Water Export Controls and Canadian International Trade Obligations
Legal Opinion Commissioned by the Council of Canadians

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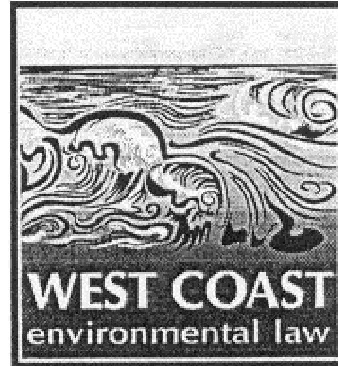

August 17, 1999

Ms. Maude Barlow
Volunteer National Chairperson
Council of Canadians
502 - 151 rue Slater Street
Ottawa, ON KIP 5H3

Privileged and Confidential

Dear Ms. Barlow;

Re: Water Export Controls and Canadian International Trade Obligations

You have asked for our opinion with respect to several questions concerning the status of prospective water export control measures in light of Canadian obligations under the North American Free Trade Agreement and various agreements under the World Trade Organization. We are pleased to provide our response herewith.

By way of introduction however, we should offer two important qualifications to our opinion. The first concerns the degree of confidence that is warranted in making predictions about the outcome of trade disputes and investor claims that may arise in this context. As you will know, many of the international trade, investment and services provisions of NAFTA and the World Trade Organization that might give rise to such disputes and claims are unprecedented and have yet to be the subject of any judicial or arbitral interpretation. Moreover, the water export control measures that have been adopted by some provinces, or which are now being considered by other Canadian governments, are also innovative and similarly untested.

Accordingly, it is extremely difficult to anticipate the views of trade dispute panels or tribunals that may be called upon to address the novel issues that are certain to arise should a trade challenge or investor claim be made in consequence of Canadian water export control measures. We believe that it is regrettable that the federal government's response to this uncertainty is to offer bold and unqualified assertions about the viability of the approach it is advocating. In light of this assertiveness we think it fair to point out its recent and dismal track record in defending Canadian cultural, and research and development programs from trade challenges. As you will probably have noted, in spite of assurances very much like the ones it now offers concerning water export controls, Canada recently lost two important WTO cases concerning its cultural and R and D programs.

The other qualification that should be noted here concerns the conservative approach we have adopted in assessing the potential for conflicts between water export control measures and Canada's international trade conunitrnents. We believe that this approach is necessary because of the nature of the consequences of under-estimating the risks that arise in this context, not the least of which is the fact that an error would be difficult, if not impossible, to reverse. Moreover, the National Treatment and proportional sharing rules of NAFTA would make it virtually impossible for Canada to restrict water exports once they are underway.

We trust that our opinion will shed some light of the important issues that you have raised. Please do not hesitate to contact us should you require any further clarification or assistance.

Sincerely,

West Coast Environmental Law
Steven Shrybman
Executive Director

Legal Opinion: Re: Water Export Controls and Canadian International Trade Obligations Commissioned by The Council of Canadians

The following is our response to the questions you have asked that we address.

1. What are the constraints on Canadian policy and legislative options concerning water exports arising in consequence of Canada's obligations under the WTO and NAFTA?

The basic architecture of both NAFTA and the World Trade Organization is common to both Agreements and can be found in the General Agreement on Tariffs and Trade 1994 (the GATT). There are several provisions of the GATT that impose constraints upon government policy, programs, and legislative options as these may pertain to water. While it is beyond the scope of this opinion to provide an exhaustive catalogue of all such GATT rules, we will highlight the provisions most likely to come into play.

While NAFTA and the WTO share several common elements, there are also important differences between these two regimes. As the following discussion reveals, of the two, the NAFTA is far more constraining of government prerogatives in this context. Accordingly, we would strongly disagree with the view that these differences are insignificant with respect to the issue of water export controls. Moreover an appreciation of the fundamental differences between these trade agreements is critical to identifying a strategy for safeguarding Canadian water from trade agreement based challenges and investor claims.

1.1 Common Elements

1.1.2 GATT Article XI: The Prohibition against Export Controls

The most obvious and likely source of conflict between water export control measures and trade disciplines arises under Article XI of GATT. Article XI.1 provides:

> *No prohibition or other restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licenses or other measures, shall be instituted or maintained by any contracting party on the importation of any product of any other contracting party or on the exportation or*

> *sale for export of any product destined for the territory of any other contracting party.* [emphasis added]

There is an extensive body of trade jurisprudence that has considered and parsed the meaning of each element of this provision as it applies to a considerable variety of *import* control measures. It is fair, we believe, to say that these cases have given Article XI a broad reading and have, at the same time, demonstrated a consistent reluctance to limit or in any other way circumscribe the ambit of its application.

However, there are many fewer cases that have considered the application of this provision to *export* control measures. Coincidentally, the leading cases that have interpreted Article XI constraints from this perspective both concern Canadian export measures for salmon and herring caught off Canada's west coast.

The first of these salmon and herring cases arose under GATT and concerned a blanket prohibition against the export on any unprocessed salmon and herring. The second, which was brought under NAFTA, challenged regulations that imposed certain landing requirements for salmon and herring for the purposes of inspection and biological sampling prior to export. Both cases were brought by the United States. Both were successful in challenging these Canadian regulatory regimes.

It is very relevant to the issues before us that the NAFTA panel interpretation of Article XI as it applies to *export* controls was even broader than that found in the jurisprudence concerning import controls. It is beyond the scope of this opinion, nor is it necessary in our view, to delve into this jurisprudence further to recognize that it would be very difficult to craft water export control measures that would not violate Article XI constraints — with two significant exceptions.

The first would be to adopt a "duty, tax or other charge" that would effectively prohibit or restrict bulk water exports. Allowance for the use of such measures is specifically contemplated by the wording of Article XI. Indeed this is one of the most fundamental points of departure between the GATT/WTO and NAFTA because under NAFTA, Canada has effectively abandoned these options under Articles 302: Tariff Elimination, 309.2 Import and Export Restrictions and Article 314: Export Taxes. For the purposes of establishing water export controls, it would be difficult to overstate the importance of this difference between these two trade agreements.

The second way in which bulk water export control measures might be considered consistent with Article XI would require establishing that water export controls do not apply to a "good" or "product" and therefore are not subject to the Article. This is of course the primary approach being advocated by the federal government. However, the proposition that water in "its natural state" would not be considered a "good" or "product" under Article XI, is not one that is supportable in our view for reasons we detail in responding to Question 2.

But for these two scenarios, water export controls are certain to violate Article XI constraints. In this case however, it may yet be possible to justify those controls if they can be brought within the parameters of Article XX: General Exceptions. However for reasons we explain in addressing Question 5, such an approach would be unlikely, in our view, to succeed.

While other WTO Agreements such as the General Agreement of Trade in Services (GATs) or the Technical Barriers to Trade Agreement (TBT) might be enlisted in aid of a challenge to water export controls, Article XI poses the most likely point of conflict between such controls and the rules of trade. While GATT represents the ground upon which WTO and NAFTA regimes converge, as noted, several elements of NAFTA impose additional limits on Canadian options in this context. We have already noted one of these, in those NAFTA provisions that prohibit the use of export tariffs that might, under WTO rules, have been implemented to effectively ban water

exports. We now turn to a consideration of the other NAFTA provisions that similarly eliminate policy and regulatory options that would have been available to Canada under the WTO.

1.2 NAFTA Constraints

1.2.1 NAFTA Article 301: National Treatment of Exports

The National Treatment requirements of Article III of GATT are restricted in their application to import measures only. Article 301 of NAFTA adopts this provision by reference and in doing so departs from the more expansive wording of Article 105 of the Canada-US Free Trade Agreement. While Article 105 appears to have extended the concept of National Treatment to exports as well as imports, Article 301 of NAFTA appears to retreat from this position by providing:

National Treatment*:*

> *Each Party shall accord national treatment to the goods of another Party in accordance with Article III of the General Agreement on Tariffs and Trade (GATT), including its interpretative notes, and to this end Article III of the GATT and its interpretative notes, or any equivalent provision of a successor agreement to which all Parties are party, are incorporated into and made part of this Agreement* [emphasis added].

However Annex 301.3: *Exceptions to Articles 301 and 309*, specifically excepts export controls on such products as logs and fish. This appears to re-introduce the concern that *National Treatment* requirements might apply to exports after all (i.e., to the goods of a Party) because otherwise these exceptions would not have been needed. It is not possible to predict with any confidence how this question might be resolved by a dispute panel at some unknown future date. However should such a panel conclude that Article 301 of NAFTA was intended to apply to exports as well, it would provide very strong support for the argument that Canada must treat water bound for export markets, in precisely the same way it would water bound for domestic consumption. The implications for water export control measures are obvious.

1.2.2 Proportional Sharing

Another unique feature of NAFTA that has no corollary in WTO Agreements can be found in the 'proportional sharing' provisions of Articles 315 (Trade in Goods) and 605 (Energy and Basic Petrochemicals), which are substantially identical. Article 315 provides:

> **Article 315: Other Export Measures**
>
> 1. Except as set out in Annex 3.15, a Party may adopt or maintain a restriction otherwise justified under Articles XI:2(a) or XX(g),(i) or (j) of the GATT with respect to the export of a good of the Party to the territory of another Party, only if:
>
> a. the restriction does not reduce the proportion of the total export shipments of the specific good made available to that other Party relative to the total supply of that good of the Party maintaining the restriction as compared to the proportion prevailing in the most recent 36-month period for which data are available prior to

the imposition of the measure, or in such other representative period on which the Parties may agree;

b. the Party does not impose a higher price for exports of a good to that other Party than the price charged for such good when consumed domestically, buy means of any measure, such as licenses, fees, taxation and minimum price requirements. The foregoing provision does not apply to a higher price that may result from a measure taken pursuant to subparagraph (a) that only restricts the volume of exports; and
c. the restriction does not require the disruption of normal channels of supply to that other Party or normal proportions among specific goods or categories of goods supplied to that other party. [emphasis added]

In other words, and notwithstanding the exceptions set out in Article XX(g), Canada would be precluded by these provisions from ever reducing the "proportion of total exports shipments of the specific good [in this case water] made available to that party relative to total supply." Another way of stating this is to say that the US is entitled to a proportional share of Canadian water resources in perpetuity, once exports get underway. These provisions once again represent a fundamental departure from WTO rules that impose substantial additional constraints on Canadian policy and regulatory options.

1.2.3 NAFTA Chapter 11: Investment

Chapter 11 of NAFTA establishes an extensive array of investor rights including the right to *National Treatment* (Article 1102), and a *Minimum Standard of Treatment* (Article 1105). By way of further protecting the interests of foreign investors and their investments, the Chapter also proscribes certain government measures such as *Performance Requirements* (Article 1106) and *Expropriation* [without] *Compensation* (Article 1110). Chapter 11, Section B also establishes its own enforcement regime that involves recourse to binding international dispute resolution at the instance of any foreign investor.

These provisions raise issues that are unique to NAFTA and with respect to which there is no parallel in the WTO. As we know, there are now several instances of these provisions being invoked by US investors to challenge Canadian regulatory initiatives. Among these is the case of Sun Belt Water Inc., which late last year filed notice of intent to submit a claim to arbitration concerning certain actions by the BC government which it asserts unfairly deprived it of the opportunity to export bulk water from British Columbia. As of our most recent inquiry, the company has yet to submit a formal claim for compensation under Article 1120.

It is also significant to the task of assessing the potential for successful challenges under Chapter 11, that GATT Article XX exceptions do not apply to these provisions. In other words, investor rights apply notwithstanding the fact that an impugned measure interfering with them, would be justified as a measure "relating to the conservation of living and non-living natural resources," or as "necessary to protect human, animal or plant life or health." It is also absolutely critical to note that Chapter 11 is not in any way limited in its application to trade in goods. In other words, both NAFTA rules concerning investment (and Services) would extend to water, whether water is classified as a good, or not. In fact, the federal government has conceded this point:

> *Chapter 11 does not prevent NAFTA Parties from prohibiting the removal of water from its natural state. But foreign investors seeking to establish investment, or with established investments, for the removal of water from its natural state would have to be treated in the accordance with the obligations of the Chapter (such as national treatment, minimum standard of treatment and the four requirements for an expropriation, if there is one).* [emphasis added]

In other words Chapter 11 disciplines apply to Canadian water resources, including access rights to Canadian water in its natural state. This means that, once governments allow water to be withdrawn from its natural state, as they have done on countless occasions for purposes that range from large scale industrial use to personal consumption, the same rights must now be accorded foreign investors. While the federal government remains silent on the issue of whether water would be subject to the services provisions of NAFTA, for similar reasons, we believe, this result is also inescapable. This arguably means that a water services provider operating in Canada would have the same rights to supply water services to US consumers as to Canadians. In our opinion, two of the most likely bases upon which claims can be made against Canada concerning water export control measures that it may adopt, would be founded on either or both Articles 1102 and 1110. We consider them in turn.

NAFTA Article 1102: National Treatment for Investors and Investments:
National Treatment

> *Each Party shall accord to investors of another party <u>treatment no less favourable than it accords, in like circumstances</u>, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.* [emphasis added]

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With respect to a claim based on *National Treatment* guarantees, it is possible in our view to craft Canadian measures that are more likely to meet the requirements of this provision. In simple terms this would require drafting water export controls measures in a manner that treated US and Canadian investors in the same way, i.e., by denying both water export licenses. With respect to water export controls, the success of this strategy will turn upon a tribunal's interpretation of the phrase "treatment no less favourable than it accords, in like circumstances, to its investors" to mean a comparison of the treatment accorded US and Canadian investors respectively, who are seeking bulk water export licenses or water diversion approvals. Thus a measure that denied such approvals or licenses to both US and Canadian alike would be deemed consistent with Article 1102 requirements.

However, we believe that it is also possible that a panel would choose, for the sake of this comparison, a domestic investor seeking a license for purposes other than export. Thus a company such as Sunbelt Water Inc., seeking a license to provide water services to municipal consumers in California, might be considered an investor "in like circumstances" with a Canadian, Mexican or US company seeking the same access for the purposes of supplying municipal consumers in British Columbia. Thus a tribunal might adopt an interpretation of "in like circumstances" to reference the character of the access rights being sought, either with respect to volume or purpose (agricultural, industrial, municipal service, etc.), rather than the nationality or location of the intended beneficiaries of the investment.

To return to a point we emphasized in the introduction to this opinion, the investment provisions of Chapter 11 represent a very significant innovation in the sphere of international trade agreements and many of the terms and concepts engendered by the provisions of this Chapter are entirely untested by trade dispute of judicial determination. Making predictions about the likely outcome of prospective litigation arising under these rules is a highly uncertain enterprise. It our view however, it would not be prudent to discount the possibility that tribunals convened to determine investor state suits will adopt a liberal interpretation of the provisions of this Chapter. In a contest between free trade and investment policies on the one hand, and the regulatory authority of governments on the other, trade panels have consistently demonstrated a decided preference for the former.

NAFTA Article 1110: Expropriation and Compensation:
Another potential ground for an investor claim under Chapter 11 can be found in the provisions of Article 1110*:*

Expropriation and Compensation.

> *A Contracting Party shall not expropriate or nationalize directly or indirectly an investment in its territory of an investor of another Contracting Party or take any measure or measures having equivalent effect (hereinafter referred to as "expropriation") except…. accompanied by payment of prompt, adequate and effective compensation …. equivalent to the fair market value of the expropriated investment ….* [Emphasis added]

The wording of this Article is obviously very expansive and has already given rise to a wide variety of claims for compensation by both U.S. and Canadian based investors. Article 1110 has no parallel under the WTO. Quite apart from the Sun Belt case, it is reasonable, in our opinion, to anticipate that this prohibition against expropriation may give rise to claims arising in response to Canadian water export controls.

Once again making confident predictions about the likely resolution of such claims should they arise is a perilous enterprise. However, there are several obvious grounds upon which claims might be made by investors seeking redress arising from government imposed constraints on bulk water exports.

S.109 of the *Constitution Act, 1867* explicitly provides for provincial ownership of its lands, mines, minerals, including water resources. However it is also clear that these proprietary rights are not without qualification, which for present purposes includes the rights of riparian users, and of licensees under federal or provincial permits. Moreover, it is entirely possible in our view that a foreign investor seeking to exercise such riparian rights for the purposes of bulk water exports might assert a claim that any denial of the opportunity to do so represents expropriation within the expansive terms of Article 1110. Alternatively, water use permits, which are silent with respect to the particular purpose for which the license was granted, might also give rise to claims under Chapter 11.

Furthermore, it is very unlikely that we will have any definitive resolution of many of the issues that arise in this context if left to the vicissitudes of dispute resolution under Chapter 11. This is the case because there is no doctrine of *'stare decisis'* (judicial precedent) that would bind any tribunal to follow the reasoning or adopt the same interpretation of another tribunal that had considered the same or similar issues. For this reason, if the status quo persists, it will be impossible in our view for Canada to develop water policy or regulatory initiatives with any certainty that these would withstand the rigours of investor-state litigation or for that matter, trade challenge.

1.2.4 NAFTA Chapter 12: Services

Chapter 12 of NAFTA sets out a comprehensive regime to govern trade and investment in the services sectors. While the WTO General Agreement on Trade and Services (the GATs) is analogous, the GATs is much less fully developed than the regime established by NAFTA. This is yet another example of NAFTA rules going far beyond those in place under the WTO.
As for the ambit of Chapter 12, Article 1201.1 provides:

> *This Chapter applies to measures adopted or maintained by a Party relating to cross-border trade in service providers of another Party, including measures respecting:*
>
> a. *the production, distribution, marketing, sale and delivery of a service;*
> b. *the purchase or use of, or payment for, a service;*
> c. *the access to and use of distribution and transportation systems in connection with the provision of a service;*

d. *the presence of a bond or other form of financial security as a condition for the provision of a service.*

Article 1201.1 wording indicates that the Chapter applies, *inter alia*, to US and Mexican companies supplying cross border services to Canadians. But, it also indicates that the Chapter would apply to a US or Mexican based water service provider, for example, operating in Canada for the purposes of providing cross-border services to another jurisdiction. We have not had an opportunity to review the drafting history of these provisions to determine whether this latter scenario was intended. In our view however, the plain meaning of these provisions is clear.

Articles 1206 and 1207 allow for certain reservations and provide for the establishment of certain quantitative restrictions by listing to Annex V of the Agreement. Water is not a listed exception and we are aware of no other provision that would exempt water service providers from rights established by this Chapter. Therefore a company operating in these circumstances would be entitled to *National Treatment* under Article 1202 and the *Standard of Treatment* set out in Article 1204.

Furthermore, and as is the case for Chapter 11, pursuant to the provisions of Article 2102*: General Exceptions,* GATT Article XX doesn't apply to the provisions of Chapter 12. However, 2106.2 does provide:

> *Provided that such measures are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on trade between the Parties, nothing in:*

a. *Part Two (Trade in Goods), to the extent that a provision of that Part applies to services,*
b. *Part Three (Technical Barriers to Trade), to the extent that a provision of that Part applies to services,*
c. *Chapter Twelve (Cross-Border Trade in Services), and*
d. *Chapter Thirteen (Telecommunications),shall be construed to prevent the adoption or enforcement by any Party of measures necessary to secure compliance with laws or regulations* <u>*that are not inconsistent with the provisions of the Agreement*</u>*, including those relating to health and safety and consumer protection.*

This provision appears to offer no meaningful exception to Chapter 12 disciplines because of the proviso that it applies only to "laws and regulations that are not inconsistent with the provisions of the Agreement." A law that denied a water service provider *National Treatment* by not approving a license to supply cross-border water services whether to Canada, or from it, would in our view be inconsistent with the provisions of Chapter 12 and therefore fall outside of the ambit of the purported exception created by Article 2102.2.

In summary:

Even this brief review reveals the considerable exposure that water export regulations would have to trade agreement based challenges or investor claims. As we have seen, these claims may be founded on very different substantive grounds. In addition, trade agreement based actions may arise in two distinct ways.

The first occurs when the state-to-state dispute procedures of NAFTA or the WTO are invoked. For geographic and practical reasons we believe that it is unlikely that such a dispute would arise other than at the instance of the US. In responding to Question 6 we suggest that Canada

address the risks of potential US trade action by, inter alia, seeking amendments to NAFTA and by negotiating a bilateral agreement with the US that would eliminate the possibility of such conflicts.

However, the more pressing concern has to do with the other way in which Canadian water conservation measures might be challenged, that is by way of investor-state claim under NAFTA or one of several bilateral investment treaties to which Canada is a party. Canada's exposure to such claims is far more problematic that the risks of a state-to-state dispute for several reasons. To begin with investor-state claims are more likely to arise because access to these extra-ordinary remedies is virtually unqualified. In addition, foreign investors would not be bound by any bilateral understanding or agreement among the NAFTA parties concerning the application of NAFTA disciplines to water, unless their rights under Chapter 11 were abrogated by explicit amendment. Nor would foreign investors likely feel constrained by any political or diplomatic considerations that discourage state-initiated complaints. Finally, the broadly framed and unprecedented character of the constraints on government initiative engendered by these investment provisions, are far more onerous than those established by other elements of Canada's international trade obligations.

Indeed, as the Sun Belt Water case illustrates, the potential for such claims is more than theoretical. In our opinion therefore, the risk of such claims not only underscores the importance of moving quickly to implement federal legislation banning water exports, but it also reinforces the need to negotiate international measures to prevent them from arising in the future. Therefore, notwithstanding the risks of state-to- state procedures, the first priority is to reduce Canada's exposure to investor-state claims concerning water.

2. Is the regulation of water as a "natural resource" an adequate safeguard against trade agreement based challenges or claims against Canadian ban on water exports?

In an options paper prepared for the Canadian Council of Environment Ministers the federal government indicates that trade considerations lead it to shift its approach from a federal ban on water exports, to a focus on a federal-provincial accord to prohibit bulk removal of water from Canada's drainage basins. Attached to their options paper is a summary of that trade analysis (attached). We believe that it is faulty for several reasons.
To begin with, the assessment begins with the bold assertion that the "watershed approach" it advocates is "consistent with our trade obligations". Unfortunately no analysis or argument is offered to support this assertion other than the statement made by the three NAFTA Parties in 1993 (the 1993 Statement) providing:

> *Unless water, in any form, has entered into commerce and becomes a good or product, it is not covered by the provisions of any trade agreement, including the NAFTA. And nothing in the NAFTA would oblige any NAFTA Party to either exploit its water for commercial use, or to begin exporting water in any form. Water in its natural state in lakes, rivers, reservoirs, aquifers, water basins and the like is not a good or product, is not traded, and therefore is not and never has been subject to the terms of any trade agreement.*

However, in setting out this position the federal government is only restating a contention that it has consistently advanced in response to questions concerning Canada's exposure to trade agreement based demands on its water resources. This begs of course the question of how this historic position might account for its change of heart on the subject of a water export ban. However because of the reliance the federal government continues to place on the 1993 Statement, it is worth considering in some detail.

2.1 Water as a "good" revisited.

As we have seen, under Article 309 of NAFTA and Article XI of GATT, countries are prohibited from imposing quantitative limits on the exportation of goods and products. In order to avoid the prohibition against such export controls the federal government reasons that it must focus its efforts regulation "water resources" which it argues would not be considered a "good" under NAFTA and GATT rules.

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Unfortunately there are several reasons to doubt the validity of this analysis. To begin with, and as many other commentators have noted, water is a "good" a under NAFTA and GATT rules because its is explicitly included under GATT tariff headings. While the federal government has argued that this inclusion only concerns water that has been actually removed from its natural state, — for example water bottled for sale — the tariff schedules include no such limitation. Second, water in its natural state is considered a commercial good under US law. US courts have repeatedly made this determination when called upon to determine the constitutionality of state restrictions on water transfers across state borders. These cases have consistently concluded that groundwater is an article of commerce, rejecting the argument that state governments have the authority to discriminate between in-state and out-of-state water use.

In Sporhase v Nebraska ex rel. Douglas, the Supreme Court of the United States was called upon to determine various matters concerning a Nebraska law that stated that it would not provide a permit for withdrawal of ground water for use in another state unless various conditions were met. In resolving the case, the Court struck down Nebraska's ground-water export control legislation as unconstitutional and held that water is an article of commerce under US law. In doing so the court also rejected the argument that state ownership of water entitled it to discriminate against out-of-state users. Finally the court dismissed the argument that water be treated differently from other natural resources because it is essential for human survival. On this point the Court stated:

> *Although water is indeed essential for human survival, studies indicate that over 80% of our water supplies is used by agricultural purposes. The agricultural markets supplied by irrigated farms are worldwide. They provide the archetypical example of commerce among several states….*

Thus the court concluded that water was an article of commerce in part because of the nature of, and trade in, the commodities that were produced with its use.

Summarizing US law on this point, a recent report by a panel of US and Canadian legal experts to the Governors of Great Lakes States concluded that "*arguments that water is not a good are not persuasive*" and "*indeed ... run contrary to the United States own jurisprudence with respect to the characterization of water as an article of commerce*..." In this light, US support for the notion that water is not subject to NAFTA rules concerning trade in goods unless it has "in any form, .. entered into commerce," would have to be regarded as disingenuous.

Third, water is considered a good under international law. The European Court of Justice has interpreted the term "good" to include anything capable of monetary valuation and of being the object of a commercial transaction (*Commission v. Italy*, Case 7/68). In addition, in *Commission v. Ireland Re Dundalk Water Supply* (Case 45/87), the court held that the term goods includes not only the sale of goods, but goods and materials that are supplied in the context of the provision of services. Where goods are supplied in the context of the provision of services, in order to fall within the goods provisions of the EC Treaty, the importation or exportation of the goods in question must be an end in itself. On this reading, if water is being shipped as a good in order to provide a service, such as providing water for public consumption or agricultural irrigation, then it would be considered a good under the EC Treaty.

Fourth, even were these hurdles to somehow be overcome, a very large proportion of Canadian water resources can already be considered subject to commercial use either because it has been allocated to various users or because it is subject to proprietary claims such as the rights of licensees and riparian users. In British Columbia for example, as of 1993, approximately 40,000 licenses for the withdrawal of surface water were in existence in the province. In fact, many provincial surface water sources are over-subscribed and are identified by the BC Ministry of Environment Lands and Parks as water-short. In the Great Lakes, the largest single use of water is for the very commercial purpose of generating hydroelectric power and is estimated to exceed one trillion gallons per day. In Ontario, millions of litres of water are withdrawn from groundwater aquifers by commercial water bottling companies, each day. Moreover, while water used for individual consumption might not be considered a commercial use, water in municipal distribution systems could hardly be considered water in its "natural state." Therefore even if one were to accept the proposition that "entered into commerce" is the appropriate standard to determine the application of rules concerning trade in goods, a very substantial proportion of Canadian water resources would have to be viewed as having "entered commerce" and for that reason, subject to these trade disciplines.

Fifth, while the 1993 Statement seems to be nothing more than a restatement of US law on the point, even should it be considered as derogating from the principles engendered by NAFTA and WTO rules, it would not be binding on a panel or tribunal called upon to resolve a dispute concerning water export control measures. A recent study by the US State Department describes the use of joint statements at international law:

> *It has long been recognized in international practice that governments may agree on joint statements of policy or intention that do not establish legal obligations. In recent decades, this has become a common means of announcing the results of diplomatic exchanges, stating common positions on policy issues, recording their intended course of action on matters of mutual concern, or making political commitments to one another. These documents are sometimes referred to as non-binding agreements, gentlemen's agreements, joint statements or declarations.* [emphasis added].

In this regard a panel or tribunal would be guided by the principles of *The Vienna Convention on the Law of Treaties 1969* (the Vienna Convention) which establishes the rules governing the application and interpretation of treaties. Articles 31 and 32 of the Vienna Convention deal with the subject of treaty interpretation and supplementary means of interpretation respectively.

> *Article 31.2(b) of the Vienna Convention states that "any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty" should be considered in the treaty's interpretation.* [emphasis added]
> *Article 32 of the Vienna Convention states that "where an interpretation under Article 31 leaves the meaning ambiguous or obscure, then recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion*". [emphasis added]

Therefore, an important question that arises here is whether the Statement should be considered as having been "accepted" by the US, within the meaning of Article 31.2(b) of the Convention. Which brings us the circumstances in which the 1993 Statement was released. Here we must note the rather startling degree of informality that surrounds this 1993 Statement upon which Canada has placed so much reliance. In fact this 1993 Statement is no more than an unsigned document, on blank paper, released as an attachment to a press statement issued by the government of Canada on December 2, 1993. There is no indication that either government offered formal support for it. Yet approval by the US Senate is required under the US Constitution with respect to all international treaties.

Rather, evidence of US support for the 1993 Statement also comes in a press statement dated December 2, 1993 and issued by the Office of the United States Trade Representative. It is not signed, nor is there any other indication of its authenticity. This press release in part reads as follows:

> *Along with Prime Minister Chretien's announcement of his intention to proclaim the NAFTA, the Governments of the United States, Canada, and Mexico are today releasing a joint statement of future work on dumping and antidumping duties and subsidies and countervailing duties, and a joint statement on natural water resources and the NAFTA. Canada has also released a separate statement on energy which underscores the Canadian Government's commitment to energy security for Canadians. None of these statements change the NAFTA in any way.* [emphasis added]

While the USTR press release does refer to the "joint statement" it also appears to qualify its effect in terms quite different than those found in the 1993 Statement itself. On these facts then, the 1993 Statement would not likely satisfy the requirements of the Vienna Convention even with respect to interpretative notes. However, even if we are wrong on this point, under the provisions of the Vienna Convention the 1993 Statement might play a role if provisions of NAFTA were deemed by a trade panel or tribunal to be unclear or ambiguous. However, even in this case, it could not operate to displace the clear meaning NAFTA requirements. Indeed this is very point the USTR pointedly made.

3. Is the proposed *Canada-wide Accord for Prohibiting Bulk Water Removal from Watersheds* (the Accord) an effective mechanism for regulating bulk water exports or diversions?

Draft proposals for this Accord provide in part:

> *Federal, provincial and territorial ministers responsible for the environment commit to a Canada-wide approach for the protection of Canadian waters, in part by prohibiting bulk removal of water from Canadian major drainage basins, including for the purposes of export. The goal is to provide sustainable management of waters, ensure clean, productive and secure fresh water resources and ecosystems while promoting social, economic, and environmental benefits for present and future generations.*
> *We agree that: Each jurisdiction will determine the approach to be used for achieving the common objective of prohibiting bulk water removal from major drainage basins.*

We suspect that the notion of such an *Accord* would seem like a reasonable, even desirable approach for dealing with the problem of bulk water exports. In fact, when viewed from the perspective of federal-provincial relations, the *Accord* has certain features to recommend it. It would, for example, offer an opportunity to integrate the efforts of provincial and federal government to ban water exports and diversions. The *Accord* also embraces the concept of watershed management, which has strong appeal from an environmental policy perspective.

3.1 Of itself, an Accord would do nothing to Prohibiting Water Exports

However we believe that there are four fundamental problems with this approach to safeguarding Canadian water. To begin with, the Accord would of itself do nothing to actually prohibit export initiatives that might be undertaken by provincial governments, municipalities, Crown agencies, corporations or even private parties. This would require legislation, and when it comes to international trade, it is the federal government, and not the provinces that has the constitutional

authority to regulate. While jurisdiction over water resources in Canada is shared, the same is not true for federal powers concerning international and inter-provincial trade. This should justifiably raise questions about the purposes of an Accord which appears to shift responsibility to provincial governments for matters with respect to which they have little constitutional authority.

Second, the Accord is not legally binding on the provinces, nor are there proposals to equip it with a credible enforcement mechanism. Thus governments, perhaps upon a change of political administration, would be able to abandon obligations they have agreed to under the Accord.

Moreover the ability of governments to readily extricate themselves from such commitments is likely to be formally expressed in the Accord itself. For example, the federal government has indicated that it would use a similar accord concerning the environment as prototype for this initiative. Under that arrangement, "a government may withdraw from the Accord six months after giving notice." Finally on this point, Quebec would be unlikely to endorse such the Accord as it has declined to do for the Environmental Harmonization Accord.

Third, by indicating that provinces will be free to develop their own approach to achieving the goals of the Accord, the federal government is setting the stage for a patchwork of policies and regulations across the country. While this problematic from a public policy point of view, it is even more so, when the principle of *National Treatment* is considered. We consider the implications of differential provincial policies from this perspective below.

For these reasons, an Accord would not in our opinion represent a credible or durable guarantee against bulk water exports, and would not therefore, be an adequate substitute for legislation that would establish enforceable sanctions against such exports. However there is another, and in our view more important, reason for rejecting this federal strategy which has to do with the risks inherent in negotiating such an Accord in the NAFTA context. For reasons we describe below, while an Accord would itself do nothing to actually prohibit water exports, it might well undermine this objective by exposing Canada to investor-state claims that would not otherwise arise, or that would be easier to defend against should they be brought. We believe that this risk exists because of the National Treatment obligations engendered by NAFTA.

3.2 An Accord May Increase Canada's Exposure to NAFTA Based Claims

We should begin by noting a critical distinction between the *National Treatment* obligations of the federal and provincial governments, respectively. While the federal government in obligated to provide best-in-Canada treatment to all foreign investors, the same is not true for provincial governments, which are obligated only to provide best-in- province treatment to such investors. Thus Article 1102(3): National Treatment, provides:

> *The Treatment accorded by a Party …. Means with respect to a state or province, treatment no less favourable than the most favourable treatment accorded, in like circumstances, <u>by that state or province to investors</u>, and to investments of investors, of the Party of which it forms a part.* [emphasis added]

However, in our view, by entering into an Accord, provincial governments may be exposing themselves to claims that they provide best-in-Canada treatment with respect to any licenses or permits to provincial water resources they have the authority to grant. Thus an export approval sanctioned by another province or the federal government may well set a standard with respect to which all other provinces must conform. Such a claim may be asserted on one or both of two grounds.

The first would assert that the Accord itself, and any action taken pursuant to it, be considered subject to federal, not provincial National Treatment obligations. The success of this argument will depend on a Tribunal's views of whether the Accord should be seen as a "measure" "adopted by or maintained" by either, or both, the provincial or federal governments. For example a Tribunal

might conclude that actions taken under an Accord be considered measures taken by the Canadian Council of Ministers of Environment (CCME) and therefore subject to best-in-Canada *National Treatment*.

In any event, it seems inevitable that making this determination would necessarily require that a Tribunal consider and make judgments about Canadian constitutional arrangements. It would almost certainly be confronted with argument that only the federal government should be seen as having the authority to ban water exports or negotiate a "Canada-wide" agreement on any subject. This raises the spectre of Canadian constitutional law being interpreted and applied by an international panel, applying international legal principles, and operating almost entirely outside of the Canadian legal context.

Whatever other concerns might be justified about such an eventuality, it is very clear that the results of such an inquiry would again be highly uncertain. Given the inherent unpredictability of dispute resolution in this context, it would be unwise in our view to discount the possibility that a Tribunal might expand provincial *National Treatment* obligations for provinces that might enter into an Accord under the auspices of the CCME. This would, in our view then imbue all actions taken under the Accord with the taint of 'best in Canada' National Treatment obligations, even where the initiative is one taken by a provincial government. In this scenario, any jurisdiction in Canada that embarked upon, or even acceded to, bulk water exports on terms contemplated by the Accord might establish the *National Treatment* benchmark to which all other jurisdictions would be held.

Thus simply by entering into an Accord, and regardless of its contents, the provincial government would be exposing provincial measures to trade disputes and investor-state claims that would be less likely to arise, or succeed, in the absence of the Accord.

The second way in which an Accord may engender National Treatment obligations that would effectively enlarge the ambit of provincial obligations under Article 1102 has to do with concept of "watershed" which is presented by federal draft proposals as "the natural unit for managing water." Federal proposals concerning the Accord have described Canada as being divided into five major drainage basins or watersheds, each consisting of a series of smaller or regional watersheds. It is important to note that several of these watersheds cross international boundaries and that at least one extends far into the United States.

Because these watersheds bridge inter-provincial and international boundaries the clear implication is that provincial measures must now be judged in this broader context. For example if a province enters into an Accord on the basis that it will manage on a watershed basis with one or more provinces or territories, it would be difficult in our view for it to meet the complaint that it has declined the same offer to US jurisdictions. It would, in other words, be in breach of its obligations to provide National Treatment to US investors or service providers by refusing to enter into similar management arrangements with respect to watersheds that cross the international boundary.

Indeed, the federal governments description of watersheds as 'Canadian' is a misuse of the term (we assume inadvertent) because 'watershed' describes a geographical feature without regard to political boundaries. It is not surprising therefore that the concept of watersheds is problematic for initiatives intended to secure resources management prerogatives for political institutions with very different boundaries. This is particularly true in the context of international trade and investment agreements that are intended to transcend these same boundaries.

While ecosystem-based watershed management is a desired outcome from an environmental policy perspective, in the context of *National Treatment* proportional sharing and investor-state litigation it invites the potential for serious and largely unpredictable consequences flowing from Canada's commitments under NAFTA. Moreover the concept of watershed or ecosystem management is not one that NAFTA recognizes. This means that it might not be possible to distinguish between in-basin and out-of-basin users, investors or service providers without

offending the NAFTA's National Treatment obligations. This point deserves to be stressed because it would preclude entering into an ecosystem based management approach to international waters, such as the Great Lakes without opening the door to claims by investors or services providers located outside of the basin that they be accorded 'treatment no less favorable'. Ultimately a Tribunal might conclude that out-of-basin claimants are not 'in like circumstances' with those within the basin. However, there is no reason to be confident about such an outcome.

To sum up then, at best the imposition of these multi-lateral constraints makes the terrain of inter-provincial negotiations far more difficult to negotiate. Moreover, the success or failure of efforts to chart a safe course through the landmines established by these trade and investment regimes will only be determined after-the-fact by trade panels and tribunals operating almost entirely outside the context of Canadian law and legal institutions.

4. Would the export of water from one Canadian province have implications for other provinces and/or the federal government.

The federal Options Paper we have noted specifically addresses this issue and concludes:

> *If legislation permits bulk removal of water in one province and a project is approved, this does not mean that other provinces have to follow suit.*

For the reasons we have just related, we don't agree. However, having considered this question in the context of a prospective Accord, we should also note two other ways in which water exports from one Canadian jurisdiction will, in our view, clearly impact on others and which exist quite independently of an any Accord.

The first has to do with the possibility of a *National Treatment* complaint being made to challenge federal measures intended to prohibit bulk water exports should the government have acquiesced to such exports before having established such a ban. Because federal authority to prohibit water exports is clear under Canadian constitutional law, a failure to exercise that power to prevent export approvals or undertakings would certainly support an argument that National Treatment rules would preclude such export constraints in other cases. In other words by failing to prohibit water exports in any case, the federal government would be precluded from according 'less favorable treatment' in all others. It is important therefore to stress the importance of swift federal action to prohibit water exports.

The second has to do with the impacts of the proportional sharing provisions of NAFTA which we have described above. These commitments clearly bind Canada and are in no way confined to the territory of a provincial government that may issue such export permits. In other words, the claim to an ongoing share of Canadian water resources that might be asserted under Article 315 would persist notwithstanding the unwillingness or inability of the granting jurisdiction to maintain export flows. In the case that water is drawn from inter-provincial watersheds or groundwater regimes the implications are obvious. However, quite apart from these direct impacts, it is entirely possible that proportional guarantees would exert pressure on the water resources of provinces not party to the original export commitments, particularly if shortages arise in the province or territory that was.

Accordingly we must pointedly disagree with federal assertions on this point. We should also indicate our disagreement with another statement made by the federal government concerning the rights of foreign investors under NAFTA, which is that "The same principles would apply to investors of other NAFTA countries as to Canadian investors." To be blunt, this is simply untrue. The right to *National Treatment*, the right to compensation for actions that 'directly or indirectly' expropriate investments, and the right to invoke international arbitration to recover damages – are

simply not available to Canadian investors. These represent fundamental differences between the substantive and procedural rights of foreign and Canadian investors respectively.

5. Are the safeguards provided by Article XX(g) of the GATT adequate to protect Canadian water export control measures from trade challenge and/or investor state claims?

Article XX: *General Exceptions*, provides in part:

> *Subject to the requirement that such measure are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures:*
> *….. (g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production and consumption;*

There have been a considerable number of international trade panels that have had occasion to parse the meaning of these provisions in some detail. In fact the WTO Appellate Body has also offered its views on the meaning of these provisions most recently in the Shrimp Turtle case.

Moreover there is also now a considerable body of legal literature on this subject. However, a review of these cases or of the commentary is clearly beyond the ambit of this opinion. Suffice it to say that expert opinion is divided upon whether it is possible, or how to craft export controls which would satisfy the requirements of Article XX(g). Furthermore whatever the differences in legal opinions expressed about these cases, certain facts undeniably emerge.

First, every challenge to a resource conservation measure that has been mounted under NAFTA and WTO has succeeded. Second, in no case has a trade panel or Appellate Body been willing to uphold a conservation measure on the grounds that it fell within the ambit of Article XX.

Moreover, in every case, trade panels and the Appellate Body have found several reasons for dismissing the applicability of Article XX exceptions. In fact, in the Shrimp-Turtle case, which is taken by many as the high water mark for trade jurisprudence concerning conservation measures, the AB found no less than seven distinct grounds upon which to impugn US marine mammal conservation measures. To further complicate matters, panels and the AB has often taken inconsistent and contradictory approaches to addressing these issues, a problem that has even drawn stern comment from the AB itself.

For these reasons we believe that the challenge of crafting water export controls to satisfy Article XX requirements would be daunting. It would not therefore be reasonable in our view to build Canada's strategy for protecting water resources from export demands upon the premise that it will by dint of its own ingenuity, be able to succeed where all others have failed.

Perhaps more to the point however, in our opinion the entire exercise is moot for three reasons. The first is that, as noted, the provisions of Article XX are specifically excluded from application to the Investment and Services rules of NAFTA. These provisions are, as we have also noted, the most problematic constraints on Canada's ability to ban bulk water exports or diversion.

Furthermore Article 315 which establishes a "proportional sharing regime" for all goods, also explicitly limits the application of Article XX. Finally, the wording of Article XX(g), notably that export controls be "made effective in conjunction with restrictions on domestic production and consumption," explicitly precludes the possibility of Canada imposing such export restrictions so that it can manage water resources sustainably and avoid the need to impose domestic restrictions.

6. What would represent the most effective strategy for establishing a ban on bulk water exports or diversions from Canada?

6.1 Federal Legislation to Ban Water Exports

For reasons that follow from our critique of the proposed Accord, in our opinion the best federal approach for preventing bulk water removals from Canada is the enactment of federal legislation designed specifically for this purpose**.** In fact, we believe that such legislation is essential if water protection objectives are to be realized. Moreover, for reasons we have described in responding to Question 4, delay in promulgating this legislation may significantly increase Canada's exposure to trade disputes, or investor claims, particularly if water export initiatives proceed in the absence of a federal statutory prohibition. This may, in turn, create *National Treatment* obligations that undermine the prerogatives of provincial governments.

It also follows from our responses to the other questions, that no matter how carefully designed, Canadian measures to prevent bulk water exports or diversion projects would still be vulnerable to trade challenges and/or investor-state claims. We need to stress however, that the potential for such disputes should not in our view be taken as an excuse for inaction. To do otherwise would not only increase the risk of trade or investor disputes, but would also concede the very legal ground that we believe Canada might successfully defend.

6.2 International Initiatives

For these reasons we believe that the immediate priority should be to implement domestic export controls. With a sound statutory framework then in place, the next step would be for Canada to pursue international measures to both strengthen these domestic initiatives, and avert the risk of trade challenges and investor claims concerning such measures. In our view these fall into two generic categories. The first is to seek an exclusion, exception or waiver for such measures in accordance with the requirements of the particular trade or investment agreement. These exclusions may in turn be specific to particular provisions or, better still, apply across the board as general exceptions to, or exclusions from, the entirety of the particular trade agreement.

The other possible approach would be to negotiate an international agreement dealing specifically with water that would explicitly supersede Canadian trade and investment obligations and take precedence in the event of conflicts with them. These two options are not mutually exclusive and should in our view be pursued as part of a comprehensive strategy that would ideally integrate the two approaches.

6.1.2 Protection from WTO Based Claims

As we have seen, the most problematic conflicts between water export controls and Canadian trade and investment commitments arise under, and are unique to, NAFTA. Thus while the WTO includes and an *Agreement on Trade-Related Investment Measures* it represents a bare rudimentary framework that engenders neither a commitment to *National Treatment* nor provisions concerning expropriation. The same is true of the skeletal WTO Agreement on Trade in Services (GATs). However the GATs is on the agenda for the next Ministerial meeting that will take place later this year in Seattle, and the US has already signaled its ambition to very substantially enlarge the scope of its application. Also absent from the WTO are any rules analogous to the proportional-sharing regime established under NAFTA Articles 315.

While the general prohibition against export controls established by GATT Article XI is definitely problematic, WTO rules allow the imposition of export taxes on water resources, which in our

view could be adopted as an effective impediment to bulk water exports. As noted, such taxes are prohibited under NAFTA. However, the imposition of such export charges at levels insufficient to effectively eliminate water exports, might actually create an incentive to export water as a source of new revenue. For this reason this option may not be a desirable one.

More to the point however, because pressure on Canadian water resources is most likely to come from the US, the availability of effective safeguard measures under the WTO is of little avail in attempting to protect Canadian water resources from US claims. For these reasons we believe that efforts to protect water from trade agreement based claims should be firmly fixed on US claims arising under NAFTA.

6.2.2 Protection from NAFTA Based Claims

In terms of seeking trade agreement-specific exemptions for water export measures, we believe that the preferred option would involve negotiating a broad exception for such measures such as the general exception for National Security measures provided by NAFTA Article 2102. This would imbed in NAFTA broad protection from the various constraints imposed by this regime on Canada's ability to establish effective water export controls. Far less effective, but still of some value, would be exemptions specific to certain elements of NAFTA, such as those concerning investment and services. Given the particular problems presented by the investment and services provisions of NAFTA, addressing these aspects of NAFTA would, in our view, still be helpful.

Addressing Potential Challenges or Claims Arising under NAFTA Chapter 11
For reasons we have already discussed, particular attention needs to be paid to addressing the risks of investor-state claims being made in consequence of prospective water export controls. There are several ways in which water export measures might be sheltered from claims arising under Chapter 11 of the NAFTA. We believe the most effective approach would be to negotiate a general carve out for such measures under these trade regimes, or as amendment to the provisions of a particular chapter, in this case Chapter 11*: Investment*. A less effective alternative would involve having the NAFTA Commission issue a statement in accordance with the provision of Article 1131.2 of the text that provides:

> An interpretation by the Commission of a provision of this Agreement shall be binding on a Tribunal established under this Section.

Accordingly, the Commission would issue an interpretative note clarifying the meaning of "investment" under Article 1139 which defines this term for the purposes of the Chapter. This interpretation would be issued to make clear that "investment" was not intended to include any license, authorization or permit to water.

The other option for removing the possibility of challenges to water export measures arising under certain provisions of Chapter 11 would be to amend Article 1108 *Reservations and Exceptions* to include specific exceptions for such measures. A better approach in our view would be to amend Annex 1138.2 to include an explicit exclusion from dispute settlement for federal and provincial legislation banning the extraction of water for the purposes of bulk export or diversion.

In sum therefore, in our view the best option for protecting Canadian measures to prohibit bulk water exports from challenge under Chapter 11 would be to negotiate a general carve our for water under NAFTA. There are however, two other, albeit less effective strategies, that would still represent an improvement over the status quo. The are:

- an interpretative note issued by the Commission clarifying that the definition of investment set out in the Chapter was not intended to include any claim to water; or,

- an addition to Annex 1138.2 to exclude from dispute settlement under the Chapter, federal and/or provincial legislation banning bulk water exports.

Of the two, we believe the latter approach is more likely to be effective because it should substantially reduce the possibility of investor-state challenges to Canadian water export control measures.

Addressing Potential Challenges under NAFTA Chapter 12: Services

No analogue to Article 1131.2 exists in Chapter 12, however both Article 1201.2*: Scope and Coverage a*nd Article 1206: *Reservations* set our various exceptions to the provisions of the Chapter. As is the case with respect to Chapter 11, Annexes to the Chapter offer another opportunity to exclude water export measures from the application of service related disciplines. In all cases, however, formal amendment of the provisions of the Chapter would have to be sought in order to exempt water export controls measures from challenge under the Chapter.

In our opinion, and for reasons just noted with respect to the Chapter 11, the best approach would be to seek a specific exclusion for federal and provincial water protection legislation. A less attractive alternative would be to amend Article 1201.2 to exclude all water related services from other application of Chapter 12 rules.

A General Exception for Water under NAFTA

While state-state disputes concerning water may be less likely to arise than investor-state claims, they nevertheless pose a significant risk to water export control measures and should in our view be addressed if the integrity of those measures is to be assured. For this reason, and for the purposes of comprehensiveness, the better course to addressing potential trade conflicts on a Chapter by Chapter basis, would be to negotiate a general exception for water protection measures in accordance with the provisions of Chapter 21. In this regard the very broad exception established under Article 2102 with respect to *National Security* provides a useful prototype for such an exception. To paraphrase and expand slightly upon the terms of this Article, this exception might be drafted to provide that:

> Nothing in this Agreement shall be construed to prevent or in any other way limit a Party from taking any action that it considers necessary for the protection or conservation of water in any form including:
>
> - relating to the extraction or trade of water for export or by diversion; or,
>
> - relating to the implementation of national policies or international agreements respecting the conservation or protection of water.
>
> Furthermore, any action taken by Party in furtherance of these objectives will not be subject to the dispute settlement provisions of Section B of Chapter 11, and of Chapter 20.

The obvious advantage to such an approach is that it provides an exception for water export measures from all provisions of NAFTA. With the usual caveat about the need for caution, we believe that if properly drafted, such a general exception would likely provide effective protection from NAFTA-based challenges to Canadian water export measures. The possibility of a US state-to-state challenge under the WTO could then be addressed by imposing an export tax on Canadian water that would effectively preclude exports. Should this course not be desirable for other policy reasons, a similar exception or carve out would need to be negotiated under the WTO. Given the diversity of interests in water that might come to fore in the global context, we can not comment on the likelihood of succeeding with such efforts.

6.2.3 An International Agreement on Water Sovereignty

In our view, it would also be desirable to negotiate a bi-lateral agreement with the US concerning water conservation that would explicitly recognize the sovereign authority of both Canada and the US to ban, embargo or tax water exports, in whatever form, or mode of withdrawal. That treaty should include a clause asserting the paramountcy of its provisions should conflicts arise with other international agreements including those concerning trade, investment and services.

In Conclusion

As we have noted, in offering our opinion on the questions you have asked that we address, we have adopted a conservative approach that we feel is justified given the enormous uncertainties and risks that abound in this context. Taking this approach, we do not believe that it is possible to craft effective water export control measures that would not be in breach of Canada's obligations under both the WTO and NAFTA. However, the potential for such conflicts should not delay action by the federal government to ban water exports. Indeed for the reasons noted, delay in doing so is likely to further limit Canada's options should water export undertakings proceed in the absence of federal statutory prohibition.

To assure the integrity of such export controls, we believe that it is also necessary for the federal government to negotiate international measures that would safeguard such controls from challenge under the international trade and investment agreements to which it is a party. Conflicts with the provisions of both WTO and NAFTA need to be addressed, in this regard. But of these two trade agreements, NAFTA is by far the most problematic. Not only does it foreclose policy and regulatory options that would be available under WTO rules, but it accords foreign investors direct access to powerful international dispute resolution processes to enforce the broadly framed rights NAFTA creates to their benefit. For this reason, addressing the constraints imposed on Canadian policy and regulatory options established by NAFTA should be Canada's first international priority.

We have identified several options for insulating Canadian water export control measures from challenges and/or claims brought pursuant to NAFTA provisions. Of these, a broad exclusion similar to the one established by NAFTA for national security measures is likely to be the most effective. A similar approach might be adopted for addressing potential conflicts with WTO rules. Finally, because challenges to prospective Canadian water export controls are likely to emanate from the US, we believe that it would also be highly desirable for Canada to negotiate a bi-lateral agreement with the US that explicitly recognizes the sovereign prerogatives of each country to manage its water resources. That agreement should stipulate that its provisions will prevail in the event of conflict with international trade and investment agreements.

We trust that this opinion will be of some assistance. Please do not hesitate to contact us should you need further clarification or assistance.

Sincerely,

Steven Shrybman LLB
(Member of the Ontario and BC Bar)
Executive Director
West Coast Environmental Law Association