

## **Q&A BACKGROUND on METHANEX'S NAFTA CLAIM**

***Updated: August 22, 2005***

### ***What is the background of the claim?***

In June 1999, Methanex initiated a claim under Chapter 11 of the North American Free Trade Agreement (NAFTA) against California's March 25, 1999 decision to ban MTBE. Chapter 11 permits foreign investors to make claims against national governments for regulatory actions that contravene protections afforded by the NAFTA.

On August 7, 2002, a NAFTA arbitration panel rejected all but one of the defenses raised against Methanex's claim. The final issue – whether a methanol producer has the standing to bring a NAFTA claim on a measure related to MTBE – required a “fresh pleading” to the panel by Methanex, made in November 2002.

After these preliminary rulings, Methanex's claim was heard in a Jurisdiction/Merits hearing that started June 7, 2004 in Washington, DC.

In its August 3, 2005 judgment, the NAFTA Arbitration Tribunal ruled against Methanex.

### ***What was the amount of the damages Methanex was seeking?***

Methanex was claiming damages of US\$970 million.

### ***What was the basis for the damages amount?***

Methanex used a third-party expert to assess the damages under the NAFTA resulting from California's decision to ban the use of MTBE in that state. The damages expert estimated the future impact to Methanex's business based on reduced sales volume, reduced pricing and increased costs (among other factors).

### ***What was the basis of the claim?***

Methanex's claim was that the actions taken by the Government of California to ban the use of MTBE by the end of 2002 (as amended to 2003) constitute a breach of Articles 1102 (National Treatment), 1105 (Minimum Standard of Treatment) and 1110 (Expropriation) of Chapter 11 of NAFTA.

Methanex believes that it is a well-recognized principle in the United States and international law that governments should not expropriate business interests if there are other appropriate alternatives.

Methanex believed that banning MTBE failed to achieve California's purpose and that there were other more appropriate alternatives. Under the NAFTA, if expropriation is selected, fair and equitable treatment and compensation, among other things, should be provided, which did not occur in Methanex's case.

***What are the alternatives to banning MTBE?***

When Methanex filed its claim, it also outlined alternative suggestions in a Five-Point Plan on gasoline, MTBE and the environment. As well as seeking to preserve air quality, Methanex's plan addressed broader gasoline and environmental issues rather than unfairly and inequitably targeting MTBE.

Given that MTBE detection in the environment is a direct consequence of gasoline releases, Methanex has repeatedly asked the question:

***“How does banning MTBE stop gasoline releases into the environment?”***

The answer to the question is that it does not. Methanex also made a submission under the environmental side agreement to the NAFTA regarding the lack of enforcement of water protection environmental laws in the state – that submission reinforced the state's own auditor's report from 1998 that provided a scathing commentary of California's failure to enforce its environmental laws.

Methanex's Five-Point Plan on gasoline, MTBE and the environment includes:

1. Providing greater flexibility to refiners by eliminating the 2% oxygenate mandate included in the federal reformulated gasoline program
2. Measures to ensure that the better of current or future air quality standards and existing gains from vehicle emission reductions already achieved by the use of oxygenates are not lost – i.e. no backsliding on air quality
3. More effective enforcement and regulatory programs to prevent the release of gasoline to the environment
4. More aggressive gasoline and MTBE remediation and treatment efforts and increased funding to support remediation and treatment research and development
5. Comprehensive consumer education programs on the proper handling and use of gasoline and the environmental benefits and risks of gasoline and MTBE

***How many other (NAFTA) claims of this kind have there been?***

Methanex's claim was the second Canadian investor claim against the United States.

There have been several claims by United States investors against Canada, with the most notable being the Ethyl case regarding the Canadian government's ban of MMT (coincidentally MMT is also a gasoline additive). The Canadian government settled the Ethyl claim. There are similarities between aspects of the Ethyl and Methanex claims.

***Should Methanex have used the NAFTA agreement to advance its own commercial interests?***

Methanex's claim is precisely what the NAFTA Chapter 11 was intended for.

Chapter 11 explicitly provides mechanisms for resolving disputes of this kind. The NAFTA's basic purpose is to liberalize trade and encourage investment. The actions Methanex took were designed to protect its US investment against the kind of arbitrary action California has taken.

The NAFTA Chapter 11 cannot change California's laws; it can only result in the award of damages actually incurred by the claimant.

It is also important to note that Chapter 11 of NAFTA itself is modelled after the hundreds of bilateral investment treaties that have been negotiated by the United States and other countries to protect foreign investors from similar actions.