood – Second Witness Statement, ¶¶ 21-22.

[457] **CL-054**, *Cargill – Award*, ¶ 292 ("[A] tribunal, in assessing whether an action of a State is arbitrary, need recognize that governments make many potentially controversial choices and, in doing so, may appear to have made mistakes, to have misjudged the facts, proceeded on the basis of a misguided economic or sociological theory, placed too much emphasis on some social values over others and adopted solutions that are ultimately ineffective or counterproductive…' Therefore, an actionable finding of arbitrariness must not be based simply on a tribunal's determination that a domestic agency or legislature incorrectly weighed the various factors, made legitimate compromises between disputing constituencies, or applied social or economic reasoning in a manner that the tribunal criticizes.") (footnote omitted).

withdraw. As set out in Part II, the Claimants have misidentified the applicable legal framework: the Ontario cap and trade program was governed entirely by the *Climate Change Act* and its regulations. In addition, the Claimants' submissions on the Harmonization Agreement are contradicted by the text of the document itself, which stated that it could not be interpreted to "restrict, limit or otherwise prevail over […] each Party's sovereign right and authority to adopt, maintain, modify, repeal or revoke any of their respective program regulations or enabling legislation."[458]

204. Fourth, the Claimants make the sweeping and unsubstantiated assertion that Ontario "violated its own laws" because it "ignored the transition of power" that took place on June 29, when the new government was sworn in.[459] That assertion is factually and legally incorrect.[460] On June 15, 2018, before the new government was sworn-in, the MECP Minister's Delegate decided not to issue an auction notice. This decision was in line with caretaker principles, including not frustrating the incoming government's policy goals.[461] After it took power, the new government lawfully enacted Regulation 386/18 under the *Climate Change Act* on July 3, 2018, and then proceeded to introduce, debate, consult on, modify, and implement the *Cap and Trade Cancellation Act*.[462]

(b) The Claimants' Attempt to Challenge Ontario's "Execution" of the Measures Also Fails

205. The Claimants further argue that Ontario's decisions to cancel the cap and trade program and compensate mandatory participants were executed in an arbitrary and discriminatory manner.[463] These allegations are contradicted by the evidence.

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[458] **R-025**, Harmonization Agreement, Preamble; *see also* Canada's Counter-Memorial, ¶¶ 55, 56, 206, 257, 258; and fn. 394.

[459] Claimants' Reply, ¶ 440.

[460] *See* Section II.D.3.

[461] **RWS-3**, Wood – Second Witness Statement, ¶ 12.

[462] *See* Section II.F. The Claimants also describe Regulation 386/18 as being outside of the "lawful exercise of any discretion granted under Section 70" of the *Climate Change Act*, citing to Canadian court decisions. *See* Claimants' Reply, ¶¶ 81, 85, 498. This is nonsensical. Regulation 386/18 was lawfully made under the *Climate Change Act*. *See* **R-006**, *Climate Change Act*, ss. 78(1), 78(6)-(7). The Claimants elected not to challenge Regulation 386/18 before domestic courts on the basis of excess of discretion (or at all), and cannot attempt to litigate the issue here. In any event, Regulation 386/18 was a policy decision, not a discretionary one, and it fell well within the statutory authority of the *Climate Change Act*.

[463] Claimants' Reply, ¶¶ 439-455.

206. First, KS&T should have understood the regulatory regime governing the Ontario cap and trade program. From the outset, participants knew that the purpose of the regime was carbon emissions abatement, that different rules applied to different categories of participants, and that the *Climate Change Act* did not contain any right to compensation.[464]

207. Second, the Claimants equate "picking winners and losers" to Ontario having applied "the burden of "compliance" […] unevenly across capped sources, with those that purchased allowances losing the value of all allowances required to cover emissions, while those that did not purchase sufficient allowances perversely avoided a similar cost for some of their emissions."[465] Ontario's decision was based on rational distinctions between participants in a regulatory program.[466] In addition, as explained by Mr. Wood, the wind-down of the program was informed by the new government's policy priority of not imposing additional costs on consumers.[467] While the Claimants and others may have preferred a different outcome, Ontario's approach was not arbitrary or discriminatory.

(c) NAFTA Article 1105 Does Not Protect an Investor's Legitimate Expectations, and in Any Event the Government of Ontario Did Not Frustrate Any Legitimate Expectations Held by the Claimants

208. All three NAFTA Parties have consistently stated that NAFTA Article 1105 does not protect an investor's legitimate expectations.[468] The minimum standard of treatment under customary

[464] **R-006**, *Climate Change Act*, ss. 2, 9-18, 70; **R-007**, Regulation 166/16, s. 69.

[465] Claimants' Reply, ¶ 218. [redacted]

[466] *See* Section II.F, above.

[467] See Section II.F, above; **RWS-1**, Wood – First Witness Statement, ¶¶ 19-25; **RWS-3**, Wood – Second Witness Statement, ¶¶ 19-20.

[468] **RL-160**, *Alicia Grace – Canada's Article 1128 Submission*, ¶ 30 ("There is no general obligation under the customary international law minimum standard of treatment, and therefore under Article 1105, to protect an investor's legitimate expectations. The mere fact that a State takes or fails to take an action that may be inconsistent with an investor's expectations does not constitute a breach of the customary international law standard of treatment, even if there is loss or damage to the investment as a result."); **RL-171**, *Eli Lilly and Company v. Government of Canada* (UNCITRAL) Submission of the United States of America, 18 March 2016, ¶ 13 ("The concept of "legitimate expectations" is not a component element of "fair and equitable treatment" under customary international law that gives rise to an independent host State obligation. […] The United States is aware of no general and consistent State practice and *opinio juris* establishing an obligation under the minimum standard of treatment not to frustrate investors' expectations; instead, something more is required than the interference with those expectations."); **RL-172**, *Eli Lilly and Company v.*

international law "is not, and was never intended to amount to, a guarantee against regulatory change, or to reflect a requirement that an investor is entitled to expect no material changes to the regulatory framework within which an investment is made."[469]

209. Despite acknowledging that there is no doctrine of legitimate expectations under the customary international law minimum standard of treatment,[470] the Claimants spend more than nine pages of their Reply arguing that Ontario created and violated their legitimate expectations. Their arguments are without merit.

210. Legitimate expectations are only created where a State has made specific representations to an investor in order to induce an investment, the investor objectively relied on those representations, and the representations were subsequently repudiated by the State.[471] For legitimate expectations to be created, a State must have "induced the expectations in a quasi-contractual manner."[472] A general law or regulation cannot amount to a "specific representation" made by the State to an investor in order to induce an investment.

211. The Claimants argue that they had "legitimate expectations" as a result of the structure of the cap and trade program, general communications from Ontario to all potential cap and trade participants, a public statement from a former Minister, the non-binding Harmonization Agreement, and Ontario's statements regarding an "orderly" wind-down.[473] None of these amount to "specific representations" made by Ontario to the Claimants to "induce their [alleged] investment".[474]

Government of Canada (UNCITRAL) Submission of Mexico, 18 March 2016 ("*Eli Lilly – Submission of Mexico*"), ¶ 15 (Mexico agrees with Canada that the "mere failure to meet an investor's legitimate expectations does not constitute a breach [of] Article 1105(1)").

[469] **RL-044**, *Mobil – Decision on Liability*, ¶ 153. *See also* **RL-050**, *Robert Azinian, Kenneth Davitian, & Ellen Baca v. The United Mexican States* (ICSID Case No. ARB (AF)/97/2) Award, 1 November 1999 ("*Azinian – Award*"), ¶ 83 ("NAFTA was not intended to provide foreign investors with blanket protection from this kind of disappointment, and nothing in its terms so provides.")

[470] Claimants' Reply, ¶ 489.

[471] **RL-044**, *Mobil – Decision on Liability*, ¶ 152; **CL-018**, *Glamis Gold – Award*, ¶ 627.

[472] **CL-018**, *Glamis Gold – Award*, ¶ 799.

[473] Claimants' Reply, ¶ 493.

[474] Ontario's statements regarding the orderly wind down of its cap and trade program cannot have induced any investments for the additional reason that they took place *after* any alleged investment.

212. Even if such allegations are considered (which is unnecessary), they each fail. First, the structure of the cap and trade program could not support a legitimate expectation that all participants would be compensated when the program was wound down.[475] Among other things, Ontario's cap and trade regulations drew distinctions between market participants and compliance entities based on the regulatory nature of the program.[476] Second, Ontario's information sessions and general outreach to potential cap and trade participants could not create any legitimate expectation that market participants would be compensated.[477] Third, far from having any expectation of the longevity of the Ontario cap and trade system,[478] the Claimants thought that [redacted] [80] Fourth, the Claimants' view of the Harmonization Agreement cannot be reconciled with the clear language of the agreement itself.[481] Finally, Ontario's wind-down of the cap and trade program was, in fact, orderly. As demonstrated in Canada's Counter-Memorial and set out in detail in Part II.F.2 above, Ontario followed a well-established process that falls far short of internationally wrongful conduct.

(d) The Claimants Have Not Established a Denial of Justice

213. In their Reply, the Claimants take issue with Canada's submissions on the scope of Crown immunity clauses and the prerequisite of an exhaustion of domestic remedies.

214. The fact that the *Cancellation Act* imposed limitations on court action does not *ipso facto* result in a violation of customary international law. The NAFTA tribunal in *Mondev v. United States*

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[475] Claimants' Reply, ¶ 495.

[476] **RWS-3**, Wood – Second Witness Statement, ¶¶ 4-5. *See also* **R-006**, *Climate Change Act*, ss. 9-18.

[477] *See* **RWS-3**, Wood – Second Witness Statement, ¶¶ 4-5.

[478] Claimants' Reply, ¶ 496.

[479] [redacted]

[480] [redacted]

[481] Canada's Counter-Memorial, ¶¶ 55, 56, 206, 257, 258, and fn. 394; [redacted] California understood the agreement in a similar manner. *See* **R-076**, *The United States of America v. The State of California*, Declaration of Rajinder Sahota in Support of State Defendants' Opposition to Plaintiff's Summary Judgement Motion and State Defendants' Cross-Motion for Summary Judgement, 2:19-cv-02142-WBS-EFB, 9 March 2020 ("*Declaration of Rajinder Sahota*") ¶¶ 66, 70.

recognized that statutory immunity provisions will be justified in certain circumstances, including where allowing liability claims would result in a "distraction to the work of the [Government]."[482] The Claimants try to differentiate between the *Mondev v. United States* award and the facts of this case by arguing that the statutory immunity in that were applied narrowly to a public specialized agency – the Boston Redevelopment Authority ("BRA") – and that the specialized functions of this agency made it more susceptible to being sued and could have resulted in a distraction to its work.[483] But the Claimants ignore the fact that section 10 of the *Cancellation Act* created a statutory immunity only in relation to acts performed under the *Climate Change Act* and the *Cancellation Act*. Therefore, while the BRA benefited from complete statutory immunity from suit for intentional torts for all of the work it performed over the years, section 10 of the *Cancellation Act* only conferred immunity from suit for specific actions related to the *Climate Change Act* and *Cancellation Act*.

215. Further, as explained in Canada's Counter-Memorial, a denial of justice under customary international law presumes that the claimant has exhausted local remedies, as long as they are adequate, effective and reasonably available and not "obviously futile". [484] Here, it was open to the Claimants to challenge the legality of the Crown immunity provision in the *Cancellation Act* – they chose not to do so, with the consequential effect of precluding the Claimants from bringing a denial of justice claim under NAFTA Article 1105.

216. As noted in Canada's Counter-Memorial, other market participants have instituted a class action lawsuit in domestic court against the Government of Ontario based on the wind-down of its cap and trade program and enactment of the *Cancellation Act*.[485] The plaintiffs in domestic court are

[482] **CL-056**, *Mondev International Ltd. v. United States of America* (ICSID Case No. ARB(AF)/99/2) Award, 11 October 2002, ¶ 153.

[483] Claimants' Reply, ¶ 465.

[484] Canada's Counter-Memorial, ¶ 213. All NAFTA Parties agree on this. *See* **RL-160**, *Alicia Grace – Canada's Article 1128 Submission*, ¶ 36; **RL-173**, *Loewen Group, Inc. and Raymond L. Loewen v. United States of America* (ICSID Case No. ARB(AF)/98) Response of the United States of America to the November 8, 2001 Submissions of the Governments of Canada and Mexico, 7 December 2001, p. 8; **RL-174**, *Loewen Group, Inc. and Raymond L. Loewen v. United States of America* (ICSID Case No. ARB(AF)/98) Second Article 1128 Submission of the United Mexican States, 9 November 2001, pp. 8-9.

[485] **R-081**, SMV Energy Solutions, Notice of class proceeding including a claim for damages pursuant to s. 18(1) of the Crown Liability and Proceedings Act, 16 December 2020; **R-082**, *SMV Energy Solutions v. Ontario*, ONSC, Amended Statement of Claim, 28 July 2021.

challenging, among other things, the constitutionality of the same provision that the Claimants contest before this Tribunal.[486] The burden lies with the Claimants to establish why it would have been "obviously futile" to make a similar challenge. As confirmed by the tribunal in *Philip Morris v. Uruguay*: "[i]t is for the Claimants to show that this condition has been met or that no remedy was available giving 'an effective and sufficient means or redress' or that, if available, it was 'obviously futile'."[487]

217. Similarly, the *Apotex* tribunal explained that there must be an actual "attempt" by a prospective claimant to exhaust local remedies before it can make a denial of justice claim:

> As against this, Apotex submits that because the chances of a successful outcome were "*unrealistic*", a petition to the U.S. Supreme Court was "objectively futile", or to be treated as if unavailable. In effect, the Tribunal is being asked to determine the likelihood of a successful result before the U.S. Supreme Court – which the Tribunal does not consider is its proper task, or indeed the correct enquiry. In the words of Judge Lauterpacht, in *Norwegian Loans* case:
>
> > [H]owever contingent and theoretical these remedies may be, an attempt ought to have been made to exhaust them.[488]

218. The Claimants cannot simply argue that a domestic challenge would have been "futile" without relying on evidence and without having made an attempt to challenge the Crown immunity provision found in section 10 of the *Cancellation Act*.

B. The Claimants Have Failed to Establish a Violation of NAFTA Article 1110

219. The Claimants' NAFTA Article 1110 arguments fare no better. In their Reply, they argue that Canada indirectly expropriated their alleged investments[489] through the Premier-Designate's

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[486] **R-081**, SMV Energy Solutions, Notice of class proceeding including a claim for damages pursuant to s. 18(1) of the Crown Liability and Proceedings Act, 16 December 2020; **R-082**, *SMV Energy Solutions v. Ontario*, ONSC, Amended Statement of Claim, 28 July 2021.

[487] **RL-048**, *Philip Morris Brand Sàrl (Switzerland), Philip Morris Products S.A. (Switzerland) and Abal Hermanos S.A. (Uruguay) v. Oriental Republic of Uruguay* (ICSID Case No. ARB/10/7) Award, 8 July 2016, ¶ 503 (Internal references omitted).

[488] **RL-030**, *Apotex – Award on Jurisdiction and Admissibility*, ¶ 288 (emphasis in original, references omitted).

[489] The Claimants' claims under NAFTA Article 1110 concern the following overlapping "investments": (1) "the Claimants' ability to 'use, enjoy, or dispose of its investment' in carbon allowances"; (2) "KS&T's investment in a carbon trading business, which included the emission allowances that KS&T purchased at Ontario auctions through its Ontario

announcement on June 15, 2018 and "the subsequent introduction of" Regulation 386/18 on July 3, 2018.[490] They allege that these two events "*individually and collectively* amounted to *an* indirect expropriation".[491] But the same alleged investments cannot be indirectly expropriated twice on two different dates. Similarly, the Claimants argue that the enactment of the Cancellation Act on October 31, 2018 "subsequently, directly expropriated" the emission allowances.[492] Again, the same "investment" cannot be expropriated twice.

220. The Claimants' allegations lack coherence and should be dismissed on this basis alone. But they also fail on both the law and the facts. In the sections that follow, Canada explains that the Claimants: 1) misstate the legal standard for expropriation, and have failed to demonstrate the existence of a property right or property interest capable of being expropriated; and, in any event, 2) have not established that Ontario indirectly expropriated any of their alleged property rights; and 3) cannot establish direct expropriation.

221. Because Canada has not expropriated any of the Claimants' alleged investments either indirectly or directly, there is no need for the Tribunal to consider paragraphs (a) through (d) of NAFTA Article 1110(1).[493] However, even if the Tribunal finds that the Claimants' investments have been expropriated, Ontario's measures were adopted for a public purpose, on a non-discriminatory basis, and in accordance with due process of law and NAFTA Article 1105(1).[494]

CITSS account"; and (3) "the Claimants' investment in the emission allowances held in KS&T's Ontario CITSS account." *See* Claimants' Reply, ¶ 515.

[490] Claimants' Reply, ¶ 512; Claimants' Memorial, ¶ 401.

[491] Claimants' Reply, ¶¶ 587, 610. *See also* Canada's Counter-Memorial, ¶ 220 and fn. 410.

[492] Claimants' Reply, ¶¶ 512, 610.

[493] The Claimants also do not dispute that the question whether there has been an expropriation and whether the four criteria in paragraphs (a)-(d) of NAFTA Article 1110(1) have been satisfied are two distinct questions, and that paragraphs (a)-(d) come into play only if the Tribunal decides that there has been an expropriation. *See* Canada's Counter-Memorial, ¶ 230 and fn. 419; Claimants' Memorial, ¶¶ 422-423; Claimants' Reply, ¶ 606.

[494] Canada agrees that no compensation was paid to the Claimants because KS&T, as a market participant, was ineligible for compensation under the *Cancellation Act*.

1. The Claimants Have Not Demonstrated the Existence of a Property Right Capable of Being Expropriated

(a) A Measure by a Party Cannot Constitute an Expropriation unless It Interferes with a Tangible or Intangible Property Right or Property Interest

222. Canada's Counter-Memorial explained that it is a rule of customary international law that, in order to constitute an expropriation, a property right or property interest must have been taken.[495] Whether there is an investment capable of being expropriated under NAFTA Article 1110 is independent from the question of whether there is an investment under Article 1139.[496] In their Reply, the Claimants argue that Canada "mischaracterizes the standard provided in Article 1110" and "misstates the order and structure of analysis for determining whether the Claimants hold rights capable of being expropriated".[497] The Claimants do not dispute that Article 1110 incorporates customary international law rules on expropriation, but argue that "this does not mean that customary international overcomes the *lex specialis* of Chapter Eleven and, particularly, the express language of Article 1110 itself."[498] The Claimants misunderstand Canada's position and the applicable legal standard.

223. First, arbitral jurisprudence[499] and commentators[500] confirm that, under customary international law, expropriation concerns property rights and property interests. In *EMV v. Czech Republic*, the tribunal made clear that "whether the contractual rights on which the Claimant relies constitute an

[495] Canada's Counter-Memorial, ¶ 235.

[496] Canada's Counter-Memorial, ¶¶ 235-237.

[497] Claimants' Reply, ¶ 516.

[498] Claimants' Reply, ¶¶ 525-526 and fns. 844-846.

[499] **CL-088**, *Fireman's Fund – Award*, ¶ 176(c); **RL-058**, *Corn Products – Decision on Responsibility*, ¶¶ 87(c), 91; **CL-020**, *Grand River – Award*, ¶ 154; **RL-075**, *Generation Ukraine – Award*, ¶¶ 6.2 and 8.8; **RL-108**, *Oxus Gold plc v. Republic of Uzbekistan* (UNCITRAL) Final Award, 17 December 2015 ("*Oxus Gold – Final Award*"), ¶¶ 298 and 301; **RL-175**, *Almasryia for Operating & Maintaining Touristic Construction Co. L.L.C. v. State of Kuwait* (ICSID Case No. ARB/18/2) Award on the Respondent Application under Rule 41(5) of the ICSID Arbitration Rules, 1 November 2019 ("*Almasryia – Award on Rule 41(5)*"), ¶¶ 58, 62.

[500] **RL-079**, Rosalyn Higgins, "The Taking of Property by the State: Recent Developments in International Law", 176 R.C.A.D.I. 259 (1982), p. 272 ("[O]nly *property* deprivation will give rise to compensation.") (emphasis in original); **RL-080**, Rudolf Dolzer, "Indirect Expropriation of Alien Property", (1986) 1 ICSID Review – Foreign Investment Law Journal 41, (1986), p. 41; **RL-086**, Newcombe & Paradell, pp. 322-323, ¶ 7.2; **RL-027**, McLachlan, Shore, Weiniger, p. 360, ¶ 8.03; **RL-084**, UNCTAD Series on International Investment Agreements II, "Expropriation: A Sequel", (United Nations: New York and Geneva, 2012) ("UNCTAD – Expropriation: A Sequel"), pp. 5-6.

investment" and "whether those rights are capable of expropriation" are "entirely separate questions."[501] The tribunal noted that the "essence of expropriation is a taking of property by the State"[502] and that there was "no inconsistency in holding that rights to performance under a contract with a private party constitute an investment but not one which is capable of being expropriated" because "[p]rotection against expropriation is not the only safeguard which the [t]reaty affords to investments".[503]

224. Recently, the tribunal in *Eskosol v. Italy* emphasized that "the doctrine of expropriation involves deprivation of protected rights in property" and that "a finding of expropriation must be premised on a showing that 'Claimants must have held a property right of which they have been deprived.'"[504] Similarly, in *Eurus Energy v. Spain* the tribunal pointed that an expropriation guarantee in an investment treaty "is concerned with the protection of property interests" and "is not intended to protect the wider range of interests associated with the idea of reasonable or legitimate expectations."[505]

225. In *Emmis v. Hungary*, the tribunal emphasized that, because under the applicable BIT "the only cause of action within the [t]ribunal's jurisdiction is that of expropriation, [c]laimants must have held a *property right* of which they have been deprived."[506] The tribunal dismissed the expropriation claim

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[501] **RL-082**, *European Media Ventures SA v. Czech Republic* (UNCITRAL) Partial Award on Liability, 8 July 2009 ("*European Media – Partial Award on Liability*"), fn. 4.

[502] **RL-082**, *European Media – Partial Award on Liability*, ¶¶ 47, 50(1).

[503] **RL-082**, *European Media – Partial Award on Liability*, ¶ 63. The tribunal concluded that the claimant's rights under a contract for the transfer of a telecommunications license were capable of being expropriated. *See* **RL-082**, *European Media – Partial Award on Liability*, ¶ 65.

[504] **RL-092**, *Eskosol S.p.A. in liquidazione v. Italian Republic* (ICSID Case No. ARB/15/50) Award, 4 September 2020 ("*Eskosol – Award*"), ¶ 470, citing **CL-010**, *Emmis – Award*, ¶ 159. In *Eskosol*, there was no dispute that the claimant was a shareholder in 12 special purpose entities that held land rights for the construction of solar power plants in Italy. The tribunal concluded, however, that the claimant "cannot show that it had a recognized property right" to enhance the value of its assets through participation in the repealed electricity tariff regime. *See* **RL-092**, *Eskosol – Award*, ¶¶ 122, 471-472.

[505] **RL-176**, *Eurus Energy Holdings Corporation v. Kingdom of Spain* (ICSID Case No. ARB/16/4) Decision on Jurisdiction and Liability, 17 March 2021 ("*Eurus Energy – Decision on Jurisdiction and Liability*"), ¶ 256. The claimant held shares in 13 Spanish special purpose companies that owned and operated wind farms in Spain. However, the claimant's expropriation claim failed "because the right claimed to have been expropriated", i.e. the claimant's alleged right to a feed-in tariff, "was not an acquired right susceptible of expropriation." **RL-176**, *Eurus Energy – Decision on Jurisdiction and Liability*, ¶¶ 3, 259, 266, 274.

[506] **CL-010**, *Emmis – Award*, ¶ 159 (emphasis added).

because the "injustices" allegedly perpetrated upon the claimants in the tendering process for a new broadcasting license did not "meet the basic requirement of a *property right*."[507] Similarly, in *Accession Mezzanine v. Hungary*, the tribunal concluded that, had it "found that the [c]laimants had vested rights under Hungarian law to the exploitation of radio frequencies at the critical date of the alleged expropriation, the claim for expropriation would only have been cognisable in respect of rights that had the characteristics of *property rights* under Hungarian law."[508]

226. International courts have also rejected claims that a customer base or goodwill, by themselves, are property that can be the subject of an expropriation. In the *Oscar Chinn* case before the Permanent Court of International Justice (**PCIJ**), the PCIJ denied an expropriation claim for failure to identify a property right.[509] In that case, a British river carrier operator claimed that the Belgian Congo had expropriated its property when it increased government funding for a state-owned competitor that resulted in the competitor being granted a *de facto* monopoly. In denying the claim, the PCIJ held that it was "unable to see in [the claimant's] original position – which was characterized by the possession of customers … anything in the nature of a genuine vested right"[510] and emphasized that "[f]avourable business conditions and goodwill are transient circumstances, subject to inevitable changes."[511]

227. The Claimants argue that "it is well-established that principles of customary international law, codified by the ILC Articles, only apply 'save to the extent that they are excluded by provisions of the NAFTA as *lex specialis*'" and that Canada "has itself previously argued that propositions of

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[507] **CL-010**, *Emmis – Award*, ¶ 255 (emphasis added). The claimants, who had an investment by way of their shares in a Hungarian company that held a broadcasting license, complained that they were mistreated in a new license tendering process. *See* **CL-010**, *Emmis – Award*, ¶¶ 5, 155.

[508] **RL-081**, *Accession Mezzanine et al. v. Hungary* (ICSID Case No. ARB/12/3) Award, 17 April 2015 ("*Accession Mezzanine – Award*"), ¶ 158 (emphasis added). Similar to *Emmis v. Hungary*, the dispute concerned the claimants' investment in a Hungarian company that held a broadcasting license. **RL-081**, *Accession Mezzanine – Award*, ¶ 2.

[509] **RL-179**, *Oscar Chinn (U.K. v. Belg.)*, 1934 Judgement of 12 December 1934, P.C.I.J. (ser. A/13) No. 63 ("*Oscar Chinn – Judgment*"), p. 88.

[510] **RL-179**, *Oscar Chinn – Judgment*, p. 88.

[511] **RL-179**, *Oscar Chinn – Judgment*, p. 88, cited in **RL-099**, *LG&E – Decision on Liability*, ¶ 197; **CL-019**, *Merrill & Ring Forestry L.P. v. The Government of Canada* (UNCITRAL) Award, 31 March 2010 ("*Merrill & Ring – Award*"), ¶¶ 141, 215; and **RL-017**, *El Paso Energy International Company v. Argentine Republic* (ICSID Case No. ARB/03/15) Award, 31 October 2011 ("*El Paso – Award*"), ¶ 366.

customary international law are displaced by the specific terms of the NAFTA."[512] The Claimants entirely miss the point. Canada has never argued that the ILC Articles, which are the result of both codification and progressive development of the rules of international law concerning the responsibility of States for internationally wrongful acts,[513] constitute a complete codification of customary international law rules on *expropriation*. Moreover, none of the cases they rely on in support of this statement are relevant to this dispute. In *ADM v. Mexico* and *Corn Products v. Mexico*, the tribunals considered the provisions of the ILC Articles concerning *countermeasures.*[514] In *UPS v. Canada*, a case that did not involve any allegation of expropriation, the tribunal agreed with Canada's position that NAFTA Chapter Fifteen provides a *lex specialis* regime in relation to the attribution of acts of monopolies and state enterprises.[515]

228. Nothing in the "express language" of NAFTA Article 1110 suggests that something not capable of being expropriated under customary international law may be expropriated under NAFTA Chapter Eleven, and the Claimants provided no evidence that NAFTA Article 1110 broadens the scope of customary international law rules on expropriation.

229. Second, the NAFTA Parties recently "confirm[ed] their shared understanding" in CUSMA that "[a]n action or a series of actions by a Party cannot constitute an expropriation unless it interferes

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[512] Claimants' Reply, ¶¶ 525-526, referring to **RL-058**, *Corn Products – Decision on Responsibility*, ¶ 76; **CL-079**, *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc. v. United Mexican States*, (ICSID Case No. ARB(AF)/04/5) Award, 21 November 2007 ("*ADM – Award*"), ¶¶ 117, 119; **CL-195**, *United Parcel Service of America Inc. v. Government of Canada* (UNCITRAL) Award on the Merits, 24 May 2007, ¶¶ 54, 62-63; **CL-196**, *United Parcel Service of America Inc. v. Government of Canada* (UNCITRAL) Government of Canada, Counter-Memorial (Merits Phase), 22 June 2005, ¶¶ 804-806.

[513] *See* **CL-051**, Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries", Report of the International Law Commission on the work of its fifty-third session (2001) ("ILC Articles"), General Commentary, p. 31, ¶ 1 (emphasis added). In a resolution concerning the ILC Articles, the United Nations General Assembly "expresse[d] its appreciation" to the ILC "for its continuing contribution to the codification and progressive development of international law", "t[ook] note" of the ILC Articles and "commend[ed] them to the attention of Governments without prejudice to the question of their future adoption or other appropriate action". *See* **RL-180**, United Nations General Assembly, "Resolution 56/83", 12 December 2001, pp. 1-2. Therefore, many – but not necessarily all – provisions of the ILC Articles reflect customary international law on the responsibility of States for their internationally wrongful acts.

[514] **RL-058**, *Corn Products – Decision on Responsibility*, ¶¶ 59, 62, 73, 76, 145-149, 158-159, 186-188; **CL-079**, *ADM – Award*, ¶¶ 113-123, 125, 148.

[515] **CL-195**, *United Parcel Service of America Inc. v. Government of Canada* (UNCITRAL) Award on the Merits, 24 May 2007, ¶¶ 47-49, 54-55, 59, 62-63, 76-78; **CL-196**, *United Parcel Service of America Inc. v. Government of Canada* (UNCITRAL) Government of Canada, Counter-Memorial (Merits Phase), 22 June 2005, ¶¶ 803-807.

with a tangible or intangible property right or property interest in an investment."[516] The Claimants argue that NAFTA Article 1110 "contains no such language" and instead "prohibits the expropriation of 'an investment', which is broadly defined in Article 1139 (and not limited to *property* rights or interests)."[517] However, the NAFTA Parties have consistently agreed that Article 1110 recognizes the expropriation of property rights or property interests only.[518] Under VCLT Article 31(3), when interpreting NAFTA Article 1110, the Tribunal shall take into account these consistent statements by NAFTA Parties either as a "subsequent agreement between the parties regarding the interpretation of the [NAFTA] or the application of its provisions" or as a "subsequent practice in the application of the [NAFTA] which establishes the agreement of the parties regarding its interpretation".[519] Further, by "confirming" their "shared understanding" in CUSMA Annex 14-B, the NAFTA Parties have made it clear that, whether or not explicitly mentioned in NAFTA Chapter Eleven, a finding of expropriation necessarily requires the existence of a "property right or property interest in an investment." Under VCLT Article 31(3)(c), when interpreting Article 1110(1), the Tribunal "shall" take CUSMA Annex 14-B into account as "relevant rules of international law applicable in the relations between the [P]arties."[520]

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[516] Canada's Counter-Memorial, ¶¶ 231-232; **RL-074**, Canada United States Mexico Agreement ("CUSMA"), Annex 14-B: Expropriation, ¶ 1.

[517] Claimants' Reply, ¶ 518 (emphasis in original).

[518] **RL-068**, *Methanex Corporation v. United States of America* (UNCITRAL) Amended Statement of Defence of Respondent United States of America, 5 December 2003, ¶ 392; **RL-177**, *Methanex – U.S. Memorial on Jurisdiction*, pp. 33-35; **RL-182**, *Grand River Enterprises Six Nations, Ltd. and others v. United States of America,* (UNCITRAL) Statement of Defence of the United States of America, 29 April 2005, ¶ 120; **RL-069**, *Glamis Gold, Ltd. v. United States of America* (UNCITRAL) Counter Memorial of the United States of America, 19 September, p. 119 and fn. 563; **RL-144**, *Lone Pine – 1128 Submission of the United States*, ¶¶ 9-10; **RL-178**, *Alicia Grace et al., v. United Mexican States* (ICSID Case No. UNCT/18/4) Article 1128 Submission of the United States, 24 August 2021 ("*Alicia Grace – United States Article 1128 Submission*"), ¶¶ 55-56; **RL-183**, *Odyssey Marine Exploration, Inc. v. United Mexican States* (ICSID Case No. UNCT/20/1) United States Article 1128 Submission, 2 November 2021 ("*Odyssey Marine – US Article 1128 Submission*"), ¶ 24; **RL-184**, *Methanex Corporation v. United States of America* (UNCITRAL) Fourth Article 1128 Submission of the Government of Mexico, 30 January 2004 ("*Methanex – Mexico's Fourth 1128 Submission*"), ¶¶ 6 and 8; **RL-172**, *Eli Lilly – Submission of Mexico*, ¶ 18; **CL-062**, *Windstream Energy, LLC v. Government of Canada* (UNCITRAL) Government of Canada Rejoinder Memorial, 6 November 2015, ¶¶ 79-82; **RL-071**, *Odyssey Marine – Canada's Article 1128 Submission*, ¶¶ 25-28.

[519] **RL-029**, Vienna Convention on the Law of Treaties, Art. 31(3)(a), (b).

[520] **RL-029**, Vienna Convention on the Law of Treaties, Art. 31(3)(c); Canada's Counter-Memorial, ¶ 231 and fn. 426; NAFTA Article 1131(1): ("A Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law.").

230. The Claimants erroneously cite *Chemtura v. Canada* in support of their argument that "if an investment by a claimant is held to fall within the definition of Article 1139, it is *prima facie* capable of being expropriated."[521] However, the *Chemtura v. Canada* tribunal emphasized that the first question was whether the claimant had "an investment in Canada capable of being expropriated",[522] and the disputing parties agreed that the investment allegedly expropriated was the claimant's Canadian enterprise (Chemtura Canada).[523] The tribunal considered that elements such as "goodwill, customers or market share" may "be seen as accessories of an 'enterprise'", and noted that it did not need to determine whether such elements, or the claimant's alleged "'lindane business' in Canada", could be considered as investments *per se*.[524] The *Chemtura v. Canada* tribunal did not decide that "goodwill", "customers", "market share" or "lindane business" were independently capable of being expropriated. In any event, KS&T's alleged "carbon trading business" could not be a part or an "accessory" of an "enterprise" expropriated by Canada because KS&T did not have an "enterprise" in Canada. Accordingly, the first step of the expropriation analysis is to identify the specific investment alleged to have been expropriated and to determine whether there is a valid property right or property interest capable of being expropriated.[525]

(b) The Claimants Have Failed to Prove that KS&T Held a Valid Property Right Capable of Being Expropriated

231. In their Reply, the Claimants allege that Ontario has expropriated "property in the form of emissions allowances purchased in May 2018 … as an investment acquired in the expectation or used for the purpose of economic benefit or other business purposes" and "interests arising from the commitment of capital or other resources in the territory of a Party to economic activity in such

[521] Claimants' Reply, ¶ 522.

[522] **CL-067**, *Chemtura Corporation v. Government of Canada* (UNCITRAL) Award, 2 August 2010 ("*Chemtura – Award*"), ¶¶ 257(i), 258.

[523] **CL-067**, *Chemtura – Award*, ¶ 258 and fn. 1. The claimant's subsidiary was an "enterprise" within the meaning of Article 1139(a), and the first part of the test under NAFTA Article 1110 was satisfied.

[524] **CL-067**, *Chemtura – Award*, ¶¶ 243, 258. Lindane is a pesticide that used to be produced by Chemtura Canada. *See* **CL-067**, *Chemtura – Award*, ¶¶ 6, 14, 23, 49.

[525] Canada's Counter-Memorial, ¶ 233. *See also* **RL-176**, *Eurus Energy – Decision on Jurisdiction and Liability*, ¶ 259: ("[I]t is necessary to ask, first, what rights are identified by the Claimant as having been expropriated.")

territory … through – *inter alia* – the Claimants' broader carbon trading business".[526] Further, the Claimants argue that the allowances held in KS&T's Ontario CITSS account "together with the Claimants' broader carbon trading business" are "capable of being expropriated."[527]

232. Canada and the Claimants agree that international law does not create property rights and, when faced with a claim of expropriation, a NAFTA tribunal must first undertake a *renvoi* to the domestic law of the Party in question in order to determine the existence, nature, and scope of the property interests that the claimants allege were taken.[528] Under Ontario law, the Claimants did not have vested property rights or property interests capable of being expropriated in either the emission allowances or in KS&T's alleged "broader carbon trading business in Ontario".

(i) KS&T's Emission Allowances Were Not Capable of Being Expropriated

233. The Claimants have not established that emission allowances are property under Ontario law.[529] To the contrary, since there is no legislative declaration of judicial decision that has yet added them to the category of property, emission allowances currently lack the legal status of property in Ontario.[530] Moreover, emission allowances are compliance instruments whose nature is "fundamentally an immunity from penalty".[531] This type of interest is not capable of constituting property because it lacks the core attributes of common law property, particularly exclusive control and use.[532]

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[526] Claimants' Reply, ¶ 528.

[527] Claimants' Reply, fn. 849.

[528] Canada's Counter-Memorial, ¶ 238; Claimants' Reply, ¶ 530. *See also* **RL-084**, UNCTAD – Expropriation: A Sequel, p. 22; **RL-027**, McLachlan, Shore, Weiniger, p. 379, ¶ 8.64; **CL-201**, *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (ICSID Case No. ARB/06/2) Award, 16 September 2015, ¶ 135; **CL-106**, *Vestey Group – Award*, ¶ 257; **RL-185**, *Gavrilovic and Gavrilovic d.o.o. v. Republic of Croatia*, (ICSID Case No. ARB/12/39) Award, 26 July 2018, ¶ 432; **RL-175**, *Almasryia – Award on Rule 41(5)*, ¶ 58; **RL-176**, *Eurus Energy – Decision on Jurisdiction and Liability*, ¶ 266.

[529] *See* Section III.C.1; **RER-3**, Katz – Second Expert Report; Canada's Counter-Memorial, ¶¶ 137-151, 244; **RER-1**, Katz – Expert Report, ¶ 83. *See also* **RER-2**, Litz – First Expert Report, ¶¶ 47, 51.

[530] *See* Section III.C.1(a); **RER-3**, Katz – Second Expert Report, ¶¶ 6, 29-35.

[531] Section III.C.1(b); **RER-3**, Katz – Second Expert Report, ¶¶ 8, 36-51. *See also* Canada's Counter-Memorial, ¶¶ 29, 139, 149-151; **RER-1**, Katz – First Expert Report, ¶¶ 9 and 60-65.

[532] Section III.C.1(c); **RER-3**, Katz – Second Expert Report, ¶¶ 9-10, 52-90.

(ii) KS&T's Alleged "Broader Carbon Trading Business in Ontario" Was Not Capable of Being Expropriated

234. The Claimants argue that their alleged "rights in a broader carbon trading business in Ontario" are "*prima facie* capable of being expropriated under Article 1110",[533] and support this argument by referencing statements from several cases to the effect that contractual rights are capable of being expropriated.[534]

235. However, the Claimants have not even identified the elements of KS&T's alleged ("carbon trading business in Ontario") beyond its involvement in cross-border sales of emission allowances,[535] let alone established the existence of any vested property right in the alleged "business". The Claimants provided no valuation of their alleged "business", and do not seek any damages for its loss.[536]

236. Nor do the Claimants allege that Ontario expropriated any contract that "gives rise to an asset owned by the claimant to which a monetary value may be ascribed."[537] In fact, other than [redacted] [39] – the Claimants have not identified any contracts the performance of which had allegedly been affected by Ontario's measures.

237. Instead, the Claimants argue that Ontario "destroyed" KS&T's "business model", "ability to trade … in the carbon market of Ontario" and "ability to transfer or receive emission allowances".[540]

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[533] Claimants' Reply, ¶ 537.

[534] Claimants' Reply, ¶ 536.

[535] Canada's Counter-Memorial, ¶¶ 3, 222, 307-310; Claimants' Memorial, ¶¶ 141, 409, 491; Claimants' Reply, ¶¶ 49, 297, 303, 383, 395, 534, 650-656. Canada's Rejoinder, Sections II.B and II.C.

[536] Claimants' Reply, ¶¶ 611, 656.

[537] **CL-010**, *Emmis – Award*, ¶ 169. In any event, "pure contractual rights" cannot be expropriated or "equated with property rights." *See* **RL-081**, *Accession Mezzanine – Award*, ¶¶ 153-156.

[538] [redacted]

[539] Claimants' Memorial, ¶¶ 496-501.

[540] Claimants' Memorial, ¶¶ 201, 213, 409, 418; Claimants' Reply, ¶¶ 170, 543, 551.

However, only vested property rights are capable of being expropriated.[541] Under Ontario law, there was no guarantee that KS&T's alleged "business model" would remain viable or that Ontario would not make changes to, replace or cancel its cap and trade program. KS&T's "business model" and ability to transact in emission allowances were not vested property rights, and were not capable of being expropriated under NAFTA Article 1110.[542]

238. In their Reply, the Claimants argue that "NAFTA tribunals have clearly recognized that an investment including market share, customers, and goodwill can be recognized as part of the overall investment in question."[543] However, none of the four cases cited by the Claimants – *Pope & Talbot*

[541] Canada's Counter-Memorial, ¶¶ 239-241. *See also* **CL-019**, *Merrill & Ring – Award*, ¶¶ 140, 142 (finding that "[e]xpropriation cannot affect potential interests"); **RL-108**, *Oxus Gold – Final Award*, ¶¶ 298, 301 (concluding that the claimant "did not secure an unconditional right to develop the [mineral deposit] through a concession agreement, but only a right to formal, exclusive and good faith negotiations", and that "a right to formal negotiations cannot be subject to an 'expropriation' … because it lacks the nature of proprietary right"); **RL-176**, *Eurus Energy – Decision on Jurisdiction and Liability*, ¶¶ 266, 274; **RL-125**, *Pawlowski AG and Project Sever s.r.o. v. Czech Republic* (ICSID Case No. ARB/17/11) Award, 1 November 2021 ("*Pawlowski – Award*"), ¶¶ 702-703.

[542] Canada's Counter-Memorial, ¶¶ 242, 246, 253. It is also undisputed that only participants registered in Ontario's cap and trade program were allowed to have an Ontario CITSS account, to apply to participate in emission allowance auctions, and to transact on the secondary market (i.e. to "transfer or receive emission allowances"), and that these rights were not capable of being alienated.

[543] Claimants' Reply, ¶ 538.

v. Canada,[544] *Methanex v. United States*,[545] *Chemtura v. Canada*,[546] and *Merrill & Ring v. Canada*[547] – support the Claimants' allegation that KS&T's "business development, marketing and trading activities"[548] and the emission allowances held in KS&T's Ontario CITSS account,[549] "*form part of the value* of its investment which was expropriated by Ontario."[550]

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[544] In *Pope & Talbot v. Canada*, the claimant's investment was its subsidiary incorporated in British Columbia, Canada, and the tribunal considered that "the Investment's access to the U.S. market" was "a property interest subject to protection under Article 1110". *See* **CL-086**, *Pope & Talbot Inc. v. Government of Canada* (UNCITRAL) Interim Award, 26 June 2000 ("*Pope & Talbot – Interim Award*"), ¶¶ 2, 96. This decision, therefore, does not support the Claimants' argument that something other than a *property* right is capable of being expropriated. The *Pope & Talbot* tribunal also failed to consider whether, under Canada's domestic law, access to a foreign market had "fundamental characteristics of property". Neither Canada nor other NAFTA Parties consider access by an enterprise to a foreign market to be a "property interest". *See* **RL-186**, *Methanex Corporation v. United States of America* (UNCITRAL) Second Article 1128 Submission of Canada, 30 April 2001, ¶¶ 56, 62; **RL-145**, *Methanex – Mexico's Second 1128 Submission*, ¶¶ 18-21; **RL-187**, *Marvin Roy Feldman Karpa v. United Mexican States* (ICSID Case No ARB(AF)/99/1) Canada's Second Article 1128 Submission, 28 June 2001, ¶ 20, 23-24. *See also* **RL-023** Kinnear: Investment Disputes under NAFTA, p. 1110-37.

[545] In *Methanex v. United States*, the claimant's investments were its two subsidiaries in Delaware and Texas. The tribunal concluded that "items such as goodwill and market share" may constitute "an element of the value of an enterprise and as such may have been covered by some of the compensation payments", and "in a comprehensive taking, these items may figure in valuation. But it is difficult to see how they might stand alone". *See* **CL-089**, *Methanex – Final Award*, p. II-A-2, ¶¶ 4-6, p. IV-A-1, ¶ 1, and p. IV-D- 8, ¶ 17 (emphasis added). *See also* **RL-023** Kinnear: Investment Disputes under NAFTA, p. 1110-40: ("This view is consistent with that of the OECD … that intangibles such as market share or market access are not stand-alone investments liable to expropriation.")

[546] In *Chemtura v Canada*, the allegedly expropriated investment was Chemtura Canada (an "enterprise" within the meaning of Article 1139(a)), and the tribunal noted that elements such as "goodwill or market position may indeed be seen as accessories of an 'enterprise', which is *per se* an investment under Article 1139 of NAFTA." The tribunal also acknowledged that it "does not need to determine whether such elements may be considered as investments *per se*, as the Claimant has expressly recognized that this was not its argument". *See* **CL-067**, *Chemtura – Award*, ¶ 243 and fn. 1.

[547] In *Merrill & Ring v. Canada*, the claimant alleged that its "interest in realizing fair market value for its logs on the international market" had been expropriated. The tribunal reasoned that while "property such as the lands, logs or timber … will be protected under Article 1139(h), just as intangible interests arising from a contract directly related to the investment will be protected," the claimant's alleged right was excluded from the scope of NAFTA Article 1139. The tribunal considered that "[t]his was in fact the kind of situation envisaged in *Methanex* in respect of goodwill and in its conclusion that goodwill cannot be considered as a standalone vested right". *See* **CL-019**, *Merrill & Ring – Award*, ¶¶ 140-141.

[548] The Claimants argue that these "activities" include KS&T's "broader carbon trading business" and "efforts … to build an enterprise of trading in Ontario emission allowances over the course of several years as part of a sustained, long-term business plan". However, KS&T did not have an "enterprise" in Canada, and the Claimants produced no business plans for KS&T's alleged "business in Ontario".

[549] The Claimants refer to "the Claimants' CITSS account". However, only registered participants could have an account, and the *Climate Change Act* prohibited registered participants from holding emission allowances on behalf of another, and from transacting in emission allowances with unregistered persons. *See* **R-006**, ss. 21, 22, 28. It is undisputed that the account holder was KS&T and that Koch Industries was not a registered participant.

[550] Claimants' Reply, ¶ 539 (emphasis added).

239. This statement mischaracterizes the NAFTA jurisprudence: several NAFTA tribunals merely held "market share, customers or goodwill" may be taken into account as an element of the value of an enterprise. The Claimants thus confuse (i) the requirement that a finding of a breach of NAFTA Article 1110 requires that the claimant had a vested property right capable of being expropriated, and (ii) the possibility that, if a claimant's enterprise is expropriated, items such as goodwill or market share may be taken into account for valuation purposes. KS&T undisputedly did not have an enterprise in Ontario, and its alleged "carbon trading business", "activities" and "efforts" clearly do not constitute property rights or property interests capable of being expropriated.

240. In sum, because KS&T held no property rights capable of being expropriated, no further analysis under NAFTA Article 1110 is required. For the sake of completeness, Canada explains that the claim would fail regardless because it fails to meet the international law requirements for there to have been either a direct or indirect expropriation.

2. In Any Event, the Claimants Have Not Established That Ontario Indirectly Expropriated Any of Their Alleged Property Rights

241. The Claimants' arguments on indirect expropriation fail because (a) Ontario did not interfere with the Claimants' distinct, reasonable investment-backed expectations; (b) Ontario's actions on June 15, 2018 did not substantially deprive KS&T of the economic value of its alleged property rights; and (c) the contested measures constitute a valid exercise of police powers by Ontario.

(a) Ontario's Measures Did Not Interfere with the Claimants' Distinct, Reasonable Investment-Backed Expectations

242. Canada and the Claimants agree that NAFTA tribunals have considered claimants' distinct investment-backed expectations as a relevant factor in determining whether there has been an indirect expropriation.[551] The Claimants, however, disagree with Canada on two points.

243. First, Canada explained that Article 1110 does not eliminate the normal commercial risks of a foreign investor, or place on a NAFTA Party the burden of compensating for the failure of a business

[551] Canada's Counter-Memorial, ¶ 248; Claimants' Reply, ¶ 556.

plan that was not prudent in the circumstances.[552] The Claimants argue that their alleged business "was profitable, and thriving", and that the Claimants' alleged losses were "not a result of a 'persistently uneconomic' business model, questionable investments during financial crises or an attempt to take advantage of an ambiguous decision with no underlying rationale".[553]

244. KS&T voluntarily decided to participate in Ontario's cap and trade program in order to bid in Ontario emission allowance auctions, accumulate allowances in its Ontario CITSS account during 2017, and promptly transfer emission allowances to its California CITSS account once California and Ontario harmonized their cap and trade programs.[554] In 2018, KS&T continued to participate in emission allowance auctions as an Ontario-registered market participant [redacted] deposited by the three jurisdictions into KS&T's Ontario CITSS account, to its California CITSS account.[555]

245. In the lead-up to the May 2018 auction, KS&T knew that cancelling Ontario's cap and trade program was a major element of the Progressive Conservative Party's electoral platform,[556] and that emission allowances would be deposited into the CITSS accounts of successful bidders only on June 11, after the election.[557] [redacted] [58] KS&T also ought to have been aware that, under the *Climate Change Act*, there was no right to compensation, no expropriation, and no amount payable by the government with respect to actions or inactions under

[552] Canada's Counter-Memorial, ¶¶ 249-250; **RL-050**, *Azinian – Award*, ¶ 83; **CL-012**, *Waste Management – Award*, ¶¶ 160, 177; **RL-090**, *Feldman – Award*, ¶ 112; **CL-012**, *Waste Management – Award*, ¶¶ 160, 177; **CL-088**, *Fireman's Fund – Award*, ¶¶ 184, 218; **CL-069**, *Nelson – Award*, ¶ 281; **RL-094**, *Eudoro Armando Olguín v. Republic of Paraguay* (ICSID Case No. ARB/98/5) Award, 6 July 2001 ("*Olguin – Award*"), ¶ 65(b).

[553] Claimants' Reply, ¶ 558.

[554] Canada's Counter-Memorial, ¶¶ 48-51, 57, 124.

[555] Canada's Counter-Memorial, ¶¶ 60-65, 75-76, 124; Canada's Rejoinder, Section II.C.

[556] *See* Canada's Rejoinder, Section II.C; Canada's Counter-Memorial, ¶¶ 66-71.

[557] *See* Canada's Rejoinder, Section II.C; Canada's Counter-Memorial, ¶¶ 72-74, 76.

[558] Canada's Rejoinder, Section II.C; [redacted]

the Act.[559] Ontario did not make any specific commitments to the Claimants that KS&T's "business model" would be successful or that the province would not change, replace or cancel its cap and trade program.[560] Nor did the Harmonization Agreement impose any enforceable limitations on Ontario's ability to amend its legislation or replace its cap and trade program with a different regulatory regime.[561] KS&T decided to bid in the May 2018 auction nonetheless.

246. The Claimants argue that KS&T "had no reasonable opportunity to sell or transfer the emissions allowances before the Ontario government abruptly and arbitrarily took measures which effectively froze the Claimants' CITSS account."[562] This is false: KS&T repeatedly transferred emission allowances from its Ontario CITSS account to its California CITSS account in the past,[563] and intended to do so again following the May 2018 auction.[564] The reason KS&T did not transfer emission allowances from Ontario to its California CITSS account was entirely self-inflicted: [redacted]

[559] *See* Canada's Counter-Memorial, ¶¶ 40-41, 99-100, 142, 146, 209, 245, 254; **R-006**, *Climate Change Act*, s. 70.

[560] Canada's Counter-Memorial, ¶¶ 179, 195, 207-212, 224, 246, 252-257. *See also* **CL-089**, *Methanex – Final Award*, p. IV-D-5, ¶¶ 9-10 ("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 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.*") (emphasis added); **CL-020**, *Grand River – Award*, ¶¶ 144-145.

[561] *See* Canada's Rejoinder, Section II.A.3; Canada's Counter-Memorial, ¶¶ 55-56, 179, 206, 257-258 and fn. 394; **R-076**, *Declaration of Rajinder Sahota*, ¶ 66 ("The 2017 agreement did not link the three programs. Those links were established independently by each jurisdiction's promulgation of its own linkage regulations.") and ¶ 70 ("The provision relating to withdrawal from the agreement states that the parties will try to provide 12-months notice before withdrawing. As the express text of the agreement indicates, this is an expression of an intention to 'endeavour' to provide this notice. It does not, and was not intended to, prevent any party to the agreement from withdrawing unilaterally or without providing 12-months notice.")

[562] Claimants' Reply, p. 196; ¶ 557.

[563] *See* Canada's Rejoinder, Section II.B.2; Canada's Counter-Memorial, ¶¶ 57, 63; [redacted]

[564] [redacted]

[redacted] [65]

247. The Claimants further argue that they "considered the business risks associated with investing in Canada, and reasonably expected – based on the express representations of Ontario – that Ontario would uphold the rule of law if it sought to withdraw from the Cap and Trade Program in the longer-term."[566] The Claimants failed to provide any contemporaneous evidence proving that they properly analyzed "the business risks associated with investing in Canada".[567] Instead, their Reply merely refers to statements by former Minister Murray that it is "difficult", "very hard" or "almost impossible" to "undo" a cap and trade program.[568] Such references are not a suitable substitute for proper due diligence, which would have required the Claimants to consider the legal framework governing Ontario's cap and trade program, including the clear statement in the *Climate Change Act* that there was no right to compensation, no expropriation, and no amount payable by the government with respect to actions or inactions under the *Act*.[569]

248. Second, Canada explained that NAFTA Chapter Eleven does not guarantee that the regulatory regime governing an investment will not change.[570] The Claimants' Reply states that "this is not the Claimants' argument"[571] and that, unlike in *Feldman v. United States* and *Methanex v. United States*, "the legislative changes in question were abrupt, arbitrary and not backed by any scientific study or

[565] *See* Canada's Rejoinder, Section II.C.

[566] Claimants' Reply, p. 196; ¶ 557.

[567] *See* ¶¶ 30, 50 and fns. 54, 125, above.

[568] Claimants' Reply, ¶¶ 45, 97, 282; **CWS-5**, Martin – Reply Witness Statement, ¶ 22; **C-195**, Graeme Martin, ON C&T Forum Notes, 28 April 2017: "Minister Murray – C&T program difficult to undo" [redacted]; **C-196**, Tvo Today, Transcript: "Turning Over a New Leaf", 27 September 2017, p. 11: "It's very hard to undo cap and train [sic].."; **R-046**, Argus Media, "Carbon auction suggests optimism over Ontario", 24 May 2018: "Former environment minister Glen Murray … has said that it will be 'almost impossible' for someone to undo the program".

[569] Canada's Counter-Memorial, ¶¶ 40-41, 99-100, 142, 146, 209, 245, 254; **R-006**, *Climate Change Act*, s. 70.

[570] Canada's Counter-Memorial, ¶¶ 251-252; **RL-050**, *Azinian – Award*, ¶ 83; **RL-090**, *Feldman – Award*, ¶ 112; **CL-089**, *Methanex – Final Award*, p. IV-D-5, ¶¶ 9-10: **CL-020**, *Grand River – Award*, ¶¶ 144-145.

[571] Claimants' Reply, ¶ 559.

careful consideration."[572] In fact, the changes were neither abrupt nor arbitrary.[573] Further, it was supported by evidence such as the 2016 Auditor-General's report.[574]

249. Canada and the Claimants agree that the reasonableness of the Claimants' expectations must be assessed at the time the Claimants made their alleged investments.[575] In their Reply, the Claimants claim that "because Ontario had for years acknowledged and promoted the role of market participants in Cap and Trade", the Claimants had "legitimate expectations" that "their position within the structure of the Cap and Trade Program would be respected, even in the case of a withdrawal," and that "they would not be the subject of unfair targeting".[576]

250. As demonstrated in Canada's Counter-Memorial and further explained above, Ontario's cap and trade program contemplated a limited role for market participants.[577] When the new government of Ontario decided to wind down the provincial cap and trade program in an orderly fashion, there were valid policy reasons to include certain categories of participants, including market participants, from eligibility for compensation.[578]

(b) Nothing Ontario Did on June 15, 2018 Substantially Deprived KS&T of the Economic Value of Its Alleged Property Rights

251. Canada and the Claimants agree that, for a NAFTA Chapter Eleven tribunal to find that an investment has been expropriated, there must be a taking of fundamental ownership rights, either directly or indirectly, that causes a "substantial deprivation" of economic value of the investment.[579]

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[572] Claimants' Reply, fn. 932.

[573] Canada's Counter-Memorial, ¶¶ 175, 177-178, 200-205, 276.

[574] Canada's Counter-Memorial, ¶¶ 68, 273 and fns. 117-118, 502-503; **R-036**, Minister of the Environment and Climate Change, 2016 Annual Report of the Office of the Auditor General of Ontario, Chapter 3 Section 3.02, pp. 149, 150, 167 and 174-175; **R-037**, Office of the Auditor General of Ontario, News Release "Ontario's Cap and Trade Will Not Significantly Lower Emissions Within the Province by 2020: Auditor General".

[575] Canada's Counter-Memorial, ¶ 248; Claimants' Reply, ¶ 561.

[576] Claimants' Reply, ¶ 561.

[577] *See* Canada's Rejoinder, Section II.A.2; **RER-4**, Litz – Second Expert Report, ¶¶ 23-34. *See also* Canada's Counter-Memorial, ¶ 256; **RER-2**, Litz – First Expert Report, ¶¶ 43, 77-83.

[578] Canada's Counter-Memorial, ¶¶ 95-97, 205, 276.

[579] Canada's Counter-Memorial, ¶ 259; Claimants' Reply, ¶ 541.

252. Canada maintains that nothing Ontario did on June 15, 2018 substantially deprived KS&T of the economic value of its alleged property rights.[580] The statement issued by the Premier-Designate did not, and could not, change the law of Ontario, cancel compliance obligations of capped participants, or prohibit participants from transferring emission allowances.[581] In their Reply, the Claimants argue that the Premier-Designate's action "directly led to the [*sic*] 'the market for Ontario-held carbon allowances [being] essentially frozen as of 15 June 2018'", and that by withdrawing from future auctions, "Ontario effectively, and permanently destroyed KS&T's business model in Ontario, and totally impaired the use, enjoyment and disposal of its investment in emissions allowances in Ontario."[582]

253. In reality, it was California that decided to de-link its CITSS registry from Ontario on June 15, 2018,[583] even though California had other options to safeguard the integrity of its system in light of Ontario's intended future withdrawal.[584] The Claimants are complaining about the decision of California to delink its CITSS accounts from Ontario's accounts,[585] and contemporaneous documents show that KS&T thought that California had [redacted] and [redacted] them.[586]

254. The Ontario legal framework governing emission allowances remained the same until July 3, 2018, when Regulation 386/18 – made under the *Climate Change Act* – came into force.[587] Until July 3, 2018, emission allowances retained their essential characteristics of an immunity from penalty for

[580] Canada's Counter-Memorial, ¶¶ 259-264.

[581] *See* Canada's Rejoinder, Section III.E; Canada's Counter-Memorial, ¶ 263.

[582] Claimants' Reply, ¶ 549.

[583] *See* Canada's Rejoinder, Section II.E; **C-105**, ICE, Notice: California Carbon Allowances Futures Contracts – Changes to Deliverable Allowances in the Compliance Instrument Tracking System Service, 18 June 2018.

[584] *See* Canada's Rejoinder, Section II.3; **RER-4**, Litz – Second Expert Report, ¶¶ 35-54.

[585] Claimants' Memorial, ¶¶ 196-197; **C-104**, California Air Resources Board, Market Notice, 15 June 2018; **CWS-2**, Martin – First Witness Statement, ¶¶ 51-52: On June 15, 2018, "California and Québec delinked registries with Ontario. … As a result of these preventative moves by California and Québec, the market for Ontario-held carbon allowances was essentially frozen as of 15 June 2018."; [redacted] Canada's Counter-Memorial, ¶¶ 288, 297, 301; Canada's Rejoinder, ¶ 86.

[586] Canada's Rejoinder, ¶¶ 7, 86; [redacted]

[587] *See* Canada's Rejoinder, Sections II.F.2, and III.C.1; Canada's Counter-Memorial, ¶¶ 83-85, 263; **R-006**, *Climate Change Act*, s. 70.

emitting GHG pollution,[588] and KS&T could trade in emission allowances with other participants in Ontario's cap and trade program, including with its own related participants (Invista or Komsa).

(c) Ontario's Measures Constituted a Valid Exercise of Police Powers Under International Law

255. As explained in Canada's Counter-Memorial, police powers are recognized by customary international law and NAFTA Article 1110,[589] and Ontario's measures satisfy the test for a valid exercise of police powers.[590]

(i) Police Powers Are Recognized by Customary International Law, as Reflected in NAFTA Article 1110

256. Canada and the Claimants agree that a measure that constitutes a valid exercise of police powers is not expropriatory and does not require payment of compensation.[591] As explained in Canada's Counter-Memorial, NAFTA Chapter Eleven does not limit the State's police powers under customary international law.[592]

257. While determining which measures fall within the police powers category may be a "hard question",[593] Canada set out a clear test – firmly rooted in customary international law and recently confirmed by all three NAFTA Parties in the CUSMA – that "[n]on-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations, except in rare

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[588] *See* Canada's Rejoinder, Section III.C.1(b); **RER-3**, Katz – Second Expert Report, ¶¶ 8-10, 51, 91; **RER-1**, Katz – First Expert Report, ¶¶ 9, 60-65.

[589] Canada's Counter-Memorial, ¶¶ 265-270.

[590] Canada's Counter-Memorial, ¶¶ 271-278.

[591] Canada's Counter-Memorial, ¶¶ 265-271; Claimants' Memorial, ¶¶ 407, 412, 415, 418; Claimants' Reply, ¶¶ 563-568, 574. *See also* Claimants' Reply, ¶ 6 ("[T]he Claimants take no position on whether or not Ontario acted correctly in abolishing the Program …; that decision is indeed one of sovereign policy.") and ¶ 664 ("The Claimants do not and have not questioned Ontario's sovereign right to change its policy direction.")

[592] Canada's Counter-Memorial, ¶ 268, citing **RL-023**, Kinnear: Investment Disputes under NAFTA, p. 1110-50. *See* Claimants' Reply, ¶ 568: "is not disputed between the Parties" that "NAFTA tribunals have recognized that the police powers doctrine applies to Chapter Eleven claims"; **RL-084**, UNCTAD, Expropriation: A Sequel, UNCTAD Series on Issues in International Investment Agreements II (United Nations: New York and Geneva, 2012), pp. 85-86

[593] Claimants' Reply, ¶¶ 567-568, citing **RL-023**, Kinnear: Investment Disputes under NAFTA, p. 1110-50.

circumstances."[594] In their Reply, the Claimants seek to artificially limit the scope of the State's right to regulate.

258. The State's police powers are not limited to "measures adopted by States to protect 'public order, health or morality'".[595] In fact, States may adopt measures to pursue various public welfare objectives, including, but not limited to, "health, safety and the environment".[596] The NAFTA Parties explicitly preserved this flexibility.[597]

259. Canada does not argue that there is "a blanket exception for regulatory measures" or that "a general regulation issued by a State and interfering with the rights of foreign investors can never be considered expropriatory".[598] Canada agrees that a non-discriminatory measure designated and applied to protect legitimate public welfare objectives may, "in rare circumstances" where "it cannot be reasonably viewed as having been adopted and applied in good faith", constitute an indirect expropriation.[599] However, the relevant question is whether the impugned measure has been adopted or applied in bad faith. The Claimants' attempt to import a broad proportionality test into an expropriation analysis under NAFTA Article 1110 ignores that the principle of proportionality is not recognized as part of the minimum standard of treatment of aliens under customary international law[600] and, in the context of police powers, was not mentioned in either the *U.S. Restatement of*

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[594] **RL-074**, CUSMA, Annex 14-B: Expropriation, ¶ 3(b). *See* Canada's Counter-Memorial, ¶¶ 232, 266, 268. This approach has also been consistently supported by NAFTA Parties. *See* Canada's Counter-Memorial, ¶¶ 231-232 and fns. 423-424; **RL-144**, *Lone Pine – 1128 Submission of the United States*, ¶¶ 16-17; **RL-178**, *Alicia Grace – United States Article 1128 Submission*, ¶¶ 58, 63; **RL-183**, *Odyssey Marine – US Article 1128 Submission*, ¶¶ 26, 31; **RL-184**, *Methanex – Mexico's Fourth 1128 Submission*, ¶ 13; **RL-188**, *Lone Pine Resources Inc., v. Government of Canada* (UNCITRAL) Article 1128 Submission of Mexico, 16 August 2017, ¶¶ 7-9.

[595] *See* Claimants' Reply, ¶ 565.

[596] Canada's Counter-Memorial, ¶¶ 265-268; **RL-090**, *Feldman – Award*, ¶ 103. *See* Claimants' Reply, ¶ 574(a) (referring to "public welfare objectives *such as* health, safety and the environment") (emphasis added).

[597] Canada's Counter-Memorial, ¶ 268. The preamble to the NAFTA indicates that the Governments of Canada, Mexico and the United States "resolved to", in particular, "PRESERVE their flexibility to safeguard the public welfare".

[598] Claimants' Reply, ¶¶ 570-571, quoting **CL-086**, *Pope & Talbot Inc. v. The Government of Canada*, UNCITRAL, Interim Award (26 June 2000), ¶ 99 and **RL-017**, *El Paso Energy International Company v. Argentine Republic*, ICSID Case No. ARB/03/15, Award (31 October 2011), ¶ 234. The Claimants' reliance on these decisions is, therefore, inapposite.

[599] Claimants' Reply, ¶ 573.

[600] *See e.g.*, **RL-189**, *Resolute Forest Products Inc. v. Government of Canada* (UNCITRAL) Comments by the Government of Canada in Response to the Second NAFTA Article 1128 Submissions, 8 May 2020, ¶ 4; **RL-190**, *Resolute Forest Products Inc. v. Government of Canada* (UNCITRAL) Second Submission of the United States of America, 10

Foreign Relations Law or the *Harvard Draft Convention on the International Responsibility of States for Injuries to Aliens* (on which the Claimants rely).[601] It must therefore be rejected.

260. Canada maintains that the exercise of the State's police powers must not be subjected to undue second-guessing by arbitral tribunals.[602] For instance, in *Invesmart v. Czech Republic*, the tribunal rejected the claimant's argument that the respondent acted in bad faith because, in revoking the banking license, it opted for a more costly option than granting the state aid requested by the claimant's bank:

> This argument mischaracterises the concept of bad faith. A government cannot be accused of acting in bad faith *merely because it chooses one of several policy alternatives*. Even where the course of action adopted is capable of criticism there is no showing of bad faith absent egregious intent.[603]

261. As demonstrated in Canada's Counter-Memorial, and further shown below, Ontario's measures (a) were designed and applied to protect legitimate public welfare objectives and were non-discriminatory in their application, and (b) did not constitute one of rare cases where regulatory

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April 2020, ¶ 23; **RL-191**, *Mason Capital L.P. and Mason Management LLC v. Republic of Korea*, (UNCITRAL) United States Article 11.20.4 Submission, 1 February 2020, ¶ 23. Arbitral tribunals have considered that they need only to determine whether a measure has a rational connection to a legitimate public policy goal, i.e. that a measure is not arbitrary or irrational. *See* **CL-190**, *Eli Lilly and Company v. Government of Canada* (ICSID Case No. UNCT/14/2) Final Award, 16 March 2017, ¶¶, 426, and 428; **CL-065**, *GAMI Investments, Inc. v. Government of the United Mexican States* (UNCITRAL) Final Award, 15 November 2004, ¶ 114; **CL-018**, *Glamis Gold Ltd. v. United States of America* (UNCITRAL) Final Award, 8 June 2009 ("*Glamis Gold –Award*"), ¶ 805; **CL-085**, *Electrabel – Decision on Jurisdiction*, ¶ 8.35.

[601] Claimants' Memorial, ¶ 412 and fn. 518; Claimants' Reply, fns. 900, 956; **CL-119**, Harvard Draft Convention on the International Responsibility of States for Injuries to Aliens (1961), Art. 10(5); **RL-104**, Restatement of the Law (Third), Foreign Relations Law of the United States (1987), s. 712, Commentary g, cited in **RL-090**, *Feldman – Award*, ¶¶ 103-105; **RL-017**, *El Paso – Award*, ¶ 238; **CL-018**, *Glamis Gold – Award*, ¶ 354; **RL-089**, *Suez – Decision on Liability*, ¶ 139. *See also* **RL-084**, UNCTAD, Expropriation: A Sequel, UNCTAD Series on Issues in International Investment Agreements II (United Nations: New York and Geneva, 2012), pp. 97("The principle of proportionality is not universally recognized as relevant in the expropriation context."), 98 ("It must be kept in mind that international law has traditionally afforded States a wide margin of discretion with respect to questions such as priority of the public purpose or suitability of the measure."), and 100.

[602] *See* Canada's Counter-Memorial, ¶¶ 187, 274, 278; **RL-169**, *Mercer – Award*, ¶ 7.42; **RL-043**, *Invesmart – Award*, ¶ 501; **RL-109**, *Rusoro Mining Ltd. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB(AF)/12/5, Award, 22 August 2016, ¶ 385; **CL-015**, *TECO Guatemala Holdings, LLC v. Republic of Guatemala*, ICSID Case No. ARB/10/23, Award (19 December 2013), ¶ 490; **CL-198**, Olympic Entertainment Group AS v. Republic of Ukraine, PCA Case No. 2019-18, Award (15 April 2021), ¶¶ 94-95; **RL-084**, UNCTAD, Expropriation: A Sequel, UNCTAD Series on Issues in International Investment Agreements II (United Nations: New York and Geneva, 2012), pp. 92-93; **RL-102**, Christie: What Constitutes a Taking of Property under International Law, pp. 332, 338.

[603] **RL-043**, *Invesmart – Award*, ¶¶ 428-430 (emphasis added).

measures "cannot be reasonably viewed as having been adopted and applied in good faith". As a result, they constituted a valid exercise of police powers.

(ii) Ontario Measures Were a Valid Exercise of Police Powers

262. In its Counter-Memorial, Canada explained that Ontario's measures were designed and applied to protect legitimate public welfare objectives, and that the Claimants' arguments fail to put Ontario's measures into their proper context.[604] In their Reply, the Claimants argue that "Ontario's measures bore no plausible relationship to the protection of the environment".[605]

263. Ontario's new government considered that the existing cap and trade program increased gas prices and imposed additional costs on Ontario's households and businesses, but did not meet the province's environmental goals.[606] Therefore, the new government sought to promptly adopt measures that would lower the gas prices and reduce the costs for Ontario households while protecting the environment in a comprehensive way.[607] The Claimants allege that Ontario cancelled

[604] Canada's Counter-Memorial, ¶¶ 272-276. *See also* Canada's Counter-Memorial, ¶ 68; **R-036**, Minister of the Environment and Climate Change, 2016 Annual Report of the Office of the Auditor General of Ontario, pp. 149, 150, 167; **R-037**, Office of the Auditor General of Ontario, News Release "Ontario's Cap and Trade Will Not Significantly Lower Emissions Within the Province by 2020: Auditor General", 30 November 2016.

[605] Claimants' Reply, ¶ 581.

[606] Canada's Counter-Memorial, ¶¶ 67-68, 273.

[607] *See* **RWS-3**, Wood – Second Witness Statement, ¶¶ 18-20, 31; **RWS-1**, Wood – First Witness Statement, ¶¶ 17-18, 33-35; **C-111**, Ontario Government News Release, "Ontario Introduces Legislation to End Cap and Trade Carbon Tax Era in Ontario", 25 July 2018("The proposed legislation will also include measures to help replace the cap-and-trade carbon tax with a better plan for achieving real environmental goals."); **C-175**, Hansard Transcript, Legislative Assembly of Ontario, 31 July 2018, per Minister Phillips, pp. 485 ("While we understand the challenges that climate change presents, we do not believe that the solution is a regressive tax. It's a punishing tax that forces poor and middle-class Ontario families to pay more for basic things like heating their homes or fuelling their cars.") and 487 ("We'll deliver real action on providing clean air, clean water, conservation, reducing emissions and cleaning up litter, garbage and waste. With the proposed legislation, we have an opportunity to usher in a new era of economically prudent, effective environmental action that will also protect families."); **C-125**, Ontario Government News Release, "Relief on the Way: Ontario Passes Legislation to End Cap and Trade Carbon Tax", 31 October 2018("The elimination of the cap and trade carbon tax will reduce gas prices, save the average family $260 per year, and remove a costly burden from Ontario businesses, allowing them to grow, create jobs and compete around the world. … Later this fall, Ontario will release a comprehensive, made-in-Ontario environment plan to help protect and conserve our air, land and water, address urban litter and waste, increase our resilience to climate change and help all of us do our part to reduce greenhouse gas emissions.").

its cap and trade program "for political reasons" because the province "merely replaced one carbon pricing regime with another – and one that imposed a higher cost on Ontario tax payers."[608]

264. The Claimants' arguments are similar to those made in *Electrabel v. Hungary*, where the claimants alleged that Hungary caused the prices payable to the claimant-owned electrical utility (Dunamenti) to be reduced for "inappropriate political reasons", *i.e.* in order to "keep consumer electricity prices artificially low".[609] The tribunal agreed that "there was political and public controversy in Hungary over the perceived high level of profits made by Hungarian Generators", but considered that "politics is what democratic governments necessarily address; and it is not, *ipso facto*, evidence of irrational or arbitrary conduct for a government to take into account political or even populist controversies in a democracy subject to the rule of law."[610] The tribunal also noted that "the Hungarian Government did not itself resort to populist language directed at Dunamenti."[611]

265. Similarly, while there may have been vigorous public debate as to what policies are more effective at protecting the environment without imposing unnecessary costs on Ontario households, that does not support the Claimants' argument that Ontario's measures "bore no plausible relationship to the protection of the environment".[612] The Government of Ontario released its environmental plan, designed to "reduce greenhouse gas emissions and help[] communities and families prepare for climate change", for public consultation on November 29, 2018[613] and continued to develop its EPS program.[614] On January 1, 2019, the province became subject to the federal backstop,[615] which the

[608] Claimants' Reply, ¶ 582.

[609] **CL-085**, *Electrabel – Decision on Jurisdiction*, ¶¶ 2.11, 7.6, 7.11, 7.21, 8.8.

[610] **CL-085**, *Electrabel – Decision on Jurisdiction*, ¶ 8.23.

[611] **CL-085**, *Electrabel – Decision on Jurisdiction*, ¶ 8.23.

[612] Claimants' Reply, ¶ 582.

[613] *See* **RWS-3**, Wood – Second Witness Statement, ¶¶ 30-31; **RWS-1**, Wood – First Witness Statement, ¶¶ 33-35; Canada's Counter-Memorial, ¶¶ 103-104; **R-062**, Ontario, Preserving and Protecting our Environment for Future Generations: A Made-in-Ontario Environment Plan, 29 November 2018, p. 2 ("2018 Environment Plan"); **R-063**, Ontario, News Release, "Ontario Releases Plan to Protect the Environment", 29 November 2018.

[614] Canada's Rejoinder, Section II.F.4; **RWS-1**, Wood – First Witness Statement, ¶ 35; **RWS-3**, Wood – Second Witness Statement, ¶¶ 32-33.

[615] Canada's Rejoinder, Section II.F.4; **RS-104**, Environment and Climate Change Canada, "Pan-Canadian Approach to Pricing Carbon Pollution: Interim Report 2020," 2021, p. 8.

new government had challenged as unconstitutional.[616] In July 2019, the Government of Ontario made a regulation that detailed how the EPS program would work and which entities would be covered,[617] and in September 2021 the federal government accepted Ontario's EPS program as an acceptable alternative to the federal output-based pricing system ("OBPS").[618] The EPS program replaced the federal OBPS in Ontario as of January 1, 2022.[619]

266. In other words, it was evident that Ontario's new plan had environmental protection as its goal. Any policy debate as to whether Ontario's preferred approach was a more or less costly or more or less effective at protecting the environment than what existed previously is not relevant for the police powers analysis under international law. It is not for a NAFTA Chapter Eleven tribunal to decide whether one policy option selected by a government was "better" or "preferable" to another. Rather, the only relevant question is whether the measure is non-discriminatory and pursues legitimate public welfare objectives – if so, and it plainly did in this case, the measure will not constitute an indirect expropriation, except in rare circumstances (which are not present here) where the measure cannot be reasonably viewed as having been adopted and applied in good faith.

267. Second, Canada explained that Ontario's measures were non-discriminatory: several other categories of participants were excluded for legitimate policy reasons.[620] In their Reply, the Claimants allege that "Ontario had arbitrarily targeted a specific class of investors" and that it was "politically expedient to throw market participants like KS&T under the bus".[621] In support of their misguided allegations, the Claimants rely on [redacted]

[616] Canada's Rejoinder, Section II.F.4; **R-183**, Government of Ontario News Release, "Ontario Announces Constitutional Challenge to Federal Government's Punishing Carbon Tax Scheme", 2 August 2018. Previously, the Premier-Designate publicly announced the incoming government's intention, following its swearing-on on June 29, 2018, to challenge the constitutionality of the federal backstop. **C-007**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Announces an End to Ontario's Cap-and-Trade Carbon Tax", 15 June 2018.

[617] Canada's Rejoinder, Section II.F.4; **AW-30**, Regulation 241/19; **RS-104**, Environment and Climate Change Canada, "Pan-Canadian Approach to Pricing Carbon Pollution: Interim Report 2020," 2021, pp. 37-40.

[618] Canada's Rejoinder, Section II.F.4; **AW-12**, Ontario, "Province Welcomes Federal Government's Decision to Accept Made-in-Ontario Emissions Performance Standards", 21 September 2020; **RS-104**, Environment and Climate Change Canada, "Pan-Canadian Approach to Pricing Carbon Pollution: Interim Report 2020," 2021, p. 39.

[619] Canada's Rejoinder, Section II.F.4; **RWS-1**, Wood – First Witness Statement, ¶ 35.

[620] Canada's Counter-Memorial, ¶ 276.

[621] Claimants' Reply, ¶ 583.

[redacted][622]

268. This is hardly evidence of Ontario's "politically expedient" "targeting" of KS&T. There were legitimate policy reasons not to compensate certain categories of participants in the cap and trade program, such as fuel suppliers, electricity distributors,[623] and market participants.[624] As Mr. Litz explains in his expert reports, during the WCI program design phase concerns were raised about allowing market participants to participate,[625] and in 2016 – two years before Ontario adopted the impugned measures – KS&T's Vice President Graeme Martin explained that [redacted] and that [redacted][626] Ontario's principled approach to compensation, including the ineligibility of market participants for compensation, was neither arbitrary nor discriminatory.

269. Third, Ontario's measures did not constitute one of rare cases where regulatory measures cannot be reasonably viewed as having been adopted and applied in good faith.[627] The Claimants argue that "[t]here was absolutely no reason for the Premier-elect's political grandstanding and his

[622] [redacted]

[623] While fuel suppliers and electricity importers had mandatory compliance obligations, they had been able to pass the cost of compliance to their customers. *See* Canada's Counter-Memorial, ¶¶ 96-97, 205, 276; **RWS-1**, Wood – First Witness Statement, ¶¶ 22, 25.

[624] Canada's Counter-Memorial, ¶ 97; **C-175**, Hansard Transcript, Legislative Assembly of Ontario, 31 July 2018, per Hon. Rod Phillips: "Our approach recognizes that regulated participants may have purchased allowances to comply with regulations, whereas market participants without a compliance obligation chose to take risks as market traders and speculators."

[625] Canada's Counter-Memorial, ¶ 37 and fn. 52; **RER-2**, Litz – First Expert Report, ¶¶ 79-81; Canada's Rejoinder, ¶ 26; **RER-4**, Litz – Second Expert Report, ¶¶ 27-31.

[626] [redacted]

[627] Canada's Counter-Memorial, ¶¶ 273-274, 277-278.

ultra vires direction to the Ministry to ignore the legislative requirements in place on 15 June 2018" and that "Ontario's actions on 15 June 2018 and 3 July 2018 … were wholly disproportionate".[628]

270. The Claimants' labels are not a replacement for a sober assessment of what happened. Ontario's decision not to participate in the August 2018 joint auction was in accordance with the caretaker convention, and Premier-Designate's announcement was not *ultra vires*.[629] Adopting a new program to replace the cap and trade program was an important part of the Progressive Conservative Party's electoral platform,[630] and – on June 15, 2018, two weeks before being sworn in – the Premier-Designate announced that the new government intended to act upon that electoral platform.[631] There was nothing "out of bounds" for a Premier-Designate to announce his government's intention, upon swearing-in, to implement certain environmental policies that had been a central part of his electoral platform.[632] The Claimants could not have legitimately expected that Premier-Designate would refrain from making announcements about implementing core elements of his electoral platform, which is commonplace for any soon-to-be incoming government,[633] or that Ontario's outgoing government would commit the incoming government by issuing an auction notice for the August 2018 auction.[634]

271. The Claimants' reliance on *OEG v. Ukraine*, where the tribunal decided that a legislative ban on gambling activities constituted an indirect expropriation, is inapposite.[635] In that case, because the

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[628] Claimants' Memorial, ¶ 587.

[629] Canada's Rejoinder, Section II.D and III.E.

[630] Canada's Rejoinder, II.D.3; Canada's Counter-Memorial, ¶¶ 67, 69, 201; **CWS-3**, Brown – Witness Statement, ¶ 35; **CWS-2**, Martin – First Witness Statement, ¶ 49.

[631] **C-007**, Office of the Premier-Designate, News Release, "Premier-Designate Doug Ford Announces an End to Ontario's Cap-and-Trade Carbon Tax", 15 June 2018: "Premier-designate Doug Ford today announced that his cabinet's *first act following the swearing-in* of his government will be to cancel Ontario's current cap-and-trade scheme, and challenge the federal government's authority to impose a carbon tax on the people of Ontario. '*I made a promise* to the people that *we would take immediate action* to scrap the cap-and-trade carbon tax and bring their gas prices down,' said Ford. 'Today, I want to confirm that as a first step to lowering taxes in Ontario, the carbon tax's days are numbered.'" (*emphasis* added)

[632] Canada's Rejoinder, Sections II.D and III.E; Canada's Counter-Memorial, ¶ 277.

[633] During the transition period, it is routine for the Premier-Designate to make statements outlining the incoming government's priorities and intentions for once it assumes office. *See* Canada's Counter-Memorial, ¶ 78 and fn. 132.

[634] Canada's Rejoinder, Section II.D; **RWS-3**, Wood – Second Witness Statement, ¶¶ 6-12.

[635] Claimants' Reply, ¶¶ 587-588.

impugned legislation was adopted following an expedited procedure, there was "almost no debate concerning the draft legislation"[636] and "the legislators had little in the way of empirical evidence before them that would have assisted them in crafting a legislative solution to the problem that was said to face the country."[637] In contrast, Bill 4 – consistent with Ontario's usual legislative processes – passed three readings and a committee stage before it received Royal Assent and came into force.[638] Debates of Bill 4 were informed by the conclusion of Ontario's Auditor General in her 2016 report that "the cap-and-trade system will result in only a small portion of the required greenhouse-gas reductions needed to meet Ontario's 2020 target" and "at significant cost to Ontario businesses and households".[639] Ontario's new government held the position that replacing Ontario's cap and trade program with a different program would lower fuel costs, decrease the burden on Ontario taxpayers, and boost economic growth and employment.[640]

272. The Claimants further allege that "[t]here was no consultation, no adjustment period, and no opportunity for the Claimants to mitigate their loss."[641] KS&T did have the opportunity to transfer to California the emission allowances deposited into its CITSS account on June 11, 2018, and doing so would have been in accordance with KS&T's [redacted][642] However, KS&T's nominal PAR was out of the office, and – despite initial plans to do so – KS&T never appointed a second

[636] **CL-198**, Olympic Entertainment Group AS v. Republic of Ukraine, PCA Case No. 2019-18, Award (15 April 2021) ("*OEG – Award*"), ¶ 27. *See also* ¶ 92: The "expedited process adopted by Parliament … by definition reduced the period for deliberation as to the merits and demerits of the proposed legislation".

[637] **CL-198**, *OEG – Award*, ¶ 92. The tribunal emphasized, however, that it "does not expect the members of any parliament to critically analyse every aspect of whatever studies might be available to parliament" and that "law-making is a process of balancing policy alternatives, purely political considerations, and other factors, a process that can seem very distant from, perhaps even antithetical to, the scientific method." **CL-198**, *OEG – Award*, ¶ 93.

[638] Canada's Counter-Memorial, ¶¶ 86, 203; Canada's Rejoinder, Section II.F.2.

[639] Canada's Counter-Memorial, ¶¶ 68, 273 and fns. 117-118, 502-503; **R-036**, Minister of the Environment and Climate Change, 2016 Annual Report of the Office of the Auditor General of Ontario, Chapter 3 Section 3.02, pp. 149, 150, 167 and 174-175; **R-037**, Office of the Auditor General of Ontario, News Release "Ontario's Cap and Trade Will Not Significantly Lower Emissions Within the Province by 2020: Auditor General".

[640] Canada's Counter-Memorial, ¶¶ 68, 102-104, 273 and fns. 118, 503; **R-062**, Ontario, Preserving and Protecting our Environment for Future Generations: A Made-in-Ontario Environment Plan, 29 November 2018, p. 3 ("2018 Environment Plan").

[641] Claimants' Reply, ¶ 588.

[642] [redacted]

AAR who could approve the transfer in his absence.[643] In any event, KS&T was well aware that the new majority government was elected by the voters on a clear promise to cancel the cap and trade program,[644] and Ontario posted Bill 4 on the Environmental Registry, giving the public 30 days to comment.[645] The Claimants were able to engage in "substantial lobbying efforts",[646] to send letters to the Attorney General of Ontario and to the Premier's Office,[647] and to provide comments on Bill 4.[648] Ontario considered comments received during the consultation period, and published a "decision summary" explaining how the government addressed these comments.[649]

273. Regardless of whether Ontario's preferred approach to environmental policy is the "best" or "most efficient", none of the Claimants' arguments undermine the fact that, the actions attributable to Ontario were a legitimate exercise of police powers under international law. Because Ontario's measures were non-discriminatory and designed and applied in good faith to protect a legitimate public welfare objective without imposing unnecessary cost on Ontarians, there was no indirect expropriation of the Claimants' alleged investments.

[643] Canada's Rejoinder, Section II.C; [redacted]

[644] Canada's Rejoinder, Section II.C; Canada's Counter-Memorial, ¶¶ 67, 71, 77-78, 201; **R-157**, Email from Paul Brown to Graeme Martin and Sam Porter, "RE: PC Party leadership candidates on carbon tax and cap and trade" 24 April 2018; **C-175**, Hansard Transcript, Legislative Assembly of Ontario, 31 July 2018, per Minister Phillips, pp. 485: "Our government was elected on a clear mandate: to put the people first and make life more affordable for Ontario families. As part of this, we made a promise to the people of Ontario that we would scrap the cap-and-trade carbon tax imposed by the previous Liberal government. The Cap and Trade Cancellation Act, if passed, will fulfill our promise to taxpayers…" and p. 487 per Andrea Khanjin: "Why are we here to debate this bill…? Because we have a clear mandate from the people of Ontario. We campaigned on a promise of eliminating cap-and-trade and the carbon tax."

[645] Canada's Rejoinder, Section II.F.2; Canada's Counter-Memorial, ¶ 87; **RWS-1**, Wood – First Witness Statement, ¶ 24; **RWS-3**, Wood – Second Witness Statement, ¶ 29; **C-012**, Environmental Registry – Bill 4.

[646] Claimants' Memorial, ¶ 229.

[647] Canada's Counter-Memorial, ¶ 89; **C-114**, Letter from KS&T to the Attorney General of Ontario, 24 October 2018; **C-115**, Letter from KS&T to the Premier's Office, 24 October 2018; **C-116**, Letter from Premier Doug Ford to Koch Industries, 5 November 2018; **C-117**, Letter from Minister Rod Philips to Koch Industries, 18 February 2019.

[648] Canada's Counter-Memorial, ¶ 88; **RS-086**, Koch Comment on Bill 4.

[649] Canada's Rejoinder, Section II.F.2; Canada's Counter-Memorial, ¶ 90; **C-012**, Environmental Registry – Bill 4; **RWS-1**, Wood – First Witness Statement, ¶ 21; **RWS-3**, Wood – Second Witness Statement, ¶ 29.

3. The Claimants Have Not Established Ontario Directly Expropriated Any of Their Alleged Property Rights

274. The Claimants allege that the *Cancellation Act* "outright cancelled the emissions allowances held in KS&T's Ontario CITSS account", and the cancellation was "for the benefit of the State, which received a substantial amount of profit."[650] The only alleged "investment" that the Claimants claim to have been directly expropriated are emission allowances purchased by KS&T at the May 15, 2018 joint auction and held in KS&T's Ontario CITSS account on October 31, 2018.[651]

275. In its Counter-Memorial, Canada explained that, in the absence of a compulsory transfer of any of KS&T's property to Ontario or an Ontario-mandated third party, there was no direct expropriation of KS&T's alleged investments.[652] The Claimants, in their Reply, argue that Ontario directly expropriated KS&T's alleged investments because "there has been a forcible appropriation of the Claimants' investment by means of legislative action."[653] The Claimants' arguments must be rejected.

276. First, both arbitral tribunals and commentators understand direct expropriation to require either a compulsory transfer to a State or a State-mandated third party, or outright physical seizure of the property.[654] Instead, the Claimants argue that the applicable test is "whether there has been a 'forcible appropriation by the State of the tangible or intangible property of individuals by means of administrative or legislative action.'"[655] The Claimants' insistence on "forcible appropriation" rather than "forcible transfer" as the applicable criterion does not, however, save their direct expropriation

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[650] Claimants' Reply, ¶ 597.

[651] The Claimants do not allege that Ontario directly expropriated KS&T's alleged "business in Ontario" or any of the Claimants' other alleged investments. Canada's arguments in this section focus on KS&T's alleged investment in the emission allowances. However, the same arguments apply to any of the Claimants' alleged investments. *See* Claimants' Reply, ¶¶ 597, 601, 604; Claimants' Memorial, ¶ 420.

[652] Canada's Counter-Memorial, ¶¶ 279-285.

[653] Claimants' Reply, ¶ 601; Claimants' Memorial, ¶¶ 420-421.

[654] Canada's Counter-Memorial, ¶¶ 280, 283, and fns. 517-521, 526. *See also* **RL-058**, *Corn Products – Decision on Responsibility*, ¶ 91; **RL-023**, Kinnear: Investment Disputes under NAFTA, p. 1110-13; **RL-084**, UNCTAD, Expropriation: A Sequel, UNCTAD Series on Issues in International Investment Agreements II (United Nations: New York and Geneva, 2012), pp. 6, 7; **RL-086**, Newcombe & Paradell, p. 323, ¶ 7.2, and p. 340, ¶ 7.11; **RL-143**, Blackaby, ¶ 8.81.

[655] Claimants' Reply, ¶ 600.

claim. The ordinary meaning of the word "appropriation" is "the act of taking something for your own use, usually without permission",[656] and the *Cancellation Act*, as Canada explained, neither "transferred" any of KS&T's alleged property to Ontario (or an Ontario-mandated third party) nor "took" any of KS&T's alleged property for Ontario's "own use".[657] Under the *Cancellation Act*, all of the emission allowances held by KS&T in its Ontario CITSS account were cancelled.[658] It is undisputed that none of KS&T's allowances were either transferred to Ontario for the government's own use (i.e. "forcibly appropriated" by Ontario) or transferred to another cap and trade participant mandated by Ontario.[659]

277. Second, to constitute direct expropriation, the compulsory transfer or physical seizure must be for the benefit of the host State or a State-mandated third party.[660] The Claimants argue that Canada has "not denied that Ontario profited in a substantial way from the cancellation of the Claimants' investment, and *the investments like* it in the Ontario market."[661] The Claimants' direct expropriation claim relates to the emission allowances purchased at the May 2018 joint auction and held in KS&T's Ontario CITSS account. Ontario received its share of proceeds from KS&T's purchase of emission allowances [redacted] and the three jurisdictions deposited emission allowances into KS&T's Ontario CITSS account, on June 11, 2018.[662] Ontario would have received this amount

[656] **RL-181**, Cambridge Online Dictionary, "appropriation".

[657] Canada's Counter-Memorial, ¶¶ 281-282.

[658] Canada's Counter-Memorial, ¶ 282. The Claimants continue to err in arguing that the *Cancellation Act* "specifically provided that these allowances [i.e. allowances held in KS&T's Ontario's CITSS account] were deemed by Ontario to have been 'never distributed' in the first place." Claimants' Reply, ¶ 601. Section 7(2) of the *Cancellation Act* merely cancelled those emission allowances that had been "created", but "never distributed"; therefore, s. 7(2) does not apply to the emission allowances held in KS&T's CITSS account because such allowances indisputably had been "distributed". *See* Canada's Counter-Memorial, fn. 522; **R-059**, *Cancellation Act, 2018*, s. 7 ("The following cap and trade instruments are cancelled: 1. All cap and trade instruments held in the cap and trade accounts of participants on July 3, 2018, other than any number of cap and trade instruments in the accounts that are retired under section 6. 2. All cap and trade instruments that were created under the *Climate Change Mitigation and Low-carbon Economy Act, 2016* and were never distributed.")

[659] Canada's Counter-Memorial, ¶ 282.

[660] Canada's Counter-Memorial, ¶ 283 and fn. 256.

[661] Claimants' Reply, ¶ 603 (emphasis added).

[662] Canada's Counter-Memorial, ¶ 284; **RWS-2**, Ramlal – First Witness Statement, ¶¶ 48, 57 and Attachment 1, transfer [redacted]

whether or not Ontario enacted the *Cancellation Act* on October 31, 2018.[663] Further, it is unclear how the Claimants' repeated references to the amount of proceeds Ontario received from *all* successful bidders at the May 2018 auction is relevant to the Claimants' claim about the alleged benefit Ontario received as a result of cancelling, several months later, the emission allowances held in KS&T's CITSS account.[664]

278. In the absence of compulsory transfer of the Claimants' property to Ontario (or an Ontario-mandated third party) and any benefit to Ontario, Ontario did not directly expropriate the Claimants' alleged investments.

V. THE CLAIMANTS ARE NOT ENTITLED TO COMPENSATION

279. In their Reply, the Claimants maintain their simplistic, outcome-driven damages case, requesting reimbursement for the purchase price KS&T paid for emission allowances at the May 2018 auction, irrespective of the alleged underlying breach. The Claimants acknowledge that in order to be awarded damages, they must prove both factual and legal causation for each of the breaches they allege. The Claimants have failed on both counts. As a result, even if the Tribunal finds a breach of NAFTA Article 1110 or Article 1105, the Claimants are not entitled to any of the damages they seek.[665]

280. Here, Canada corrects the Claimants' Reply submissions on the applicable law (**Section A**), and explains that the Claimants have failed to meet their burden with respect to their claims for Article 1110 damages (**Section B**), Article 1105 damages (**Section C**), and "associated costs" (**Section D**). Even if the Tribunal were to award damages, the evidence establishes that the quantum should be reduced to account for the Claimants' contributory fault (**Section E**).

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[663] Canada's Counter-Memorial, ¶ 284.

[664] See Claimants' Reply, ¶¶ 14, 232, 603. In any event, Ontario's share in the proceeds from the sale of emission allowances to KS&T [redacted] was a small percentage [redacted] of the overall amount of proceeds Ontario received from the May 2018 auction (USD 368 million).

[665] Other international tribunals have refused to award any damages when faced with similarly defective damages claims See, for example **RL-123**, *Nordzucker AG v. The Republic of Poland* (UNCITRAL) Third Partial and Final Award, 23 November 2009, ¶ 64; **RL-125**, *Pawlowski – Award*, ¶ 737; **RL-121**, *Biwater Gauff – Award*, ¶ 798, **CL-080**, *CME Czech Republic B.V. (The Netherlands) v. The Czech Republic* (UNCITRAL) Partial Award, 13 September 2001 ("*CME – Partial Award*"), ¶ 235.

A. The Claimants' Demand for Compensation Ignores Established Damages Principles and International Law

281. The disputing parties agree that NAFTA Article 1116(1) accords standing only to an investor alleging that it "has incurred loss or damage, by reason of, or arising out of" an alleged breach of the NAFTA.[666] The treaty requires a sufficient causal link or an "adequate[] connect[ion]" between the alleged breach of NAFTA and the loss sustained by the investor.[667] The disputing parties agree that in addition to customary international law and the text of the NAFTA, Article 31 of the ILC Draft Articles is instructive.

282. The parties further agree that causation has two elements: factual and legal.[668] However, in Sections B and C below, Canada explains how the Claimants have conflated these elements and failed to establish the necessary causal link.

283. Finally, the disputing parties generally agree on the burden and standard of proof. The parties agree that the party asserting a fact has the burden of proving it on a balance of probabilities,[669] and that the burden of a party to prove its damages covers not only the facts, but also legal points sustaining its position.[670] However, the Claimants are mistaken when they argue that the burden shifts to Canada after having challenged the Claimants' case on causation. In damages, the claimant always bears the burden of proof in relation to the fact and amount of loss, which includes demonstrating the causal link between the respondent's wrongful conduct and the claimant's loss.[671]

284. Applied to the facts of this case, the Claimants must establish the fact and amount of loss, as well as the causal link between Canada's alleged wrongful conduct and the Claimants' loss. The

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[666] Canada's Counter-Memorial, ¶ 295; Claimants' Reply ¶ 646.

[667] **RL-090**, *Feldman – Award*, ¶ 194. *See also* **RL-121**, *Biwater Gauff – Award*, ¶ 779 ("Compensation for any violation of the BIT, whether in the context of unlawful expropriation or the breach of any other treaty standard, will only be due if there is a sufficient causal link between the actual breach of the BIT and the loss sustained by [the Enterprise].")

[668] Claimants' Reply, ¶ 618.

[669] Claimants' Reply, ¶ 619.

[670] **RL-192**, T. Walde and B. Sabahi, "Compensation, Damages, and Valuation", The Oxford Handbook of International Law (Oxford University Press, 2022), p. 1110 (p. 30 of PDF)

[671] **RL-120**, S. Ripinsky & K. Williams, "Damages in International Investment Law", (London, British Institute of International and Comparative Law: 2008) ("Ripinsky & Williams"), p. 162.

Claimants premised their expropriation claim on the allegation that Premier-Designate Ford's June 15 announcement precipitated a series of events that "caused" them loss.[672]

285. The requirement for a State to make reparation is not automatic upon a finding of breach.[673] Before assessing reparation, the Tribunal must consider causation. The causation inquiry is analytically distinct from a finding of breach and the assessment of quantum. First, the tribunal's decision regarding the breach will set the scope (but not the outcome) of the causation analysis. Then, the causation analysis will set the scope (but not the outcome) of the quantum analysis.[674]

286. In assessing causation, the tribunal must examine whether the claimed injury was "caused", in law and in fact, by the State's internationally wrongful act.[675] The Claimants attempt to conflate factual and legal causation in applying these requirements to the facts of this case. The Claimants' approach contravenes customary international law on State responsibility.

287. Requesting that this Tribunal undertake a thorough causation analysis is not "shameless" as the Claimants assert,[676] but rather a principled approach applying international law and established damages principles to the facts of the case. While Canada maintains that there is no jurisdiction and no breach in this case, as outlined in Parts III and IV above, in the event that the Tribunal disagrees and finds a breach of either NAFTA Article 1110 or 1105, it must then engage in a separate causation inquiry to assess that both requirements – factual and legal – are met.

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[672] Claimants' Reply, ¶¶ 159, 169.

[673] **RL-193**, Pearsall and Heath, "Causation and Injury in Investor-State Arbitration", (Contemporary and Emerging Issues on the Law of Damages and Valuation in International Investment Arbitration) [Excerpt], pp.88-89 ("In light of the separation between breach and harm, the assignment of damages will depend on a further finding of 'injury' in which causation will play a determinative role. The requirement to make reparation does not arise automatically upon a simple finding of breach. Rather, Article 31 makes clear that a causal link is a definitional element of an 'injury' as understood in international law. As such, it must be established that the damages sought in connection with an internationally wrongful act form part of the 'injury caused by' that act. If an 'injury' is established, then, pursuant to Article 31, the responsible State is required to make reparation.")

[674] **RL-193**, Pearsall and Heath, p. 85.

[675] **RL-194**, Andrea K. Bjorklund, "Causation, Morality, and Quantum", 32 Suffolk Transnat'l L. REV 435 (2009) ("Bjorklund"), p. 436.

[676] Claimants' Reply, ¶ 614.

288. In the factual causation analysis, the question is whether the wrongful conduct caused the harm or injury *in fact*. Commentators have framed this as a "scientific notion of causation", in that the wrongful conduct was necessary for the resulting injury to occur.[677] Canada maintains that the injury must have been "*in consequence of* the wrongful act."[678] Some arbitral tribunals have examined factual causation by asking whether the claimed injury would have arisen "but-for" the internationally wrongful act.[679] However, the but-for test as presented by the Claimants is incorrect.

289. The Claimants argue that "for the Respondent, the issue is whether 'an identified breach was a 'but-for' cause in the chain of causation'."[680] This is misleading. Canada's argument in its Counter-Memorial was that *even where* a claimant establishes that an identified breach was a "but for" cause in the chain of causation, recovery of damages is not permitted unless the claimant can prove that "the wrongful conduct was a sufficient, proximate, adequate, foreseeable or direct cause of the injury".[681] In examining factual causation, the Tribunal must look at whether the injury arose *as a result* of the wrongful act, not whether it was "a" cause in the chain.

290. The Claimants must also prove legal causation. In its Counter-Memorial, Canada explained that in order to recover damages, a claimant must prove that "the wrongful conduct was a sufficient,

[677] **RL-195**, Michael S. Moore, "Causation and Responsibility: An Essay in Law, Morals, and Metaphysics", January 2009, p. 83 (emphasis in original).

[678] Claimants' Reply, ¶ 619 (emphasis added by the Claimants).

[679] However, commentators have increasingly noted the risks of using a but-for test, particularly in cases of overdetermination. *See* **RL-196**, Ilias Plakokefalos, "Causation in the Law of State Responsibility and the Problem of Overdetermination: In Search of Clarity", European Journal of International Law (Vol. 26, No. 2, 2015) ("Plakokefalos"), pp. 476-477.

[680] Claimants' Reply, ¶ 619 (emphasis added by the Claimants).

[681] Canada's Counter-Memorial ¶ 294.

proximate, adequate, foreseeable or direct cause of the injury."[682] Legal tests of causation limit the amount of legally relevant damages.[683] Commentary 10 to Article 31 of the ILC Draft Articles states:

> Thus, causality in fact is a necessary but not a sufficient condition for reparation. There is a further element, associated with the exclusion of injury that is too "remote" or "consequential" to be the subject of reparation. In some cases, the criterion of "directness" may be used, in others "foreseeability" or "proximity". But other factors may also be relevant: for example, whether State organs deliberately caused the harm in question, or whether the harm caused was within the ambit of the rule which was breached, having regard to the purpose of that rule.[684]

291. This element of the causation analysis has been described as the "scope of responsibility" element.[685] As one commentator noted:

> What courts are trying to achieve when they use language such as 'proximity', 'remoteness', 'foreseeability' or 'causation in law' is justification, as far as possible, for a decision that, while recognizing that the defendant's conduct was a cause of the outcome, there are reasons not to find for the plaintiff.[686]

292. In the Claimants' submission, if the loss can be traced "link by link" to the Respondent's unlawful act, that is sufficient to attract liability for a State under international law.[687] The Claimants

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[682] For example, in *CME v. Czech Republic*, the tribunal stated that "Even if the breach therefore constitutes one of several "s*ine qua non*" acts, this alone is not sufficient. In order to come to a finding of a compensable damage it is also necessary that there existed no intervening cause for the damage. In our case the Claimant therefore has to show that the last, direct act, the immediate cause… did not become a superseding cause and thereby the proximate cause. In other words, the Claimant has to show that the acts of CET 21 were not so unexpected and so substantial as to have to be held to have superseded the initial cause and therefore become the main cause of the ultimate harm." The tribunal concluded that an award of damages was not appropriate in that case, because "the 1993 breach of the Treaty was too remote to qualify as a relevant cause for the harm caused." **CL-080**, *CME – Partial Award*, ¶¶ 234-235. In this case, the Claimants must similarly prove that the immediate cause of their loss (California de-linking its CITSS accounts from Ontario accounts) did not become a superseding cause and thereby the proximate cause of their loss. They have failed to do so, and this Tribunal must similarly decline to award damages.

[683] **RL-120**, Ripinsky & Williams, p. 135.

[684] The ILC also notes that: "In other words, the requirement of a causal link is not necessarily the same in relation to every breach of an international obligation. In international as in national law, the question of remoteness of damage "is not a part of the law which can be satisfactorily solved by search for a single verbal formula". The notion of a sufficient causal link which is not too remote is embodied in the general requirement in article 31 that the injury should be in consequence of the wrongful act, but without the addition of any particular qualifying phrase." **CL-051**, ILC Draft Articles, Commentary 10.

[685] **RL-196**, Plakokefalos, pp. 478-479.

[686] **RL-196**, Plakokefalos, p. 478.

[687] Claimants' Reply, ¶ 636.

frame the test as being whether a "reasonable person" could have foreseen "that through successive links the irregular acts finally would lead to the damage."[688] To make sense of the Claimants' explanation of "foreseeability" and "proximate cause" requires the benefit of hindsight.

293. In the Claimants' application of the test, one must start from the end result (the injury) and trace it back to a wrongful act. This is not correct. Rather, one must look at what the wrongdoer knew, or should have known, at the relevant time and whether that particular outcome (the "injury" at issue) was so proximate to that act that it was foreseeable. The rules of international law protect against actions that are intentional, or so obviously predictable that they should be avoided.[689]

B. The Claimants' Claim for Damages with Respect to the Alleged Expropriation of its Emission Allowances Fails on Both Factual and Legal Causation

294. The Claimants argue that this Tribunal should award them a full refund of the USD 30 million purchase price paid for the emission allowances they acquired at the May 2018 joint auction, which the Claimants argue were expropriated on June 15, 2018. This is the "injury" for which the Claimants seek reparation.[690] However, as will be explained in the following subsections, the Claimants conflate factual and legal causation to try and pin their loss on Ontario for two acts which were not the factual or legal cause of their loss. Their attempts must be rejected.

295. It is necessary to recall the KS&T's business model, which is that of a cross-border trader that moved regulatory instruments across jurisdictions looking for [redacted][91] The purpose of KS&T's purchase of emission allowances in the May 2018 auction was to transfer them to California for resale to KS&T's California-based affiliates.[692]

[688] Claimants' Reply, ¶¶ 622-624.

[689] **CL-051**, ILC Draft Articles, Article 31, Commentary 10.

[690] According to the Claimants, the critical date was June 15, 2018: that was the date on which they were "directly affected" and there was an "immediate devastating effect on the value of the Claimants' allowances. See, for example, for example, Claimants' Memorial ¶¶ 206, 252, 408. *See also* Claimants' Reply, ¶¶ 169, 628, 635.

[691] [redacted]

[692] **RS-086**, Koch Comment on Bill 4.

296. The Claimants did not commence this NAFTA proceeding because Ontario cancelled its program – in fact, they welcomed the cancellation,[693] and acknowledge in their pleadings that Ontario had every right to change its policy.[694] Rather, the "injury" for which the Claimants seek reparation is the inability to transfer their allowances to their California CITTS account once California de-linked from Ontario.[695] This starting point of "injury" has significant implications for the causation analysis.

1. The Claimants' Concession on Factual Causation is Fatal to their Damages Claim

297. The Claimants' focus their causation arguments on Professor Stavins' opinion that California and Quebec de-linking their CITSS registries from Ontario was "objectively foreseeable." The test is not whether the "outcome was objectively foreseeable"[696] or whether an act was "a" cause in the chain of causation.[697] Rather, the test is whether the wrongful act caused the claimed injury "in fact."

298. As Canada explained above, factual causation is a 'scientific' inquiry, in which the tribunal examines cause and effect. A tribunal must assess questions of 'foreseeability' later, at the legal causation stage. The Claimants' convoluted argument on factual causation reveals a critical flaw: it implicitly acknowledges that causation 'in fact' for the losses they claim in this arbitration was due to an action of California, not Ontario.[698] Instead of addressing this head-on, the Claimants conflate the two concepts.

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[693] **RS-086**, Koch Comment on Bill 4 ("Koch does not support the concept of cap and trade").

[694] Claimants' Reply, ¶¶ 70, 197, 436, 559, 664.

[695] Other participants in the Ontario program who were participating as compliance entities did not suffer an "injury" on June 15. Rather, Ontario took action with respect to the emission allowances in their CITSS accounts on July 3, 2018. This would be the starting point of injury for participants in the program who were not cross-border traders like KS&T. Indeed, even the Claimant Koch Industries' subsidiary companies in Ontario, Invista and Komsa, did not suffer loss on June 15 (or at all) and are not a part of this arbitration.

[696] Claimants' Reply, ¶ 634.

[697] Claimants' Reply, ¶ 619.

[698] As Canada explained above and in its Counter-Memorial, three separate acts occurred on June 15: Premier-Designate Ford issued a press release announcing an orderly wind-down of the program; Ontario decided not to issue the auction notice for the August 2018 linked auction; and California and Quebec de-linked their accounts from Ontario. Only one of these caused the Claimants' claimed injury "in fact."

299. Throughout their pleadings, the Claimants admit that California caused their injury by "closing their markets to Ontario allowances as of the evening of 15 June 2015."[699] The Claimants use the passive voice throughout[700] and try to frame this as a "*de facto*" freeze by Ontario.[701] However, this does not detract from the fact of their admission, on their own legal case, that California caused the loss in question.[702] The cause of their injury was not a *de facto* freeze by Ontario; it was a *de facto* freeze by California.[703]

300. The Claimants' contemporaneous documents support this conclusion ([redacted].[704] Consistent with California causing the loss (and thus being able to remedy it), in the immediate aftermath of California's de-linking [redacted]

[699] Claimants' Reply, ¶ 9.

[700] See for example, Claimants' Reply, ¶ 159 (the announcement "directly precipitated the California and Quebec market notice of that same evening"); ¶ 169 ("precipitated the entirely predictable closure of California and Quebec markets to Ontario-held allowances"); ¶ 177 ("preventative actions taken by California and Quebec on the night of 15 June 2018").

[701] Claimants' Reply, ¶ 85.

[702] Moreover, the Claimants' cannot imply that the Premier-Designate's announcement and the California firewall are cotemporaneous acts. The Premier-Designate's announcement took place on the morning of June 15. There was a full day of trading that day, in which another participant was able to execute three successful transfers of emission allowances from its Ontario to California accounts. After the close of business that day, California delinked its CITSS registry. KS&T had every opportunity to transfer emission allowances up to the close of business on June 15, [redacted]

[703] The fact that the Claimants' grievance is with the *de facto* freeze by California on June 15 (and not the *de jure* freeze by Ontario on July 3) is obvious when one examines their situation as a cross-border trader in contrast with a compliance entity in Ontario that was acquiring allowances to satisfy compliance obligations. For the latter group, the allowances could have been applied to compliance obligations until June 30, and traded until July 3, 2018. For those entities, the critical date for "injury" would be July 3 when Ontario enacted Regulation 386.

[704] [redacted]

See [redacted] The Claimants' damages case in this arbitration does not allege, much less prove, that Ontario's decision not to participate in the August auction caused them loss. The Tribunal should draw an adverse inference from their marked difference between the Claimants' contemporaneous statements and their current position in this arbitration.

[redacted][705] While these efforts were in vain, it is indicative of what the Claimants have known since June 15, 2018: an act of California, not Ontario, caused any loss in fact.

301. The Claimants' expert Professor Stavins is also clear that it was an act of California that caused the alleged loss.[706] However, the Claimants use his testimony to try and advance their legal argument. In Professor Stavins' view, California had no choice but to cause the Claimants loss.[707] Professor Stavins applies the Claimants' incorrect "objectively foreseeable outcome" test of factual causation to argue that California's de-linking was a "predictable response."[708] Implicit in his conclusion is a critical concession that California that caused the Claimants' injury in fact. Further, as Canada will explain in the following section, even when correctly applied to the framework of legal causation, Professor Stavins' conclusion is unsound.

2. In Any Event, the Claimants Have Failed to Establish Legal Causation

302. In the Claimants' submission on legal causation, "[t]he causal chain is short: Premier-elect Ford's announcement, de-linkage, loss."[709] This is simplistic and hinges entirely on Professor Stavins' incorrect assertion that de-linking was the only option available to California.

303. California had other options.[710] First, California could have adopted the same approach as the RGGI states recently did when New Jersey announced its plan to withdraw in 2018, and Virginia announced its plan to withdraw in 2021. In both cases, the remaining RGGI states kept the connection with the leaving state intact, and decided to honour the allowances. Similarly, California could have kept the connection with Ontario intact and continued to honour allowances that it sold at joint

[705] [redacted]

[706] **CER-2**, Stavins – Second Expert Report, ¶ 18.

[707] **CER-2**, Stavins – Second Expert Report, ¶¶ 18, 34, 35, 36, 94.

[708] **CER-2**, Stavins – Second Expert Report, ¶ 35.

[709] Claimants' Reply, ¶ 636.

[710] *See* **RER-4**, Litz – Second Expert Report, Section VI.

auctions with Ontario. Like the remaining RGGI states, California could then have made adjustments to their program in order to absorb the extra Ontario allowances.[711]

304. As Franz Litz explains, another option that California could have taken was to honour select allowances based on their date and/or origin.[712] For example, they could have selectively honoured only those allowances that were sold in the first two auctions of 2018, in which all three jurisdictions participated. Alternatively, California could have selectively honoured its connection with certain account holders and certain account types. For example, California could have permitted participants in Ontario to apply to have the allowances in their Ontario holding accounts recognized in California, provided the applicant could prove that the emission allowances had been purchased to meet a compliance obligation in California.

305. Had California chosen a different course of action, as other states have done in similar situations as described by Mr. Litz, the Claimants' injury could have been mitigated or prevented entirely. This breaks the legal chain of causation, which means the Claimants are owed no compensation from Canada.

C. The Claimants Repeatedly Decline to Plead their Article 1105 Damages with Specificity

306. The Claimants' claim for damages under Articles 1110 and 1105 are duplicative, requesting the same USD 30 million purchase price for a breach of either provision.[713] As Canada explained in its Counter-Memorial, requesting reimbursement for the purchase price of the emission allowances does not correspond to what was "lost" even if the Tribunal finds a breach of Article 1105.[714]

307. If the Tribunal finds a breach of Article 1105 as a result of a combination of events, it must still conduct a factual and legal causation inquiry that examines each constituent element and the loss

[711] The RGGI states did the same when New Jersey left the program in 2018. *See* **RER-4**, Litz – Second Expert Report, ¶¶ 41-42.

[712] **RER-4**, Litz – Second Expert Report, ¶¶ 47-49.

[713] Claimants' Memorial, ¶ 495, explaining that the Claimants paid a market price of USD 14.65 per allowance at the May 2018 auction. They seek damages as of June 14, [redacted] The actual purchase price paid in May 2018 was USD 30,158,240.95 but the Claimants seek USD 30,528,785.89.

[714] Canada's Counter-Memorial, ¶ 305.

flowing from it.[715] However, the Claimants have again stated that they "reserve the right" to re-plead their case later to identify the loss flowing from each specific action they allege is a breach of Article 1105.[716] The Claimants cannot blame the deficiencies in their damages claim on lack of opportunity to plead their case – they have had two full opportunities to do so already. The Claimants' Article 1105 damages claim is deficient for largely the same reasons their Article 1110 damages claim fails: they cannot prove factual and legal causation.

308. For example, the Claimants argue that it was a violation of Article 1105 for Ontario to deny compensation to market participants. In the "but-for" world the Claimants advocate, they would have to show that compensation for market participants would have been the same as for capped participants, even though they were in substantially different circumstances. Capped participants had greenhouse gas emissions. When Ontario decided to compensate mandatory participants, it compensated those mandatory participants that had acquired allowances over and beyond their actual reported emissions. It would be a perverse policy result if a capped participant that was required to participate in the program received compensation for only that amount beyond their emissions, and yet a market participant could recoup 100% of their CITSS account holdings. Had Ontario decided to compensate both capped and market participants, the amount of compensation could very well have been much lower and based on a different formula. The Claimants have failed to establish what they would have been entitled to under a "non-arbitrary" or "non-discriminatory" compensation rationale.

309. The Claimants make a similarly faulty assumption with respect to their claim that they were wrongfully denied access to domestic courts in order to challenge the *Cancellation Act*. Legal and factual causation require the Claimants to establish the value of what was "lost" by this breach, which is the opportunity to have their case heard by a Canadian court. While the Claimants fail to raise a case for the actual loss (loss of opportunity), the case that they do make (requesting full reimbursement for the emission allowances purchased by KS&T) is flawed. There is no guarantee, and this Tribunal cannot speculate, on what the result would have been for market participants (like

[715] Canada's Counter-Memorial, ¶¶ 292-296.

[716] Claimants' Reply, ¶ 648.

KS&T) in the Claimants' "but-for" world had the *Cancellation Act* not contained Crown immunity provisions.

310. Finally, the Claimants argue that the breach of Article 1105 was the "abrupt and arbitrary cancellation of the Cap and Trade Program, and its cancellation of all emissions allowances held in Ontario CITSS accounts."[717] Again, this does not excuse the Claimants from establishing factual and legal causation. Ontario cancelled the cap and trade program, and canceled remaining allowances in Ontario CITSS accounts, on October 31, 2018. The Claimants have failed to establish the value of their allowances if Ontario had cancelled the cap and trade program in a manner that was not "abrupt". Skipping the requisite causation tests for Article 1105 must result in the Claimants being denied compensation.

D. The Claimants Have Failed to Establish Entitlement to Any of their Claimed "Associated Costs"

311. The Claimants have failed to establish that they are entitled to compensation with respect to their claimed "associated costs". They simply assert that a "reasonable person" would have foreseen these losses. This is not a basis upon which the Tribunal can order compensation.

312. There are multiple reasons why the Tribunal should reject the claim for [redacted] as compensation for an alleged loss in obtaining replacement allowances [redacted]

313. First, the Claimants have declined to provide critical underlying evidence in support of this transaction. The insufficiency of evidence is enough for the Tribunal to reject this request: the purported replacement cost of [redacted] is simply pulled from the [redacted] [18] It is not supported [redacted] and there is no way to corroborate or confirm the numbers without the underlying documents, which the Claimants refused to produce.

[717] Claimants' Reply, ¶ 641.

[718] [redacted]

314. The claim for the cost of the replacement allowances is deficient in several other respects, including the timeline and the other options available to KS&T at various stages of the process. The Claimants state that KS&T intended to deliver emission allowances from the May 2018 auction to [redacted] [19] However, Mr. King does not cite to any evidence in support of his statement. It is not clear how, when, and under what terms KS&T agreed to that extension with its related party entity.

315. [redacted] KS&T had the option of acquiring allowances in the August 2018 joint California-Quebec auction using its California CITSS account.[720] According to the June 15, 2018 auction notice, the auction application period would close on July 16, 2018, and allowances would be transferred into CITSS accounts of successful bidders on September 10, 2018.[721] This would have given KS&T time to transfer the allowances to [redacted]

316. Instead, on July 27, 2018, KS&T acquired [redacted] emission allowances from an undisclosed counterparty at a cost of [redacted][722] As per the summary results report,[723] the August 14, 2018 auction settled at USD 15.05 – [redacted] If KS&T had fulfilled its [redacted] delivery obligation

[719] **CWS-4**, King – First Witness Statement, fn. 33.

[720] This dispenses with the Claimants' baseless mitigation arguments as well. Because KS&T could have acquired emission allowances in the August auction from its California CITSS account, there was no need for KS&T to purchase allowances at a markup in a third party sale. [redacted]

[721] **R-187**, Auction Notice, "California Cap-and-Trade Program and Québec Cap-and-Trade System Joint Auction of Greenhouse Gas Allowances On August 14, 2018", 15 June 2018, p. 7.

[722] [redacted]

[723] **R-188**, California Cap-and-Trade Program and Quebec Cap-and-Trade System, August 2018 Joint Auction #16, Summary Results Report, p. 4.

by buying allowances in the August 2018 auction, it would have been USD 60,964.20 cheaper than buying allowances on the secondary market from a third party.[724]

317. Even if the Tribunal accepts the Claimants' evidence without documentary support, their claims fail on legal causation. The Claimants state that "a reasonable person would have foreseen that market participants might have ongoing contractual commitments in linked jurisdictions, which they intended to fulfil using allowances purchased in Ontario. Losses incurred in meeting those obligations by other means cannot be considered 'remote'."[725]

318. The Claimants offer no credible explanation as to how any jurisdiction would reasonably foresee the unknown contractual commitments of unknown market participants. In any event, principles of compensation in international law do not require reparation for any loss that is tangentially related to the breach: it must be direct, foreseeable and not too remote.[726] The claim for the cost of replacement allowances is a prototypical example of remoteness that is not compensable under international law.[727]

319. The claim for the Claimants' lobbying costs is equally too "remote" to be the subject of reparation. In addition, the Claimants have failed to substantiate these alleged losses. The Claimants exhibited [redacted] [728] There is no proof that the Claimants (as opposed to KCPS) actually paid those invoices,[729] and the date range extends eight months after

[724] [redacted]

[725] Claimants' Reply, ¶ 637.

[726] **CL-051**, ILC Draft Articles, Article 31, Commentary 10.

[727] For example, in *Metalclad v. Mexico* the tribunal rejected Metalclad's request for damages to its other business operations, finding that the causal relationship was "too remote and uncertain to support this claim." *See* **CL-016**, *Metalclad Corporation v. The United Mexican States* (ICSID Case No. ARB(AF)/97/1) Award, 30 August 2000, ¶ 115.

[728] [redacted] at paragraph 505 of the Claimants' Memorial.

[729] [redacted]

the last measure challenged in this arbitration.[730] None of the Claimants' alleged lobbying costs are compensable, but even if they were, these lobbying costs are unsubstantiated and must be rejected.[731]

E. The Evidence Establishes that KS&T's Willful or Negligent Omissions Contributed to the Alleged Loss

320. In its Counter-Memorial, Canada explained the international legal principle of contributory fault, demonstrating that even if this Tribunal decides to award the Claimants damages, the amount awarded must be reduced in order to account for the Claimants' role in their loss.[732] The NAFTA Parties have recently stated NAFTA tribunals should take principles of contributory fault into account in assessing damages.[733] As Canada explained in its Counter-Memorial, tribunals have deducted damages by 50% or 25%.[734] A State cannot be responsible for damages it did not cause.[735]

[730] Ontario issued its Final Determination regarding KS&T's application for compensation on March 14, 2019. **C-10**; *see also* Claimants' Memorial, ¶ 336; Claimants' Reply Memorial, ¶ 402.

[731] [redacted]

[732] Canada's Counter-Memorial, ¶ 316.

[733] **RL-199**, *B-Mex – Fourth US Article 1128 Submission*, ¶ 65, **RL-198**, *B-Mex – Canada's Third 1128 Submission*, ¶¶ 46-48; **RL-200**, *B-Mex, LLC and Others v. United Mexican States* (ICSID Case No. ARB(AF)/16/3) Government of Mexico Response to Article 1128 Submissions, 24 June 2022, ¶ 23.

[734] Canada's Counter-Memorial, ¶ 319 and fn. 583. Alternatively, the reduction could be made with respect to the particular facts of the case. Here, all of the Claimants' damages should be disallowed. However, if the Tribunal wished to consider particular transactions, it could deduct USD 12,506,500, [redacted] *See also* Claimants' Memorial, ¶ 495, explaining that the Claimants paid a market price of USD 14.65 per allowance at the May 2018 auction. They seek damages as of June 14, when the price per allowance was [redacted] The actual purchase price paid in May 2018 was U SD 30, 158,240.95 but the Claimants seek USD 30,528,785.89. If the tribunal agrees with the Claimants on their primary case (valuation as of June 14, 2018) the necessary deduction is USD 12,605,500 ([redacted]. If the tribunal awards the Claimants damages based on the purchase price paid at the May 2018 auction, the necessary deduction should be USD 12,452,500.

[735] **CL-051**, ILC Draft Articles, Art. 39 (emphasis added). The commentary to Article 39 clarifies that a tribunal should take into account actions considered "wilful or negligent, i.e. which manifest a lack of due care on the part of the victim of the breach for his or her own property or rights." *See* **CL-051**, ILC Draft Articles, Art. 39, commentary (5), p. 110.) *See also* **RL-194**, Bjorklund, p. 446. *See also* **RL-197**, JM Marcoux and A. Bjorklund, "Foreign Investors' Responsibilities and Contributory Fault in Investment Arbitration", Cambridge University Press (2020), p. 881.

321. In their Reply, the Claimants accuse Canada of "victim-blaming," but they do not put forward any meaningful counter-argument on contributory fault.[736] The evidence shows that KS&T willingly engaged in risky business practices and, through a negligent failure to follow its own risk mitigation plan, contributed to its own loss. As a result, any damages award must be substantially reduced.

KS&T Did Not Heed Its Own Internal Warnings and Overbid in the May 2018 Auction Through its Ontario CITSS Account

322. KS&T's decision to participate in the May 2018 auction as an Ontario-registered market participant was a result of poor planning and was contrary to express warnings. The Claimants knew months ahead of time that, if elected, the Progressive Conservative Party would wind down the cap and trade program.[737] [redacted] [38]

323. Closer to the election, and before the auction bids were submitted, the polls forecast a Progressive Conservative majority.[739] In fact, then-Premier Wynne conceded before Election Day.[740] Regardless, KS&T made a significant bid from their Ontario (rather than its California) CITSS

[736] In their Reply at paragraphs 670-677, the Claimants rely on: (i) the fact that the new government would be sworn in on 29 June 2018 and as such "no substantial policy change legally could be enacted until then"; (ii) the terms of the withdrawal provision of the Harmonization Agreement; and (iii) their supposed "emissions trading business in Ontario." Each of the Claimants' attempted rebuttals are baseless. First, no substantial policy change took place until July 3, when Ontario enacted Regulation 386/18. Second, as Canada explained above, the Claimants ascribe a fundamentally incorrect interpretation to the withdrawal provision of the Harmonization Agreement. It was, at most, a "best efforts" provision. Any reliance the Claimants placed on it in operating their business was seriously misplaced. Third, at paragraph 614, the Claimants claim that they "invested significant time and energy in setting up their Ontario CITSS account" and they could not simply "abandon" it by participating from their California account. Claimants' Reply, ¶ 614. As set out in Part II.B, the Claimants vastly exaggerate KS&T's activities in Ontario.

[737] **R-031**, Ontario PC, "Patrick Brown and the Ontario PCs release the People's Guarantee", 25 November 2017; **R-032**, PC Party of Ontario, "People's Guarantee"; **R-034**, PC Party of Ontario, "Doug Ford Will Fight a Carbon Tax and Scrap Kathleen Wynne's 'Cap and Trade' Slush Fund", 23 April 2018; **R-046** Argus Media, "Carbon auction suggests optimism over Ontario", 24 May 2018. The Claimants' own witnesses in this arbitration testified that they were well-aware of this fact. *See* **CWS-3**, Brown – Witness Statement, ¶ 35; **CWS-2**, Martin – First Witness Statement, ¶ 49.

[738] [redacted]

[739] **R-191**, CTV News, "Ontario PCs leading in polls across the province, but NDP narrowing the gap", 18 May 2018.

[740] **R-192**, Global News, "Kathleen Wynne admits Liberals won't win election, urges voters to still vote for the party", 2 June 2018.

account.[741] At the May 2018 auction, as a result of its bidding strategy, KS&T obtained [redacted] [42]

324. The Claimants' documents confirm that they were [redacted] in Ontario and that they had [redacted][743] As described below, their risky strategy might have worked but for several negligent omissions and miscalculations.

The Claimants Negligently Failed to Take Basic Steps to Allow for CITSS Functionality

325. As Canada explained in its Counter-Memorial, KS&T could have transferred the entire balance of its Ontario CITSS holdings to its California account.[744] By the Claimants' own admission, KS&T was an active participant, "monitoring and trading every day, with specialized expertise and knowledge."[745] It should have been well positioned to take swift action.[746]

326. In response, the Claimants say (i) it is unreasonable to assert that the Claimants should have transferred their allowances within four days of receiving them; and (ii) that the "Claimants' legitimate understanding at the time was that there was no immediate urgency to transfer the allowances abroad even after the election had concluded."[747] The Claimants' arguments are contradicted by their own past practice and the contemporaneous documents produced in this arbitration.

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[741] KS&T made bid through its Ontario account in order to avoid environmental disclosures in California: "Koch Companies have elected not to participate through California accounts due to California requiring unlimited* environmental disclosures, for which they will not provide any helpful guidance. This results in an unacceptable potential exposure." *See* **R-175**, Moore - Mandated Markets Aug18 v2.pptx, 20 August 2018, p. 13 (emphasis added).

[742] [redacted]

[743] [redacted]

[744] Canada's Counter-Memorial, ¶ 323.

[745] Claimants' Memorial, ¶ 72.

[746] Canada's Counter-Memorial, ¶ 323.

[747] Claimants' Memorial, ¶ 673.

327. KS&T had a practice of immediately transferring allowances to its California account.[748] For example, when the jurisdictions were linked on January 1, 2018 KS&T promptly – [redacted] – transferred [redacted] emission allowances in its Ontario CITSS account to California.[749] After the February 2018 auction, KS&T [redacted] its Ontario CITSS account by transferring to California. By the end of April 2018, the balance of its registry account in Ontario was [redacted].[750]

328. Further, on June 15 another participant in the Ontario system successfully executed three separate transfers of emission allowances from its Ontario account to its California account.[751] KS&T likewise could have transferred allowances anytime from June 11 up until the close of business on June 15 (after the Premier-Designate's announcement that morning), as this other participant did.

329. The Claimants' contemporaneous documents contradict their claim that KS&T saw no urgency to transferring the allowances ([redacted].[752] The documents establish that the Ontario PAR, Paul Brown, was asked to transfer the allowances to California on June 13 but he was out of the office, [redacted].[753]

330. [redacted]

[748] Canada's Counter-Memorial, ¶ 124.

[749] Canada's Counter-Memorial, ¶ 57.

[750] **RWS-2**, Ramlal – First Witness Statement, ¶ 54 and Attachment 1, transfers No. 126127, 126246, and 126440. *See also* [redacted]

[751] **C-200**, Email from Jeff Hurdman to Alex Wood, "Preventing Auction Registration", 15 June 2018, p. 1.

[752] [redacted]

[753] [redacted]

331. In summary, even if the Tribunal finds that the Claimants have established jurisdiction, a breach, and causation of damage (they have not), the Tribunal should decline to award damages or reduce the quantum awarded as a result of the Claimants' contributory fault.

VI. REQUEST FOR RELIEF

332. For the foregoing reasons, Canada respectfully requests that this Tribunal:

(a) dismiss the Claimants' claims in their entirety;

(b) require the Claimants to bear all costs of the arbitration, including Canada's costs of legal assistance and representation; and

(c) grant any other relief that it deems appropriate.

September 30, 2022

Respectfully submitted on behalf of Canada,

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