COMMENTS

A STEP IN THE WRONG DIRECTION: THE *LOEWEN* FINALITY REQUIREMENT AND THE LOCAL REMEDIES RULE IN NAFTA CHAPTER ELEVEN

Although more than a decade has passed since Canada, Mexico, and the United States enacted the North American Free Trade Agreement ("NAFTA"),[1] the treaty continues to make more than its fair share of headlines and to draw substantial criticism. Among other things, scholars and tribunals are still trying to decipher the meaning and extent of the investment provisions of Chapter Eleven,[2] which were designed to protect foreign investors in NAFTA countries by imposing international standards of treatment. Since Chapter Eleven potentially governs many transactions and may give rise to international liability of member states, it is critical that the international community deal adequately with these interpretation problems.

Among the most recent problems are questions concerning whether the local remedies rule applies under the Chapter Eleven regime, and, if so, how it applies. The local remedies rule is a standard of customary international law that requires parties who have been injured in a foreign nation to exhaust all other available remedies prior to seeking international redress.[3] The requirement ensures respect for the sovereignty of the host nation by treating all nations as competent to repair their own wrongs, and it guarantees the host nation the first chance to avoid international liability.[4] But it is unclear whether the local remedies rule is applicable under NAFTA. Article 1121, which requires investors to give up ongoing or future domestic claims as a condition precedent to seeking relief under Chapter Eleven, has been interpreted by some to waive the local remedies rule for Chapter Eleven claims.[5] However, no international tribunal has decided conclusively whether the local remedies rule applies under NAFTA.

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[1] North American Free Trade Agreement, Dec. 17, 1992, U.S.-Can.-Mex., 32 I.L.M. 289, 605 (entered into force Jan. 1, 1994) [hereinafter NAFTA].

[2] *Id*. art. 1101–38, at 639–49.

[3] *See infra* Part III.

[4] *See infra* Part III.B.1.

[5] *See infra* Part IV.

In a recent case, *The Loewen Group, Inc. v. United States*,[6] it appeared as though the international community might finally get an answer to this important question. Seldom has a state trial court decision caused a stir like the one involved in *Loewen*, and seldom has the anticipation of a soon-to-be-released international arbitral award sparked such heated debate.[7] The *Loewen* decision concerned a $500 million Mississippi jury verdict against a Canadian corporation that resulted in a claim against the United States alleging, among other bases for international responsibility, a denial of justice in violation of Chapter Eleven's "Minimum Standard of Treatment" clause.[8]

Loewen presented an opportunity to settle the important issue of whether Article 1121 waives the local remedies rule. However, by misinterpreting the breadth of the local remedies rule and thereby managing to avoid the Article 1121 waiver debate altogether, the decision cast the interpretation of Chapter Eleven into an even greater state of confusion. Essentially, the tribunal held that because Loewen failed to appeal the trial court's decision, its claim failed a "finality" requirement. This finality requirement, in the tribunal's view, is not part of the local remedies rule, but is instead a separate, substantive requirement that would appear to apply only where the denial of justice is the result of an injury initiated in the courts. Therefore, the tribunal held that, regardless of whether Article 1121 waives the local remedies rule, it does not

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[6] ICSID Case No. ARB(AF)/98/3, 42 I.L.M. 811 (NAFTA Ch. 11 Arb. Trib. 2003). The award, along with the briefs and memoranda, are available at http://www.naftalaw.org.

[7] As one critic stated,

> Now, foreign corporations could attempt to evade verdicts rendered against them through due process in a U.S. court, by filing a suit to be heard by a three-person tribunal, behind closed doors. In essence, the United States is surrendering its control . . . . Moreover . . . this case could completely undermine the importance that the U.S. judicial system has placed on juries . . . . [T]he tribunal did not limit what types of cases amounted to government measures, leaving the door open for this principle to be extended all the way up to the Supreme Court.

Andrew J. Shapren, *NAFTA Chapter 11: A Step Forward in International Trade Law or a Step Backward for Democracy?*, 17 TEMP. INT'L & COMP. L.J. 323, 343 (2003) (internal citations omitted). Similarly, two advocacy groups, Public Citizens and Friends of the Earth, cited *Loewen* as evidence of NAFTA's infringement on U.S. sovereignty and have called for renegotiation of Chapter Eleven. Renée Lettow Lerner, *International Pressure To Harmonize: The U.S. Civil Justice System in an Era of Global Trade*, 2001 BYU L. REV. 229, 243. For a description of the development of NAFTA Chapter Eleven's "legitimacy crisis," see generally Ari Afilalo, *Towards a Common Law of International Investment: How NAFTA Chapter 11 Panels Should Solve Their Legitimacy Crisis*, 17 GEO. INT'L ENVTL. L. REV. 51 (2004).

[8] As this Comment discusses in greater detail in Part II, the case involved the Canadian corporation's appeal to a NAFTA tribunal of the adverse state court judgment, which was alleged to constitute a denial of justice because, among other things, the damage award was unusually high and the judge allowed the trial to be infected by discrimination.

waive the substantive finality requirement—an independent bar to Loewen's claim.

The tribunal's definition of the local remedies rule was incorrect. As this Comment argues, both legal reasoning and the weight of international precedent suggest that the finality requirement is, and always has been, a part of the local remedies rule. Therefore, if Article 1121 waives the local remedies rule—and this Comment argues that it does—it also waives any requirement of finality. Because it has become common for parties to waive the local remedies rule in agreements only recently, the subject matter of the *Loewen* opinion is a new arena of debate, and this Comment confronts the local remedies rule in a new light. This Comment begins by briefly introducing Chapter Eleven in Part I. In Part II, it proceeds through the factual background and conclusions of the *Loewen* case. Part III discusses two logical flaws of the *Loewen* tribunal's conclusion: first, the limitation of the tribunal's finality requirement to some types of denial of justice claims but not to others is unsustainable; and second, the near perfect overlap in the purpose of the local remedies rule and the tribunal's finality requirement creates a distinction without a difference. Most importantly, it will show that the tribunal incorrectly defined the local remedies rule as a procedural requirement and finality as a substantive requirement. Part IV introduces the debate as to whether Article 1121 waives the local remedies rule and argues that it does in fact waive the rule, whether or not the parties fully understood that effect when they drafted the article.

The terms of Chapter Eleven are unclear regarding whether the NAFTA parties intended to waive the local remedies rule, but the overwhelming view now is that Article 1121 does waive the rule.[9] Without an exhaustion requirement, the NAFTA parties face potential liability from any foreign claimant who is unhappy with the decision of a trial court. If the *Loewen* case is any guide, the United States—and probably the other two NAFTA parties—likely does not want such a result. The NAFTA parties must therefore decide whether they want the rule to apply, and then, what to do about it.

I. NAFTA CHAPTER ELEVEN

NAFTA is a multilateral agreement that creates a free trade zone between Canada, the United States, and Mexico. Chapter Eleven of NAFTA establishes

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[9] *See infra* Part IV.

rules and protections governing foreign investments in the signatory countries, and it allows injured aliens to bring claims directly against foreign governments for violations of those rules.[10] Although several articles of Chapter Eleven are relevant in the *Loewen* decision, particularly important is NAFTA Article 1105, entitled the "Minimum Standard of Treatment" clause. Article 1105 contemplates the existence of an international standard of due process: "Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security."[11] The clause allows an investor who has been subjected to inadequate treatment to bring a claim in a NAFTA tribunal in certain circumstances.

Although there has been some ambiguity about the relationship between Chapter Eleven and preexisting standards of international law, Article 1105 clearly embodies no more than the customary international standards for treatment of aliens, and at least in the judicial context, the international standards for denial of justice.[12] As Part III.A.1 demonstrates, a "denial of

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[10] *E.g.*, NAFTA, *supra* note 1, art. 1115, at 642 ("An investor of a Party may submit to arbitration under this Section a claim that another Party has breached an obligation . . . ."). *See generally* Robert B. Ahdieh, *Between Dialogue and Decree: International Review of National Courts*, 79 N.Y.U. L. REV. 2029 (2004) (describing the nature of Chapter Eleven review of national courts as something greater than judicial dialogue and transnational comity, but lesser than appellate review). The Chapter prescribes, for example, that a member nation must treat foreign investments no less favorably than it would treat domestic investments. NAFTA, *supra* note 1, art. 1102, at 639. It also mandates that a member nation must treat foreign investments no less favorably than it would treat investments of other nations. *Id.* art. 1103, at 639. Finally, member nations may not expropriate the assets of a foreign investor unless for a public purpose, with adequate compensation, and in conformity with international standards of due process. *Id.* art. 1110, at 641–42.

[11] NAFTA, *supra* note 1, art. 1105(1), at 639.

[12] In December 2001, the NAFTA Free Trade Commission ("FTC") published the following interpretation of 1105:

> 1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.
> 2. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.

NAFTA Free Trade Commission, *Notes of Interpretation of Certain Chapter 11 Provisions*, 13 WORLD TRADE & ARB. MATERIALS, Dec. 2001, at 139, 140. There has been some controversy as to whether the FTC interpretation is binding on NAFTA tribunals. Article 1131 allows the FTC to interpret provisions of Chapter Eleven and makes those interpretations binding on the NAFTA parties. NAFTA, *supra* note 1, art. 1131, at 645. The controversy is whether the December 2001 FTC statement is merely an "interpretation," which binds the parties under Article 1131, or an "amendment" or "modification," which would require the approval of the NAFTA parties themselves. *See generally* Guillermo Aguilar Alvarez & William W. Park, *The New Face of Investment Arbitration: NAFTA Chapter 11*, 28 YALE J. INT'L L. 365, 397–98 (2003) (describing the

justice" is any one of a number of acts of a state's judicial system that subjects the state to international responsibility.

Among the most important issues in *Loewen*—and, consequently, in this Comment—is how the local remedies rule should be interpreted in the context of a modern, Chapter Eleven world. The local remedies rule is a standard of international law that requires injured aliens to exhaust all available remedies offered by a host state's domestic system prior to bringing any claim for international responsibility against that state.[13] The issue of the scope of the local remedies rule, both generally and under Chapter Eleven, is timely because the unpredictability and vagueness of Chapter Eleven's standards are not disappearing. For one thing, nearly every nation in the western hemisphere is negotiating over the Free Trade Agreement of the Americas ("FTAA"), which is intended to go into effect in 2005.[14] The Canadian Trade Prime Minister has indicated that Canada will not sign the agreement if it contains anything like Chapter Eleven.[15] Also, the United States is currently trying to form similar agreements with other nations.[16] Furthermore, many of the

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controversy and noting that "no satisfactory way has been found to resolve the potential conflict between . . . Article 2202 and the provisions of Article 1131").

However, one tribunal has held that, consistent with the FTC interpretation, Article 1105 incorporates both historical and current standards of customary international law. *See* Mondev Int'l Ltd. v. United States, ICSID Case No. ARB(AF)/99/2, 42 I.L.M. 85, ¶ 125, at 109 (NAFTA Ch. 11 Arb. Trib. 2003) (stating that NAFTA investors are entitled to treatment under customary international law as interpreted by the parties in the FTC statement).

For several reasons, the details of exactly how those customary standards are used in a NAFTA context are still being ironed out. First, relatively few cases have interpreted and applied Article 1105 since its creation ten years ago, so very little is known about how the article operates as to any particular aspect of denial of justice. *E.g.*, Daniel M. Price, *Some Observations on Chapter Eleven of NAFTA*, 23 HASTINGS INT'L & COMP. L. REV. 421, 424 (2000) ("[T]he circumstances in which a violation of the [Article 1105] standard would be found are fairly narrow, which is why there have been only a handful of cases that have applied the standard."). According to a NAFTA-related website, there have been only forty-one investor-state disputes under NAFTA for which there are public documents available. *See* The Disputes, *at* http://www.naftaclaims.com/disputes.htm (last visited Apr. 17, 2005). Of these, only several are frequently cited for their discussions of the substantive requirements of Article 1105. Second, the subjective standards, and even the definition, of denial of justice have always been subject to debate, even before NAFTA. *See infra* Part III.A.1. Third, as the controversy over the FTC interpretation demonstrates, it was only recently decided that Chapter Eleven should include no more than customary international standards.

[13] *E.g.*, ALWYN V. FREEMAN, THE INTERNATIONAL RESPONSIBILITY OF STATES FOR DENIAL OF JUSTICE 404 (2d ed. 1970).

[14] Shapren, *supra* note 7, at 324.

[15] *Id.* On the other hand, the United States has granted its President far-reaching authority to present the agreement to Congress without the possibility of amendment, so it is important to understand the implications of such a provision if it is included. *Id.* at 324–25.

[16] *See* David A. Gantz, *The Evolution of FTA Investment Provisions: From NAFTA to the United States-Chile Free Trade Agreement*, 19 AM. U. INT'L L. REV. 679, 680–82 (2004) (discussing U.S. agreements with

bilateral investment treaties ("BITs") that exist in the world today have similar provisions and would benefit from a cogent interpretation of the local remedies rule.[17] Because some similar agreements already exist and others are in the works, the international community must settle the meaning and scope of the local remedies rule and Chapter Eleven.

II. THE *LOEWEN* CASE

Loewen presented an opportunity for an international tribunal to determine whether Article 1121 waives the local remedies rule for Chapter Eleven claims. Before it ballooned into an international incident, the *Loewen* case began as a contract dispute between two funeral companies in a Mississippi state court. Loewen[18] was a Canadian corporation with branches all over the United States that had recently expanded into the Mississippi market, where it competed with Jeremiah O'Keefe, a Mississippi businessman who owned several funeral homes. Loewen had agreed to sell an insurance company and a related trust fund to O'Keefe and to provide O'Keefe with the exclusive right to provide certain insurance policies sold through Loewen funeral homes.[19] In exchange, O'Keefe had agreed to sell two funeral homes and to assign to Loewen an option to buy a cemetery tract.[20] Later, O'Keefe sued Loewen for breach of contract, fraud, and antitrust violations, seeking actual damages of $5 million.[21] Although the underlying dispute involved only $5 million in actual damages, the court awarded an astonishing $500 million in damages to O'Keefe after a jury trial.[22]

Chile and Singapore that contain elements similar to Chapter Eleven); Denise Manning-Cabrol, *The Imminent Death of the Calvo Clause and the Rebirth of the Calvo Principle: Equality of Foreign and National Investors*, 26 LAW & POL'Y INT'L BUS. 1169, 1191 (1995) (discussing pending negotiations between the United States and Bolivia, Colombia, Uruguay, and Venezuela).

[17] *See* Manning-Cabrol, *supra* note 16, at 1197–98 (citing survey revealing that only twenty-eight of the world's 335 BITs do not contain a fair and equitable treatment provision). For an example of a BIT, see J. Steven Jarreau, *Anatomy of a BIT: The United States-Honduras Bilateral Investment Treaty*, 35 U. MIAMI INTER-AM. L. REV. 429 (2004).

[18] The claimants (defendants) were The Loewen Group, Inc., The Loewen Group International, Inc., and Raymond L. Loewen. This paper will identify the claimants collectively as "Loewen," and Raymond Loewen as "Raymond Loewen" or "Mr. Loewen."

[19] The Loewen Group, Inc. v. United States, ICSID Case No. ARB(AF)/98/3, 42 I.L.M. 811, ¶ 30, at 815 (NAFTA Ch. 11 Arb. Trib. 2003).

[20] *Id.*

[21] *Id.* ¶ 37, at 816.

[22] *Id.* ¶ 4, at 812.

Loewen brought its NAFTA claim after the conclusion of the trial, several unsuccessful attempts to remedy its complaints in Mississippi courts, and ultimately, a settlement agreement with O'Keefe. The tribunal summarized Loewen's relevant claim as follows:

> [T]he trial court, by the way in which it conducted the trial, in particular by its conduct of the *voir dire* and its irregular reformation of the initial jury verdict for $260,000,000, by permitting extensive nationality-based, racial and class-based testimony and counsel comments, violated Article 1105 of NAFTA . . . the excessive verdict and judgment (even apart from the discrimination) violated Article 1105 . . . [and] the Mississippi courts' arbitrary application of the bonding requirement violated Article 1105 . . . .[23]

The following discussion will address, first, the alleged improprieties that took place in the trial, and second, the reasons that Loewen's Chapter Eleven claims failed.

A. *The Trial*

The trial was filled with "extensive irrelevant and highly prejudicial" remarks that tended to prejudice the jury against Loewen[24] to such a degree that the NAFTA tribunal deemed the trial "so flawed that it constituted a miscarriage of justice."[25] The trial judge allowed references to Raymond Loewen's Canadian nationality, which was contrasted with O'Keefe's local Mississippi roots.[26] The judge also allowed repeated racial references to be used against Loewen. For example, O'Keefe's attorney stated that Loewen did business exclusively with white people and had exploited the National Baptist Convention, many of whose members were African American. The judge allowed the introduction of class-based distinctions between Loewen, portrayed as a large, wealthy corporation, and O'Keefe, a family-owned Mississippi business. Furthermore, the trial judge refused to give a jury instruction proposed by Loewen to the effect that the jury was "not to be swayed by bias, prejudice, favour or other improper motive."[27]

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[23] *Id.* ¶ 39, at 816.

[24] *Id.* ¶ 4, at 812.

[25] *Id.* ¶ 54, at 819.

[26] For example, O'Keefe's attorney portrayed Mr. Loewen as a foreign invader who had descended on the state of Mississippi, while depicting O'Keefe as a war hero. O'Keefe's attorneys described the American jury system as one that O'Keefe had "fought for and some died for." *Id.* ¶ 61, at 821.

[27] *Id.* ¶ 82, at 824. The preceding list, with its artificial categories, inadequately expresses the extent of the trial's problems:

Also, the damage award against Loewen was unusually high, and the court allowed an assessment of punitive damages that violated Mississippi's bifurcated trial procedure.[28] Although in Mississippi the jury is not allowed to consider punitive damages during the first phase of the trial, O'Keefe's attorneys referred to punitive damages both during voir dire and throughout the trial.[29] The jury returned a verdict of $260 million, $160 million of which was later revealed to have been for punitive damages.[30] The judge threw out the $160 million, and at the punitive damages hearing the jury returned a verdict for $400 million. Thus, the judge entered a total verdict of $500 million.[31] The judge denied Loewen's subsequent motion to reduce the punitive damages, which was based on the ground that they resulted from bias, passion, and prejudice.[32]

Furthermore, the court rigidly refused to waive a bond requirement prior to appeal. Under Mississippi law, a party seeking an appeal must post a bond worth 125% of the judgment to stay execution of the judgment pending the appeal.[33] Loewen was unable to procure the required amount.[34] The law

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> When the trial is viewed as a whole . . . the O'Keefe case was presented by counsel against an appeal to home-town sentiment, favouring the local party against an outsider. To that appeal was added the element of the powerful foreign multi-national corporation seeking to crush the small independent competitor who had fought for his country in World War II.

Id. ¶ 70, at 823.

28 *Id.* ¶¶ 88–96, at 825–27.

29 *Id.* ¶¶ 88, 90, at 825–26.

30 In a note to the judge, the jury foreman admitted that $160 million of the judgment was for punitive damages and $100 million was for compensatory damages. *Id.* ¶ 94, at 826. The NAFTA tribunal considered this "a failure adequately to instruct the jury to limit their initial award to compensatory damages." *Id.* ¶¶ 94–95, at 826.

31 *Id.* ¶ 101, at 827. The tribunal wrote, "[T]he total award (even the award of compensatory damages) appears to be grossly disproportionate to the damage suffered by O'Keefe." *Id.* ¶ 113, at 829. For a rundown of the court's calculations, see *id.* ¶¶ 97–114, at 827–29.

32 *Id.* ¶¶ 102–03, at 827. According to Lucien Dhooge, the tribunal should have held that the punitive damages award constituted an uncompensated expropriation under NAFTA Article 1110 and under United States, Canadian, and international standards regarding expropriation and punitive damages. Lucien J. Dhooge, The Loewen Group v. United States*: Punitive Damages and the Foreign Investment Provisions of the North American Free Trade Agreement*, 19 CONN. J. INT'L L. 495, 569–70 (2004). Thus, the United States should have been liable for the fair market value of Loewen's expropriated investment immediately before the entry of the punitive damages award in Mississippi. *Id.* at 570.

33 MISS. R. APP. P. 8(a).

34 Here, the required bond was $625 million, posted within seven days. Notice of Arbitration/Statement of Claim, R. Loewen and Loewen Corp. ¶ 126, at 45, *Loewen*, ICSID Case No. ARB(AF)/98/3 (1998). Of course, according to the United States, Loewen's inability to pay the bond was Loewen's own doing. According to the United States,

allows the judge discretion to reduce the amount of the bond if the appealing party can show good cause, and Loewen filed a motion requesting reduction, but the judge denied the motion. The judge also denied Loewen's motions for judgment notwithstanding the verdict, a new trial, remittitur, and reduction of the compensatory and punitive damages awards.

Upon conclusion of the trial, Loewen made several unsuccessful attempts to resolve its claim within the Mississippi judicial system. On November 27, 1995, one week after the trial judge refused to lower the bond amount, Loewen appealed the bond requirement to the Mississippi Supreme Court.[35] The next day, Loewen filed a motion, which the judge dismissed, asking the trial court to stay enforcement of the judgment and offering to post a $125 million bond.[36] On November 30, the Mississippi Supreme Court granted an interim stay of execution conditioned on the posting of a $125 million bond, and, on December 20, it extended the stay indefinitely. On January 24, 1996, however, it denied Loewen's motion and ended the stay completely. O'Keefe's attorneys sent a settlement offer the next day, and the parties settled on February 1. The Mississippi Supreme Court immediately dismissed Loewen's appeal with prejudice.

B. The NAFTA Tribunal's Award of July 2003

The *Loewen* tribunal engaged in an extended discussion of Article 1105 and concluded that, by allowing the alleged misdeeds of O'Keefe's counsel

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> . . . Loewen's business model of "growth through acquisitions," funded with proceeds of sales of debt and equity, was well-known to be an exceptionally high-risk venture that threatened the company's collapse upon the occurrence of any number of unknown contingencies, not limited to an adverse jury award. A 1992 article about Loewen concisely described the problem:
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> > It's a circle game. Acquisitions feed earnings, which in turn pump the P/E ratio. And with the high P/E, they can keep selling stock to make more acquisitions. But as soon as one part weakens, the whole thing collapses.
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> Loewen's alleged inability to post the full bond was attributed solely to the highly-leveraged position of the company that was the result of Loewen's aggressive growth strategy. Even Loewen's own counsel in this proceeding has acknowledged that "of course . . . Loewen was over-leveraged and wanted to be more and more leveraged. He was borrowing a great deal."

Counter-Memorial of the United States of America 97, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001) (internal citations omitted). Therefore, the United States argued, Loewen should not complain that it was coerced into the settlement.

35 *Loewen*, 42 I.L.M. ¶ 179, at 840.

36 *Id.* ¶ 180, 183, at 840–41. The judge's decision was based on a concern with providing absolute security to the judgment in the face of suggestions that other lawsuits were pending against Loewen, that the value of Loewen's stock was plummeting, and that Loewen might file for bankruptcy. *Id.* ¶ 183, at 840.

and the excessive jury award, the trial court substantively violated Article 1105.[37] However, despite the egregiousness of the conduct at issue, the tribunal dismissed Loewen's case for two reasons: first, the Loewen corporate entity was no longer Canadian, so the tribunal had no jurisdiction under NAFTA; and second, Loewen had failed to satisfy a finality requirement by exhausting all available local remedies. Therefore, the discussion of the substantive standards of Article 1105 was merely dicta.

1. Loewen's Nationality

Loewen's claim failed because of a threshold jurisdictional issue. In order to file a claim against the United States under Chapter Eleven, an investor must be Canadian or Mexican.[38] Although Loewen was Canadian at the outset of the case, it had reorganized as a U.S. corporation before the final disposition and assigned its NAFTA claim to a Canadian corporation, Nafcanco, which Loewen had created solely to continue the claim. The tribunal held that Loewen, now an American company, was the real party in interest, and that NAFTA requires continuous nationality throughout an entire proceeding.[39] Therefore, Loewen's claim failed because Loewen had become a U.S. corporation.[40]

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[37] *See id.* ¶ 54, at 819 ("[W]e have reached the firm conclusion that the conduct of the trial . . . constituted a miscarriage of justice amounting to a manifest injustice as that expression is understood in international law. Whether this conclusion results in a violation of Article 1105 depends upon the resolution of . . . [whether] State responsibility arises only when final action is taken . . . ."). Additionally, as a point of interest, the requirement of the $625 million bond as a prerequisite to an appeal and the trial judge and appellate court's refusal to lower it would not have amounted to a denial of justice: "[T]here is no principle of international law which requires a State to provide a right of appeal," and the refusal to lower the amount was "at worst an erroneous or mistaken decision." *Id.* ¶¶ 188–89, at 841.

[38] As stated by the *Loewen* tribunal,

> The format of NAFTA is clearly intended to protect the investors of one Contracting Party against unfair practices occurring in one of the other Contracting Parties. It was not intended to and could not affect the rights of American investors in relation to practices of the United States that adversely affect such American investors.

Id. ¶ 223, at 846 (referring to NAFTA Articles 1116–1117).

[39] For an argument that the "so-called continuous-nationality rule" should not be viewed as a binding rule of customary international law or as a "rule" at all, see Matthew S. Duchesne, *The Continuous-Nationality-of-Claims Principle: Its Historical Development and Current Relevance to Investor-State Investment Disputes*, 36 GEO. WASH. INT'L L. REV. 783 (2004).

[40] *See Loewen*, 42 I.L.M. ¶¶ 220–39, at 846–50.

2. *The Finality Requirement and the Article 1121 Waiver Issue*

However, the tribunal made it clear that Loewen's claim also failed due to Loewen's failure to satisfy a finality requirement.[41] Although the tribunal's decision that the trial would have constituted a substantive violation of Article 1105 was dicta, the tribunal left it unclear whether its discussion of finality and the local remedies rule was also dicta. The tribunal has since clarified its position: Loewen's failure to satisfy the finality requirement was not dicta but was instead an alternate ground for the decision.[42]

In a brief filed on February 15, 2000, the United States argued that the tribunal lacked jurisdiction over Loewen's claims because the Mississippi trial court's decision was not a final act of the relevant judicial system and, therefore, could not be attributed to the United States.[43] In a preliminary decision, the tribunal responded by suggesting that the finality requirement "is no different from the local remedies rule,"[44] but the tribunal explicitly deferred on the issue of whether NAFTA Article 1121(2)(b) waived the local remedies rule.

The United States disagreed with the tribunal's initial characterization.[45] First, it argued that the local remedies rule only deals with the admissibility of claims, not the merits of those claims.[46] Exhaustion in a denial of justice claim is a substantive requirement of state responsibility rather than a procedural one. Since a lower court decision does not amount to an unlawful act of a state, it creates no international responsibility.[47] Second, the United States argued that Article 1121 does not waive the local remedies rule in the context of denial of justice; instead, it simply requires claimants to waive certain rights in order to

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41 *See id.* ¶ 217, at 846.

42 *See generally* Decision on Respondent's Request for a Supplementary Decision, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2004), *available at* http://www.international-economic-law.org/Loewen/Loewen%20-%20Decision%20on%20Request%20for%20Reconsideration.pdf.

43 *See generally* Memorial of the United States of America on Matters of Competence and Jurisdiction 49–85, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2000).

44 Decision on Hearing of Respondent's Objection to Competence and Jurisdiction ¶ 71, at 20, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001).

45 For two statements of the strongest arguments for the United States, see Opinion of Christopher Greenwood, Appendix to Counter-Memorial of the United States of America, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001); Opinion of Richard B. Bilder, Appendix to Counter-Memorial of the United States of America, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001).

46 Rejoinder of the United States of America 88–89, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001).

47 *Id.*; *see* Counter-Memorial of the United States of America 108–09, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001).

pursue other proceedings, in court or otherwise.[48] Its primary purpose, therefore, is not to benefit the claimant but to prevent state parties from having to answer claims in two courts at once. Also, the United States argued that to allow a claim to succeed in an international court would be absurd because it would allow claimants to use a NAFTA tribunal as an international court of appeal.[49]

Loewen, on the other hand, argued that it was not required to appeal the trial decision. First, it argued that the unqualified language of Article 1121 waived the local remedies rule.[50] Second, it argued that international law recognizes no difference between the finality and exhaustion requirements, and that the United States cited no authority supporting its argument that there was such a difference.[51] Third, it argued that exhaustion is procedural in most cases, and since the rule is procedural, it is waivable.[52]

In its July 2003 decision on the merits, the tribunal accepted the United States' arguments and held that the finality requirement is distinct from the local remedies rule. According to the tribunal, the local remedies rule is procedural and requires a party "to exhaust the local remedies in that State before the party can raise the complaint at the level of international law."[53] The finality requirement, on the other hand, is substantive: Finality of the judicial decision is an "essential condition of a State being held responsible for a judicial decision."[54] Thus, the tribunal stated that the local remedies rule and the finality requirement serve distinct purposes: The local remedies rule ensures that the alleged offending state has an opportunity to redress its own mistake, and finality ensures that the state is responsible.[55]

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[48] Counter-Memorial of the United States of America 111, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001).

[49] *See id.* at 112–13.

[50] *See* Final Submission of The Loewen Group, Inc. Concerning the Jurisdictional Objections of the United States ¶¶ 36–37, at 17–18, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2000).

[51] *Id.* ¶¶ 38–41, at 18–20.

[52] *Id.* ¶¶ 42–45, at 20–22. Although the *Loewen* tribunal agreed with convention and with Loewen that the local remedies rule is procedural, the tribunal improperly distinguished the local remedies rule from finality. Under the tribunal's formulation, the traditional local remedies rule is procedural, and the finality requirement is substantive. But the tribunal used an unduly narrow definition of the local remedies rule that excludes finality. As this Comment argues, because finality is merely a form of the local remedies rule, the procedure versus substance dichotomy is incorrect. *See infra* Part III.B.2.

[53] *Loewen* , 42 I.L.M. 811, ¶ 149, at 835 (2003).

[54] *Id.* ¶ 153, at 836.

[55] *See id.* ¶ 159, at 837. The tribunal bases the purported difference on the fact that the State is not held internationally responsible until the finality requirement is fulfilled: "[T]hat a decision of a lower court be challenged through the judicial process before the State is responsible for a breach of international law . . .

Further, the tribunal did not go so far as to rule upon whether Article 1121 waived the local remedies rule. However, it did decide that because Article 1121 did not expressly waive the distinct, substantive finality requirement for acts of the judiciary, the judicial process must continue to the highest level, even if the parties waived the local remedies rule.[56] Therefore, the tribunal held that because the finality requirement and the local remedies rule are distinct ideas, even if Article 1121 waived the local remedies rule, it did not waive the finality requirement.

Confusingly, however, after distinguishing finality from the local remedies rule, the tribunal continued referring to finality as part of "the obligation to pursue local remedies."[57] On several occasions, the tribunal mentioned "exhaustion" and "local remedies" when referring to Loewen's failure to appeal. For example, directly after making the distinction, the tribunal mentioned the finality requirement as "the duty to pursue local remedies in its application to a breach of international law constituted by a judicial act."[58] Likewise, in a section entitled "Did Loewen Pursue Available Local Remedies," the tribunal stated that "the next question is whether the appeal to the Mississippi Supreme Court was an available remedy that Loewen should have pursued."[59] The tribunal then concluded "that Loewen failed to pursue its domestic remedies . . . and that, in consequence, Loewen has not shown a violation of . . . NAFTA."[60]

According to the tribunal, Loewen did not satisfy the finality requirement because it had other domestic options besides agreeing to settle its claim. The tribunal mentioned three possibilities: Loewen could have pursued its appeal despite the risk of execution on its assets; Loewen could have filed for bankruptcy under Chapter Eleven of the Bankruptcy Code, which would have resulted in a stay of the judgment; or Loewen could have filed a petition for certiorari to the U.S. Supreme Court.[61] The tribunal rejected the first possibility because of the threat of immediate execution by O'Keefe. However, Loewen failed to show why it settled its claim rather than pursuing

means that this requirement and the local remedies rule, though they may be similar in content, serve two different purposes." *Id.*

[56] *Id.* ¶¶ 163–64, at 838.

[57] *Id.* ¶ 165, at 838.

[58] *Id.*

[59] *Id.* ¶ 207, at 844.

[60] *Id.* ¶ 217, at 846.

[61] *Id.* ¶¶ 207–10, at 844–45.

the other two options.[62] According to the panel, Loewen's settlement with O'Keefe reflected a business decision not to pursue local remedies.[63]

III. THE LOCAL REMEDIES RULE VERSUS FINALITY IN DENIAL OF JUSTICE CLAIMS: THE ERRORS OF THE *LOEWEN* DECISION

Before a party can bring an international claim against a state, the party must first satisfy the local remedies rule. One statement of the rule is as follows:

> No international claim for indemnity may be presented on behalf of an aggrieved national as long as there remains . . . *effective means for obtaining reparation* in the State in which the wrong was committed . . . . [A] complaint based upon denial of justice or any other wrong to an alien will be rejected . . . where it appears that *the claimant has failed to exhaust his local remedies*.[64]

Thus, only after the injured party has sought remedies in the domestic system to the extent that there remain no "effective means for obtaining reparation" can the party turn to international measures against the state. In most cases, the local remedies rule is merely a procedural requirement that must be fulfilled before bringing the claim, and it forms no element of the wrongful act.[65]

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[62] *See id.* ¶¶ 217, at 846. However, Loewen later reopened the issue by claiming that there was evidence before the tribunal that Loewen did consider those other options. Article 58 Submissions as to Raymond L. Loewen's Article 1116 Claim ¶¶ 17–30, at 5–9, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2003); *see also* Lerner, *supra* note 7, at 268–74 (arguing that these suggested remedies would have most likely been unsuccessful). But the tribunal later held that all issues had been dealt with in the final decision on the merits. Decision on Respondent's Request for a Supplementary Decision, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2004), *available at* http://www.international-economic-law.org/Loewen/Loewen%20-%20Decision%20on%20Request%20for%20Reconsideration.pdf.

[63] *Loewen*, 42 I.L.M. ¶ 213, at 845.

[64] FREEMAN, *supra* note 13, at 404 (emphasis in original).

[65] *E.g.*, International Law Commission, *Draft Articles on Responsibility of States for Internationally Wrongful Acts*, art. 44(a)(2) (Nov. 2001), *available at* http://www.un.org/law/ilc/texts/State_responsibility/responsibility_articles(e).pdf (stating that a claim is not admissible if "[t]he claim is one to which the rule of exhaustion of local remedies applies and any available and effective local remedy has not been exhausted"); Béla Vitányi, *International Responsibility of States for Their Administration of Justice*, 22 NETH. INT'L L. REV. 131, 161 (1975) ("[*T*]*he unsuccessful exhaustion of local remedies is not a condition under substantive law for the creation of the international responsibility of the State concerned, but a condition to exercise the international right of diplomatic protection* . . . .") (emphasis in original). The state alleging non-exhaustion has the burden of proof of non-exhaustion, after which the burden shifts to the claimant to prove that an exception applies. *See* Juan Carlos Bayarri v. Argentina, Case 11.280, Report No. 2/01, OEA/Ser.L/V/II.111 Doc. 20 rev. ¶ 30, at 75 (2000), *available at* http://wwwserver.law.wits.ac.za/humanrts/cases/2-01.html ("If the State alleging the failure to exhaust local remedies proves that there are domestic remedies that should have

The *Loewen* tribunal conceived a finality requirement that was separate from the local remedies rule. The tribunal's argument is strongly stated as follows: A state is obligated to provide a fair and efficient "system" of justice, so there is no international violation until the entire system fails. An unjust trial court decision does not represent the failure of the entire system. Thus, a final decision by the state's entire system is needed to show that there has been a substantive violation.[66] Also, the tribunal noted that in no case of which it was aware had a state been held internationally liable for the error of a trial court when there remained an opportunity to appeal.[67]

The United States pointed to only one case in the modern era in which a tribunal discussed the requirement to appeal—albeit indirectly—despite an explicit waiver of the local remedies rule.[68] In *Oil Field of Texas*, the Iran-U.S. Claims Tribunal wrote the following: "In these circumstances, *and taking into account the Claimant's impossibility to challenge the Court order in Iran*, there was a taking . . . for which the Government is responsible."[69] The United States argued that because the Iran-U.S. Claims Tribunal still took into account the inability of the claimant to appeal despite an explicit waiver of the local remedies rule, the tribunal must have been referring to and acknowledging a finality requirement separate from the local remedies rule. However, the tribunal in that case did not go as far as the *Loewen* tribunal to state explicitly that finality is a separate requirement. In fact, with that language, *Oil Field of Texas* simply noted that there was no possibility of further appeal and that the international case could proceed. The United States also cited several sources to support its assertion that the requirement to appeal is substantive because a state is not liable until the highest court speaks.[70] As a whole, these cases all

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been used, the petitioners will have to show that those remedies were exhausted or that one of the exceptions . . . obtains.").

[66] *See Loewen*, 42 I.L.M. ¶¶ 149–56, at 835–37.

[67] *Id.* ¶ 154, at 836.

[68] Other than the case discussed in this paragraph, the United States pointed to several cases that are now more than a century old. *See* Opinion of Christopher Greenwood ¶ 33, at 16, Appendix to Counter-Memorial of the United States of America, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001). Those cases came generally from a time before it was even settled that the local remedies rule was procedural. *See infra* Part III. International law has changed dramatically since then. *See, e.g.*, *infra* Part III.A.1.

[69] Opinion of Christopher Greenwood ¶ 32, at 16, Appendix to Counter-Memorial of the United States of America, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001) (quoting *Oil Field of Texas*, 12 Iran-U.S. CTR 308, 319).

[70] *See, e.g.*, Opinion of Richard B. Bilder ¶ 41, at 33–34, Appendix to Counter-Memorial of the United States of America, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001). However, those sources are not helpful because the same would be true whether the requirement to appeal was procedural or substantive. In either case, the state has a chance to fix the wrong it has caused through the action of its lower courts.

support the United States' argument—adopted by the tribunal—that an international claimant must appeal adverse court decisions before bringing an international claim. This Comment does not dispute that statement; rather, this Comment argues that the requirement to appeal is, and always has been, a part of the local remedies rule.

With the exception of those few cases cited by the United States, finality has not previously, at least in the most recent era of international law, been discussed in this light. The requirement of a final court judgment is usually discussed as a part of the local remedies rule, not as a separate substantive requirement. Thus, by holding that in the presence of a waiver of the local remedies rule, a separate, substantive finality requirement still requires appeal to a state's highest court, the *Loewen* tribunal broke new ground in the area of denial of justice. Unfortunately, in doing so, it erred in several ways. Aside from the tribunal's confusing language noted above, the tribunal's opinion suffers two major flaws. First, it creates a finality requirement that seems to apply only to denial of justice claims in which the original wrong occurs within the courts (which this Comment will call "primary denial of justice") and not to denial of justice claims that originate from wrongs that occur outside the courts (which will be called "secondary denial of justice"). Second, it claims that the finality requirement and the local remedies rule serve different purposes, the local remedies rule a procedural purpose and the finality requirement a substantive purpose. The following discussion takes each of these two problems in turn and shows that both distinctions are unwarranted under modern understandings of denial of justice. Then, the discussion summarizes a more logical understanding of the law.

A. *Finality and the Modern Definition of Denial of Justice*

The *Loewen* tribunal's first error is that the terms of the opinion strongly imply that the finality requirement applies only to "primary denial of justice" claims, those in which the international wrong occurs as an unjust decision of the judicial system itself.[71] This means that there is no finality requirement for "secondary denial of justice" claims, those in which the wrong occurs outside the judicial system but for which the judicial system provides no effective remedy. However, under a modern definition of denial of justice, there is no theoretical distinction between the two types of claims. The following discussion will first provide a definition of the "denial of justice" concept and

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[71] *See infra* Part III.A.2.

demonstrate that there should be no special rules for some denial of justice claims that do not apply equally to other denial of justice claims. Then, it will illuminate the specific errors of the *Loewen* tribunal.

1. The Modern Definition of "Denial of Justice"

As a preliminary matter, "state responsibility" arises when a state is charged with committing an internationally wrongful act.[72] It is a broad concept that simply refers to any violation of international law, whether from a breach of the terms of a treaty or of customary international law, for which a state can be held liable. The local remedies rule applies to all allegations of internationally wrongful acts.[73] A denial of justice is one example of a wrongful act that triggers state responsibility. In general, denial of justice refers to certain violations associated with a state's judicial system: "A denial of justice . . . [is] any defect in the organization of courts or in the exercise of justice which entails a violation of the international legal duties of States with respect to the judicial protection of aliens."[74] But beyond the notion that denial of justice involves courts, the breadth of the doctrine has always been the subject of debate.

International law now recognizes that the term "denial of justice" covers a broad variety of situations, which can be placed into two major categories. First, a denial of justice claim can be based on the classic conception of the inability or unwillingness of courts to adequately remedy an antecedent wrong that occurred outside the judiciary, also known as a "secondary denial of justice" claim.[75] In these cases, a denial of justice occurs when a court denies a foreign claimant a procedural right—including acts such as denial,

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[72] *E.g.*, International Law Commission, *supra* note 65, at art. 1 ("Every internationally wrongful act of a State entails the international responsibility of that State."); Louis B. Sohn & R.R. Baxter, *Responsibility of States for Injuries to the Economic Interests of Aliens*, 55 AM. J. INT'L L. 545, 548 (1961) (proposing Draft Convention on the International Responsibility of States for Injuries to Aliens) ("A State is internationally responsible for an act or omission which, under international law, is wrongful, is attributable to that State, and causes an injury to an alien.").

[73] *See, e.g.*, Sohn & Baxter, *supra* note 72, art. 1(2)(a), at 548 ("An alien is entitled to present an international claim under this Convention only after he has exhausted the local remedies provided by the State against which the claim is made.").

[74] 1 ENCYCLOPEDIA OF PUBLIC INTERNATIONAL LAW 1007, 1007 (1992).

[75] *See, e.g.*, Clyde Eagleton, *Denial of Justice in International Law*, 22 AM. J. INT'L L. 538, 542 (1928). As this Comment notes, the original, antecedent conduct could be a wrongful act of another branch of the state—such as the president—or a wrongful act of an individual, nonstate actor. This difference is not important to the immediate discussion, but it will become important later in the discussion of the substantive or procedural nature of the local remedies rule. *See infra* Part III.B.2.

unwarranted delay, or obstruction of access to the courts; deficiency in the administration of justice; or failure to provide guarantees of proper administration of justice—after the claimant is injured by some actor outside the court itself, whether an individual or another branch of the state.[76] Second, and more broadly, denial of justice can be based on a conception of denial of justice in which, as in *Loewen* itself, a lower court's decision constitutes both the original wrong and the denial of justice, which are called "primary denial of justice" claims. A modern definition of denial of justice includes both types of claims.[77]

But this modern definition was not always accepted in the international community. Historically, debates over the breadth of the concept have tended to center around three main elements: whether denial of justice includes only the wrongs of courts (narrower) or also includes any wrong of the state (broader);[78] whether it includes only wrongs that occurred initially outside the courts (narrower) or also includes wrongs that originated within the courts (broader);[79] and whether it includes only denial of access to the courts (narrower) or also includes other violations perpetrated by courts (broader).[80] For example, the narrowest possible conception of denial of justice would include only actions of the courts, only a court's failure to remedy wrongs that occurred outside the courts (secondary claims), and only the court's failure to provide access. The broadest possible conception would include practically any wrong of any branch of the state, and if within the courts, any violation of rights in the courts, whether it was the failure to correct some original wrong in some other branch of government or within the courts themselves.

States have disagreed on the breadth of the doctrine because different groups of states tried to protect different interests. So-called "creditor" or "plaintiff" states are those "whose institutions are strong and whose courts [are] relatively impartial, who lend money to other countries for their development and whose nationals are accustomed to carry[ing] on business abroad." So-called "debtor" or "defendant" states, on the other hand, are those

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[76] *See, e.g.*, Vitányi, *supra* note 65, at 149.

[77] *See, e.g.*, Edwin M. Borchard, *The Law of Responsibility of States for Damage Done in Their Territory to the Person or Property of Foreigners*, 23 AM. J. INT'L L. SPECIAL NO. 131, art. 9, at 134 (1929) (noting that the term "denial of justice" includes procedural wrongs as well as "manifestly unjust judgments" of courts).

[78] *See, e.g.*, Eagleton, *supra* note 75, at 540. Today, no one denies that a denial of justice involves the courts. *See supra* note 74 and accompanying text.

[79] *See, e.g.*, G.G. Fitzmaurice, *The Meaning of the Term "Denial of Justice"*, 13 BRIT. Y.B. INT'L L. 93, 98–102 (1932).

[80] *See, e.g.*, Eagleton, *supra* note 75, at 539–40.

"whose independence and civilization are relatively recent, whose institutions are often weak and whose courts are not infrequently under the control of the executive or at the service of purely national interests."[81] Because at one time it became common for people to believe that a denial of justice was the only basis for international responsibility, creditor states wanted to give the term as broad a meaning as possible, and debtor states wanted to give the term as narrow a meaning as possible.[82] Of course, neither the broadest nor the narrowest view has been accepted.[83]

Scholars have advanced several positions regarding where between the two extremes the definition of denial of justice lies, some tending toward the narrower view but most tending toward the broader view. Professor Clyde Eagleton, for example, tended toward the narrow, traditional extreme. He argued that denial of justice refers exclusively to inadequate judicial redress for an antecedent wrong (secondary claims).[84] He also argued that the antecedent injury for which the alien seeks redress in the courts must always be negative in character—an omission or negligence, but never a positive act—and that the alien must be the plaintiff in the attempt to obtain a judicial remedy.[85] Eagleton's definition of denial of justice did not include primary denial of justice, and even in secondary cases the term would not apply where a *defendant* was denied any rights in court.

In contrast, Professor Fitzmaurice, writing only a few years later, expressed a more expansive view of the types of acts that constitute denial of justice.

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[81] Fitzmaurice, *supra* note 79, at 93.

[82] *See id*. at 93–94. Thus, the former, particularly the United States, tended to advocate the broad view. With the advent of Chapter Eleven, however, traditional creditor states are now subject to the same possible treatment as debtor states. Not surprisingly, the United States supports strong investment provisions when it is in the creditor position, but not when it is in the debtor position. For an interesting discussion of the double standard, see Alvarez & Park, *supra* note 12.

[83] The broadest view has not been accepted because, if denial of justice were broad enough to encompass any act of international responsibility, there would be no need for a concept called "denial of justice" separate from "internationally wrongful act." The narrowest view, which would include only denial of access to the courts, has not been accepted either. *See, e.g.*, Lerner, *supra* note 7, at 250–51 (noting that, instead, an "intermediate" view has been adopted, which encompasses procedural and substantive wrongdoings by courts). As Professor J.L. Brierly observed, "There are many possible ways in which a court may fall below the standard fairly to be demanded of a civilized state without literally closing its doors . . . [such as] corruption, threats, unwarrantable delay, flagrant abuse of judicial procedure, [or] a judgment dictated by the executive." J.L. BRIERLY, THE LAW OF NATIONS: AN INTRODUCTION TO THE INTERNATIONAL LAW OF PEACE 227 (5th ed. 1955).

[84] *See* Eagleton, *supra* note 75, at 542.

[85] *Id*. at 559. Arguably, these additional restrictions make Eagleton's definition narrower in some respects than the narrow extreme discussed above.

According to Fitzmaurice, denial of justice should not be reserved for failure to redress a prior wrong. He used the example of an individual executed without trial, which would be an original wrong by a state but without judicial failure. It is artificial, he wrote, to say "that such an act constitutes an original *in*justice and not a (or an original) *denial* of justice."[86] Also, unlike Eagleton's definition, in Fitzmaurice's definition, an original wrong that occurs in a court can constitute denial of justice, and the aggrieved foreigner need not have been a plaintiff. Fitzmaurice illustrated this idea with a simple example in which *A* sues *B*, a foreigner. The trial court properly rules for *B*. *A* appeals, and the appeals court affirms the judgment. *A* appeals to the highest court, which reverses based on some anti-foreign bias. This situation would constitute a denial of justice from an original wrong in the court that was not a failure to redress a previous wrong.[87] Similarly, Fitzmaurice argued, an unjust judicial decision by itself can constitute a denial of justice, but only if the court was guilty of bias, fraud, dishonesty, or the like.[88]

Fitzmaurice was neither the first nor the only person to advocate the idea that denial of justice could be predicated on an original wrong in a national court, a primary claim. The 1929 Harvard Law School *Draft Convention on Responsibility of States for Damage Done in Their Territory to the Person or Property of Foreigners* defined denial of justice to include not only obstruction of access to courts but also an error of a court that produces manifest injustice.[89] Another scholar wrote in the same year that "[t]he present tendency of juristic opinion appears to disregard the distinction between acts of the legislative, executive, and judicial authorities and to attribute responsibility to the state for all injuries suffered by aliens in violation of international law."[90] Under those circumstances, it makes little sense to exclude even a jury verdict from the definition.[91]

Subsequent developments have more or less adopted the broader Fitzmaurice view. Modern international law recognizes that a denial of justice

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86 Fitzmaurice, *supra* note 79, at 106 (emphasis in original). Another example would be the permanent obstruction from the courts of a married couple (at least one of whom was foreign) trying to get a divorce, which would constitute a denial of justice even though the litigants are not redressing a prior wrong.

87 *Id.* at 108.

88 *Id.* at 112.

89 Borchard, *supra* note 77, art. 9, at 134. However, a judgment of a national court that does not produce "manifest injustice" is not a denial of justice.

90 J.W. Garner, *International Responsibility of States for Judgments of Courts and Verdicts of Juries Amounting to Denial of Justice*, 10 BRIT. Y.B. INT'L L. 181, 184 (1929).

91 *Id.* at 185.

claim can be predicated on an original wrong that occurs within the judiciary, regardless of the procedural posture of the foreign claimant. For example, under the 1961 Harvard Law School *Draft Convention on the International Responsibility of States for Injuries to Aliens*,

> [a] decision or a judgment of a tribunal or an administrative authority . . . involving the determination of the civil rights or obligations of an alien or of any criminal charges against him, and either denying him recovery . . . or granting recovery against him or imposing a penalty, whether civil or criminal, upon him is wrongful:
>
> (a) if it is a clear and discriminatory violation of the law of the State concerned;
> (b) if it unreasonably departs from the principles of justice recognized by the principal legal systems of the world; or
> (c) if it otherwise involves a violation by the State of a treaty.[92]

In other words, the drafters' interpretation of customary international law was that a state is responsible not only for denial of access to a tribunal[93] and denial of a fair hearing[94] but also for discriminatory treatment in court. Thus, the drafters recognized that the concept of denial of justice covers both primary and secondary cases. As some scholars have put it, denial of justice under the modern definition can be either *procedural*, such as denial of access to tribunals, undue delay, or detention without a hearing, or *substantive*, such as an unjust court judgment, even absent any procedural irregularities.[95]

Furthermore, the *Loewen* case demonstrates that the NAFTA parties, and the *Loewen* tribunal itself, have adopted this broader, more modern definition of denial of justice. Loewen's claim was a primary denial of justice claim based on an original wrong within the Mississippi courts. In the *Loewen*

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[92] Sohn & Baxter, *supra* note 72, art. 8, at 550–51. In fact, the United States has long endorsed the view that denials of justice include manifestly unjust court decisions. Lerner, *supra* note 7, at 262.

[93] Sohn & Baxter, *supra* note 72, art. 6, at 550.

[94] *Id*. art. 7, at 550.

[95] *See generally* A.O. Adede, *A Fresh Look at the Meaning of the Doctrine of Denial of Justice under International Law*, 14 CAN. Y.B. INT'L L. 73, 86–90 (1976). Likewise, Freeman wrote that denial of justice included both procedural and substantive protection because both were necessary for the protection of substantive international rights of aliens. Denial of justice, he wrote,

> may reside in the laws organizing the courts and judicial procedure, or in acts of the judge . . . . Or . . . in judicial activity which effects an invasion of some one of his *material* rights by failing to apply a particular rule of international law, whether consecrated by treaty or by the general custom of States.

FREEMAN, *supra* note 13, at 51 (emphasis in original).

tribunal's decision on jurisdiction, the tribunal recognized that a jury decision in a civil suit constituted a government "measure adopted or maintained by a Party" for which state responsibility could be assessed under Chapter Eleven.[96] Also, the tribunal acknowledged in its final award that but for the finality issue, the jury's decision in the *Loewen* case would have been a violation of Article 1105.[97] Although NAFTA tribunals apply Article 1105 rather than "denial of justice" itself, they must incorporate customary standards of denial of justice as a backdrop in order to properly interpret Chapter Eleven's requirements.[98] In *Loewen*, the fact that the tribunal did not dismiss the Article 1105 claim because there had been no extrajudicial original wrong or because Loewen had been the defendant in the court action below shows that NAFTA Chapter Eleven has adopted the modern, expansive view of denial of justice akin to that of Fitzmaurice and denied the traditional definition as espoused by Eagleton.

In conclusion, the definition of denial of justice in modern international law tends toward the broader end of the spectrum. It recognizes that a wide range of acts can constitute denial of justice, whether they fit into the primary category or the secondary category. A court's failure to remedy an antecedent wrong from outside the judicial system and a wrong initiated within the court system are both, equally, denials of justice; both equally subject the state to responsibility; and both equally require satisfaction of the local remedies rule. There is no theoretical distinction between them.

2. *The* Loewen *Tribunal Improperly Treated Primary and Secondary Cases Differently*

The trouble with the *Loewen* decision is that its finality requirement seems to apply only to primary denial of justice claims, but not to secondary claims. According to the tribunal, "the question then [of the *Loewen* case] is as to the scope and content of the obligation to pursue local remedies in a case *in which the alleged violation of international law is founded upon a judicial act*."[99] The tribunal made several statements linking finality exclusively with primary denial of justice. For example, the tribunal distinguished "the local remedies

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96 Decision on Hearing of Respondent's Objection to Competence and Jurisdiction 16, The Loewen Group, Inc. v. United States, ICSID Case No. ARB(AF)/98/3 (NAFTA Ch. 11 Arb. Trib. 2001). Such an interpretation accorded with the interpretation of "measure" in international law and with general principles of state responsibility. *Id*. at 11–12.

97 *See Loewen*, 42 I.L.M. 811, ¶ 54, at 819 (2003).

98 *See supra* note 12.

99 *Loewen*, 42 I.L.M. ¶ 165, at 838 (emphasis added).

rule" from "the requirement that the judicial process be pursued to the highest court *where a judicial act constitutes the breach of international law*."[100] Also, the tribunal stated that

> Article 1121 may have consequences where a claimant complains of a violation of international law *not constituted by a judicial act* . . . . [But] Article 1121 involves no waiver of the duty to pursue local remedies in its application to a *breach of international law constituted by a judicial act*.[101]

This passage says that if the parties to an agreement waive the local remedies rule, the waiver affects only secondary claims, but not primary claims, presumably because the finality requirement still applies in primary claims and a waiver of the local remedies rule does not also waive the finality requirement.

One possible interpretation of the tribunal's reference to cases "in which the alleged violation of international law is founded upon a judicial act"[102] is that the tribunal meant this to refer to both primary and secondary denial of justice—but not to other types of claims for state responsibility that do not involve courts—and that the tribunal focused on primary denial of justice in this case simply because those were the facts at hand. However, there is no indication by the tribunal, either explicitly or implicitly, that the tribunal intended such a reading. Instead, the language taken as a whole strongly indicates that finality applies only in primary cases.[103] Further, even if that were a plausible reading, there is no precedent for distinguishing the exhaustion requirement that applies in denial of justice claims from that of other claims for state responsibility.[104]

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[100] *Id.* ¶ 146, at 835 (emphasis added).

[101] *Id.* ¶¶ 163–64, at 838 (emphasis added).

[102] *Id.* ¶ 165, at 838.

[103] In addition to the tribunal's language in the final award, see also, for example, Opinion of Christopher Greenwood 9–10, Appendix to Counter-Memorial of the United States of America, *Loewen*, ICSID Case No. ARB(AF)/98/3 (2001). Professor Greenwood notes that there is a difference between secondary cases, "where the question is whether the respondent State's courts have provided a remedy for that State's wrongful act," and primary cases, where "it is the behaviour of those courts which is itself said to constitute the wrongful act." *Id*. Greenwood then goes on to state that "a waiver of the local remedies rule will affect the first case but not the second," meaning that the local remedies rule applies in secondary cases, and the finality requirement applies in primary cases. *Id*.

[104] *See, e.g.*, FREEMAN, *supra* note 13, at 404 (noting that exhaustion applies equally to all "claim[s] for indemnity," including "a complaint based upon denial of justice or any other wrong to an alien"); Sohn & Baxter, *supra* note 72, art. 1(2)(a), at 548 (noting that the local remedies rule applies to all allegations of internationally wrongful acts).

Thus, the tribunal's decision leads to the following conclusions. First, the finality rule requires that in primary denial of justice claims, litigants must appeal adverse decisions and get a final court decision in order to invoke state responsibility. Second, however, there is no such finality rule in secondary claims, although the local remedies rule presumably requires the same thing. The problem is that the definition of denial of justice now includes primary and secondary cases and subjects them to the same requirements. Therefore, the tribunal's distinction is inconsistent with the current understanding of denial of justice.

The tribunal's distinction between primary and secondary cases also has other implications. Under the *Loewen* opinion, the *local remedies rule* requires claimants to exhaust local remedies, including appeals, when a government official or individual harms the alien; however, when the original act is a lower court decision, the *finality requirement* takes effect and requires such appeal. The tribunal does not clarify whether in a primary case both requirements apply simultaneously or the finality requirement takes the place of the local remedies rule. Simultaneous application makes little sense because it is unnecessary to have two rules requiring the same act. Also, there is no basis in precedent for the finality requirement replacing the local remedies rule, and, again, it would be redundant—redundant, that is, unless the local remedies rule is waived, as in *Loewen*.[105]

The tribunal's distinction also implies—in fact, the tribunal explicitly states—that a waiver of the local remedies rule has different effects in primary and secondary cases.[106] In secondary cases, waiver of the local remedies rule is effective to waive the requirement to seek a remedy at all levels of the court system; however, in primary cases, waiver of the local remedies rule is not enough—a waiver is somehow not truly a waiver. Thus, the only logical reason to have a separate finality requirement seems to be to take the bite out of waiver, at least in primary denial of justice cases, so that, if the parties waive the local remedies rule and a primary denial of justice claim arises, an international tribunal can still invoke the finality requirement in order to

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[105] Thus, only in the situation in which the local remedies rule has been waived—as in the *Loewen* case itself—is it coherent to apply a separate finality requirement. For a discussion of why this is a problem, see *infra* notes 106–07 and accompanying text, as well as the conclusion of this Comment.

[106] *See Loewen*, 42 I.L.M. ¶¶ 163–64, at 838 ("Article 1121 may have consequences where a claimant complains of a violation of international law *not constituted by a judicial act* . . . . [But] Article 1121 involves no waiver of the duty to pursue local remedies in its application to a *breach of international law constituted by a judicial act*.").

dismiss the claim. To apply ad hoc requirements simply to avoid a waiver of the local remedies rule because of the facts of a particular case, as the tribunal did here, is disingenuous.[107]

B. The Purposes of the Local Remedies Rule and the Finality Requirement

The *Loewen* tribunal conceived of exhaustion of local remedies and finality as two separate requirements with two separate purposes. It also saw the local remedies rule as a procedural requirement and finality as a substantive requirement. The following discussion demonstrates that this distinction, like that between primary and secondary denial of justice cases, was incoherent. Since the local remedies rule already serves the purposes advanced by the tribunal for finality, there is no need for a separate finality requirement.[108]

First, the following discussion recounts the traditional reasons for the local remedies rule and shows that these apply equally to the finality requirement. It also shows that the experts define the local remedies rule broadly enough to make the finality requirement, which serves the same purposes, redundant. Second, it attacks the tribunal's use of the terms "procedural" and "substantive": Instead, it is more consistent with customary international law to say that the local remedies rule serves either a procedural or substantive function depending on whether the wrongful act against the foreigner was an act of the state or of an individual. This section shows that the requirement to exhaust, including appeals to higher levels of the judicial system, is procedural in all but a handful of denial of justice cases.[109]

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[107] As this Comment's conclusion discusses, that is exactly what the tribunal was trying to do here. Since Article 1121 appears to have waived the local remedies rule, the tribunal had to find some way to protect the United States from facing liability arising from the decision of the Mississippi courts.

[108] That is, unless the parties have waived the local remedies rule. But since the local remedies rule has always been defined broadly enough to serve the same purposes asserted for finality, it again appears that the tribunal was using new requirements to take the bite out of the United States' apparent waiver. *See supra* notes 106–07 and accompanying text.

[109] The tribunal held that the requirement to exhaust in secondary cases—called the local remedies rule—is procedural, and the requirement to exhaust in primary cases—called finality—is substantive. Instead, an exhaustion requirement is procedural if state responsibility arises immediately from the injurious act—such as the act of a state actor like an executive or, as this Comment argues, a court—but is substantive if state responsibility does not arise immediately from the injurious act—such as the act of an individual or some other nonstate actor. *See infra* Part III.B.2.

1. Finality and the Local Remedies Rule Serve the Same Purposes, So a Separate Finality Requirement Is Redundant

According to the tribunal, the main purpose of the finality requirement is "to afford the State the opportunity of redressing through its legal system the inchoate breach of international law occasioned by the lower court decision."[110] The tribunal stressed the importance of protecting state sovereignty: Absent the local remedies rule, the lack of a finality requirement "would encourage resort to NAFTA tribunals rather than resort to the appellate courts and review processes of the host State, an outcome which would seem surprising, having regard to the sophisticated legal systems of the NAFTA Parties."[111] As this Section shows, the suggested rationale—to enable host nations to correct their own mistakes before allowing international claims to proceed, thereby protecting state sovereignty—is almost identical to the rationales that have been advanced for the local remedies rule. Because the local remedies rule already serves the stated purposes of the tribunal's finality requirement, there is no need for a separate finality requirement.

Commentators advance several rationales for the local remedies rule. For example, Professor Edwin M. Borchard discussed the following five reasons:

> [F]irst[ly], the citizen going abroad is presumed to take into account means furnished by local law for the redress of wrongs; secondly, the right of sovereignty and independence warrants the local state in demanding for its courts freedom from interference, on the assumption that they are capable of doing justice; thirdly, the home government of the complaining citizen must give the offending government an opportunity of doing justice to the injured party in its own regular way; fourthly, if the injury is committed by an individual or minor official, the exhaustion of local remedies is necessary to make certain that the wrongful act or denial of justice is the deliberate act of the state; and fifthly, if it is the deliberate act of the state, that the state is willing to leave the wrong unrighted.[112]

The local remedies rule reinforces the notion that a state should have the first opportunity to redress wrongs caused by its government—including legislative, executive, administrative, judicial, and other officials—as well as those caused by its citizens, before facing the possibility of international sanction.

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[110] *Loewen*, 42 I.L.M. ¶ 156, at 837.

[111] *Id.* ¶ 162, at 837.

[112] EDWIN M. BORCHARD, THE DIPLOMATIC PROTECTION OF CITIZENS ABROAD § 318, at 817–18 (1915).

Alwyn Freeman gave several additional justifications. Requiring exhaustion might actually be favorable to the claimant: If the claimant is able to find redress in local courts, there will be no need to bring an international claim.[113] Also, similar to Borchard's main rationale, fairness and the presumption of uniformity between states demand that a local government have a chance "to insist upon adjudicating all issues which fall within its competence under municipal law."[114] The result of the restriction is to preserve national autonomy and alleviate friction between national and international bodies. Further, the rule acts as a form of docket control: "Only those cases which are really worthy of consideration should be allowed to come before international courts."[115]

In sum, by allowing the host state to correct the mistakes of its own officials and citizens the local remedies rule protects state sovereignty.[116] The rule reflects international law's presumption of a state's competence to resolve its own problems through its own system.[117] In fact, some scholars argue that the local remedies rule exists to allow the host state to fulfill an international obligation to correct injuries that occur within its borders. For example, Freeman stated that once there is a violation of international law, the international sanction is fixed and can "be dissolved only upon compliance with the *subsidiary duty of reparation* that is born of the violation of an international rule."[118] Thus, according to Freeman, states have an affirmative "duty of reparation" to injured aliens. To be able to bring an international claim before allowing the host state the first opportunity to correct underlying injuries would deny the state the ability to exercise that duty. These rationales are indistinguishable from those given by the tribunal for its finality requirement: Both requirements are intended to give host states the first chance to redress their own wrongs, and both are intended to ensure deference to state sovereignty.

Although the differences between finality and the local remedies rule do not seem to have existed in the past, it is not surprising—based on the

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[113] FREEMAN, *supra* note 13, at 416.
[114] *Id.*
[115] *Id.* at 417 (internal quotation marks omitted).
[116] Vitányi, *supra* note 65, at 159. The problem of national sovereignty is one of the major complaints NAFTA critics had about the tribunal's decision to hear the *Loewen* claim. *See, e.g.*, Shapren, *supra* note 7, at 343 (arguing that the grant of jurisdiction to the *Loewen* case meant that the United States was surrendering the sovereignty of its national court system to a three-person tribunal behind closed doors).
[117] Vitányi, *supra* note 65, at 159.
[118] FREEMAN, *supra* note 13, at 443 (emphasis in original).

similarity in purposes between the local remedies rule and the finality requirement—that prior definitions of the local remedies rule have been broad enough to encompass and serve the same purposes as the tribunal's finality requirement. For example, in his 1938 tome on denial of justice, Freeman wrote, "It is but a specific application of [the local remedies] rule that *no claim based upon a denial of justice may be predicated upon the decision of a lower court*."[119] Freeman did not assert specifically that in the context of a case of primary denial of justice there is no separate finality requirement. However, if the local remedies rule is as broad as Freeman (and this discussion) claims, then it would be redundant to have a separate finality requirement.[120]

Like Freeman, other sources define the local remedies rule in a way that adequately covers the same ground as the finality requirement.[121] As the International Law Commission declared, "[L]ocal remedies shall be deemed to have been 'exhausted' when the decision of the competent body or official that rendered it is final and without appeal."[122] C.F. Amerasinghe, Executive Secretary of the World Bank Administrative Tribunal, wrote that "the principle has not been disputed" that the local remedies rule requires claimants to "proceed to the highest court in the total system, which may include more than one line of tribunals or courts."[123] Similarly, Professor William S. Dodge stated, "[I]t is clear that the local remedies rule is not satisfied until the injured alien has completely exhausted its appeals and has obtained a final decision from the highest court of the host State to which it has a right to resort."[124] These statements indicate that the local remedies rule already does what the

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[119] *Id.* at 415 (emphasis in original).

[120] Except, that is, in cases in which the local remedies rule has been waived. *See supra* notes 106–07 and accompanying text.

[121] In addition to the sources cited in this paragraph, see *McElhinney v. Ireland*, in which the European Court of Justice held,

> The purpose of the domestic remedies rule is to give the respondent State the opportunity of preventing or putting right the violations alleged . . . . The applicant took his complaints to the highest court in . . . Ireland and, therefore, exhausted domestic remedies in so far as that country is concerned.

121 Eur. Ct. H.R. 199, 207–08 (2000).

[122] International Law Commission, *Responsibility of the State for Injuries Caused in its Territory to the Person or Property of Aliens: Revised Draft*, [1961] 2 Y.B. INT'L L. COMM. 46, art. 18(2), at 48, I.L.C. Doc. A/CN.4/34/Add.1.

[123] C.F. AMERASINGHE, LOCAL REMEDIES IN INTERNATIONAL LAW 181 (1990) (citing Finnish Ships Arbitration, 3 R.I.A.A. 1479, 1495 (1934)).

[124] William S. Dodge, *National Courts and International Arbitration: Exhaustion of Remedies and Res Judicata Under Chapter Eleven of NAFTA*, 23 HASTINGS INT'L & COMP. L. REV. 357, 362 (2000).

finality rule purports to accomplish: Both require appeals in the face of adverse court decisions. Therefore, there is no need for both rules.

Additionally, in the context of denial of justice cases based on unjust court decisions, there has been more explicit support for the notion that the purpose of the tribunal's finality requirement is served by the local remedies rule. In the *Ambatielos Claim (Greece v. United Kingdom)*,[125] the International Court of Justice confronted the issue more directly in a case much like the *Loewen* case. Ambatielos, a Greek national, contracted with Major Bryan Laing to purchase nine ships from the United Kingdom's Ministry of Shipping.[126] He executed mortgages on the ships, but two were never delivered, so he pursued arbitration under the terms of the agreement.[127] The British Board of Trade then filed suit against Ambatielos on the mortgage deeds, and the trial resulted in a judgment in favor of the United Kingdom.[128] However, the government had refused to produce some interdepartmental minutes and some letters between Major Laing and his superior, and Laing was not brought into the court as a witness even though he had been subpoenaed.[129] Ambatielos appealed the judgment and asked the Court of Appeal to call Major Laing, but the Court refused, stating that it would be against precedent because Ambatielos could have called Laing at the trial. Ambatielos did not appeal from the Court of Appeal's decision.[130]

Ambatielos then went directly to the International Court of Justice, which eventually dismissed the claim due to his failure to exhaust local remedies. According to the Commission, the local remedies rule requires that a complainant "should have exhausted the possibilities of appealing to a higher court against any adverse decision of a lower one."[131] In fact, the local remedies rule required the use of all "the procedural facilities which municipal law makes available to litigants before such courts and tribunals" because the whole legal system must have an opportunity to correct the trial court's decision before the injured alien can bring the claim to the international

125 23 I.L.R. 306 (1956).
126 *Id.* at 306.
127 *Id.* at 307.
128 *Id.* at 308.
129 *Id.*
130 *Id.*
131 *Id.* at 335 (adopting the United Kingdom's argument).

forum.[132] Thus, Ambatielos's failure to appeal to the House of Lords was a failure to exhaust local remedies that required some excuse or explanation.

The *Ambatielos* and *Loewen* cases are almost identical: both were contract claims, both injured aliens were defendants in the trial court below, both were injured by the wrongful acts of the trial court, and both failed to appeal to the highest level of the host state's judicial system. Therefore, there is no reason for the international community to treat them differently. However, Ambatielos's claim failed because he did not exhaust the local remedies available to him, while Loewen's claim failed for an entirely different reason: Loewen did not fulfill a separate finality requirement. As *Ambatielos* demonstrates, the local remedies rule already requires claimants to appeal adverse court decisions to the highest available court, so there is no need for a separate finality requirement. No need, that is, unless the local remedies rule has been waived. In fact, the only difference between these two cases seems to be that in *Loewen*, the parties apparently waived the local remedies rule. This further indicates that the *Loewen* tribunal was using finality as a way to get around the problem of Article 1121, as the conclusion to this Comment argues.[133]

In support of its separation of the two requirements, the *Loewen* tribunal asserted, "No instance has been drawn to our attention in which an international tribunal has held a State responsible for a breach of international law constituted by a lower court decision when there was available an effective and adequate appeal within the State's legal system."[134] That may be true, but this fact does not refute the primary hypothesis of this Comment. Indeed, the fact that the claimant must appeal before bringing an international claim would be true whether it was part of the local remedies rule or a separate requirement. In fact, Freeman asserted that the local remedies rule had the same effect: "Failure to appeal has on more than one occasion been the ground for an international tribunal's refusal to render an award in cases of alleged denial of justice."[135]

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[132] *Id*. at 336. Note that this statement of the reason behind the local remedies rule is almost identical to the *Loewen* tribunal's language describing the need for a separate finality requirement. *See* The Loewen Group, Inc. v. United States, ICSID Case No. ARB(AF)/98/3, 42 I.L.M. 811, ¶ 143, at 834 (NAFTA Ch. 11 Arb. Trib. 2003) ("State responsibility only arises when there is a final action by the State's judicial system as a whole.").

[133] *See supra* notes 106–07 and accompanying text.

[134] *Loewen*, 42 I.L.M. ¶ 154, at 836.

[135] FREEMAN, *supra* note 13, at 416.

2. *The Multiple Purposes of the Local Remedies Rule and the Timing of State Responsibility*

This subsection confronts the tribunal's assertion that the finality requirement and the local remedies rule are distinct because the former serves a substantive purpose and the latter serves a procedural purpose.[136] This debate runs headlong into the question of at what precise point in the process of a denial of justice claim, whether primary or secondary, does the state become responsible for the action. The tribunal states that its finality requirement, which applies in primary cases, is a substantive requirement because the act of an inferior court by itself cannot incur state responsibility: There is no internationally wrongful act until the highest court upholds the injurious ruling. The tribunal's narrow version of the local remedies rule, however, is a procedural requirement because state responsibility arises immediately from the underlying act, and the claimant must seek local remedies as a procedural hurdle before bringing a claim.

This subsection argues, first, that the exhaustion requirement of the local remedies rule (as correctly defined) can act as both a procedural *and* a substantive requirement. The requirement will be procedural for any case in which state responsibility arises immediately from the act and substantive for acts that do not incur immediate state responsibility, such as acts of individuals. Second, it will show that judicial acts, just like the acts of other branches of the state, do incur immediate state responsibility. Therefore, the requirement to appeal is procedural in all but a handful of denial of justice cases.

In other words, it is inappropriate to judge the nature of an exhaustion requirement as procedural or substantive based solely on whether it is being used in a primary or secondary denial of justice claim, as the *Loewen* tribunal did. Instead, the nature of the exhaustion requirement should be based on the nature of the injurious act itself: The local remedies rule is procedural for all primary claims and for secondary claims based on acts of other branches of government, and substantive for secondary claims based on the acts of

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[136] As the *Loewen* tribunal stated,

> The requirement that a decision of a lower court be challenged through the judicial process *before the State is responsible for a breach of international law constituted by judicial decision* means that this [finality] requirement and the local remedies rule, though they may be similar in content, serve two different purposes.

Loewen, 42 I.L.M. ¶ 159, at 837.

nongovernmental actors. Consequently, what the tribunal calls "finality" turns out to be part of the procedural function of the local remedies rule in all cases except for those premised on the act of an individual.

a. The Procedural and Substantive Nature of the Local Remedies Rule

Academics and drafters have long disagreed as to whether the local remedies rule is substantive or procedural. In the 1930 Hague Codification Conference, for example,[137] some delegates defended the view that the exhaustion of local remedies was a substantive requirement for state responsibility. In fact, there was such disagreement that the delegates adopted a compromise formulation that a state's responsibility "*may not be invoked* . . . until after exhaustion of the remedies available."[138] Such wording left the answer intentionally ambiguous.

However, more recently, the international community adopted the view that, in most cases, the local remedies rule is procedural. According to one academic,

> [T]he foreign national must exhaust such local remedies before its home State can take up the claim on an international level . . . . The rule does not mean that, until it has been complied with, no international tort has been committed. Clearly, at this stage, an international obligation has been broken.[139]

In fact, the *Loewen* tribunal presumes that the local remedies rule is a procedural requirement.[140]

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[137] *See generally* Edwin M. Borchard, *"Responsibility of States," at the Hague Codification Conference*, 24 AM. J. INT'L L. 517 (1930) (describing the proceedings).

[138] FREEMAN, *supra* note 13, at 444 (emphasis in original).

[139] 1 GEORG SCHWARZENBERGER, INTERNATIONAL LAW 603 (3d ed. 1957). Similarly, as the International Law Commission stated in 1961, "An international claim brought for the purpose of obtaining reparation for injuries sustained by an alien . . . shall not be *admissible* until . . . all the remedies and proceedings established by municipal law have been exhausted." International Law Commission, *supra* note 122, art. 18(1), at 48 (emphasis added). Likewise, in the International Law Commission's *2001 Draft Articles on Responsibility of States for Internationally Wrongful Acts*, a state's international responsibility occurs immediately upon commission of an internationally wrongful act. *See* International Law Commission, *supra* note 65, art. 1. However, under the heading "Admissibility of Claims," a claimant cannot invoke the international responsibility of a state if the "claim is one to which the rule of exhaustion of local remedies applies and any available and effective local remedy has not been exhausted." *Id.* art. 44(a)(2); *see also* Sohn & Baxter, *supra* note 72, art. 1(2)(a), at 548 ("An alien is *entitled to present* an international claim . . . only after he has exhausted the local remedies provided by the State against which the claim is made.") (emphasis added).

[140] *Loewen*, 42 I.L.M. ¶ 149, at 835. However, as the United States argued in one of its briefs, there are still several schools of thought on this issue. *See* Juliane Kakott, *Interim Report on "The Exhaustion of Local Remedies"*, *in* FIRST REPORT OF THE INTERNATIONAL LAW ASSOCIATION LONDON CONFERENCE, at 9–10

The problem with defining the local remedies rule generally as either procedural or substantive is that because the rule applies broadly to many forms of state responsibility, it serves more than one function.[141] Instead, the local remedies rule should be described in a way that better illuminates its various functions.[142] For example, Freeman described the local remedies rule as both procedural and quasi-substantive.[143] As the next several paragraphs demonstrate, whether the local remedies rule serves its procedural or substantive role is based solely on the timing of state responsibility in a particular case.

The local remedies rule is procedural in the sense that, in many cases, state responsibility arises immediately after an injury occurs, and the exhaustion requirement is merely a procedural hurdle that must be overcome before an international claim can be filed. For example, if the United States Congress were to pass a law—or the President of the United States were to issue an Executive Order—expropriating the assets of a Canadian investor, state responsibility would be immediate. However, the local remedies rule would require suit in a U.S. district court and pursuit of any available local remedies (including any available appeals) before an international claim could be brought. This would be a procedural requirement. When state responsibility exists immediately, but the claim cannot be brought until local remedies are exhausted, the local remedies rule serves a procedural function. "[W]hen breach of [a] treaty or rule of international . . . law is alleged, international responsibility is inchoate, becoming complete or ripe only when the state has spoken finally, and if the breach is then uncorrected, the wrong dates back to

(2000), *available at* http://www.ila-hq.org/html/layout_committee.htm (making the 2000 Conference Report available). According to the procedural theory, the local remedies rule is only a practical rule designed as a device for implementation of state responsibility. *Id.* at 9. Under the substantive theory, there is no state responsibility at all until the claimant satisfies the local remedies rule. State responsibility is not engaged by either the first breach or the last, but instead by the entire course of events. *Id.* at 9–10. Under the intermediary theory, the local remedies rule is procedural in all cases except those in which the breach of the international obligation derives exclusively from the action of "judicial organs which have failed in their duty to provide an individual with the internationally required judicial protection against injuries sustained in breach of purely internal law." *Id.* at 10.

The *Loewen* tribunal calls the local remedies rule purely procedural and the finality requirement—which is completely separate—purely substantive. This Comment, as this Section shows, adheres to a theory more like the intermediary theory: The local remedies rule is procedural in all cases except those in which an individual injures an alien because in those cases, an act of the state is still necessary to create state responsibility.

[141] Herbert W. Briggs, *The Local Remedies Rule: A Drafting Suggestion*, 50 AM. J. INT'L L. 921, 925 (1956).

[142] *Id.*

[143] FREEMAN, *supra* note 13, at 407.

the original injury."[144] Thus, once there is state responsibility, the alien must exhaust local remedies—a procedural requirement—to be able to bring that claim before an international tribunal. At that time, it is up to the host state to dissolve its inchoate responsibility by complying with the duty of reparation that arises from breaking an international obligation.[145]

The rule is substantive in the sense that in some cases, an original act causing injury creates no state responsibility until the court denies justice, so the local remedies rule is a substantive requirement that must be met before an international claim arises. For example, if Company A, a Mississippi corporation, commits some wrong against Company B, a Canadian corporation, the wrong does not incur immediate state responsibility. There, and only there, the local remedies rule is a substantive requirement because a state cannot be responsible for the act of a private actor. Thus, only in cases involving underlying acts by individuals is there no international responsibility until a court denies justice.

Therefore, the question in the *Loewen* case becomes whether a decision of a lower court in a primary denial of justice claim is an act that violates international law on its own—like acts of other branches of government—or whether it is more like the act of an individual, which requires a further denial of justice to incur state responsibility. If it is the former, then the alien's obligation to exhaust local remedies in primary denial of justice cases—which includes what the *Loewen* tribunal called "finality"—is procedural, contrary to the tribunal's argument. If it is the latter, then the alien's obligation to exhaust local remedies in primary denial of justice cases is substantive, as the tribunal argues. As the following section demonstrates, a trial court's decision incurs immediate state responsibility, just like acts of other branches of government. Thus, the international community does not need a substantive exhaustion requirement, such as the one created by the *Loewen* tribunal, except in denial of justice cases that result from the acts of individuals.

b. Immediate State Responsibility for Judicial Acts

The tribunal's theory, based in part on the United States' argument that the judicial process from start to finish is one act of the state, was that there can be no state responsibility at all for judicial decisions until the entire legal process

[144] Borchard, *supra* note 137, at 533 (referring to the view of a Dr. Latifi of India). In response to Latifi's suggestion, Professor Borchard stated, "To such a legal proposition, there can be no objection." *Id.*

[145] FREEMAN, *supra* note 13, at 443.

of a state has had a chance to correct the unjust decision.[146] This argument echoes that of Professor De Visscher, Belgian delegate to The Hague Codification Conference, who argued that a state does not speak until its highest court acts.[147] The major problem with De Visscher's theory is that it distinguishes the acts of lower courts from acts of other minor officials and require, as does the *Loewen* tribunal: the implication that inferior courts can never commit an internationally wrongful act,[148] which leads to the further implication that a lower court's decision is a less reprehensible act of a state than is an unjust act of a minor official of some other branch of the government.[149] Such a distinction is unwarranted in modern international law.[150]

Instead, whether an act creates international responsibility should depend on the act itself rather than its source: A state should be immediately responsible for any act by an arm of the government, including a judicial decision, as long as that act violates a treaty or possesses an internationally illegal character.[151] This interpretation is consistent with the various draft

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[146] The argument was that the requirement to appeal is substantive because a lower court's decision is not the same as the failure of a national court system to provide justice. Therefore, there is no denial of justice until the claimant pursues all available avenues of appeal. The United States based its argument, in part, on the United States and United Kingdom's comments on a recent International Law Commission draft that a lower court decision should not be considered a breach of international law. Rejoinder of the United States of America 105–08, The Loewen Group, Inc. v. United States, ICSID Case No. ARB(AF)/98/3 (NAFTA Ch. 11 Arb. Trib. 2001). However, contrary to this argument, the requirement to appeal can still be procedural even though it gives appellate courts the opportunity to correct the state's errors. *See supra* Part III.B.1.

[147] Borchard, *supra* note 137, at 532.

[148] FREEMAN, *supra* note 13, at 446.

[149] Borchard, *supra* note 137, at 533 (stating that this "supposed distinction" indicates the "essential unsoundness" of De Visscher's theory). Also, De Visscher's statement was made during a debate over proposed language concerning the timing of state responsibility, and the statement did not represent the opinion of a majority or even a large portion of the delegates. In fact, there was so much disagreement that no convention was ever agreed upon. *Id.* at 540.

[150] It is worth noting here that the United States rarely views court action as "state action," which is important in determining whether federal constitutional rights have been violated. *See, e.g.*, Shelley v. Kraemer, 334 U.S. 1, 13 (1948) (noting that the Fourteenth Amendment protects against actions of the government and "erects no shield against merely private conduct, however discriminatory or wrongful"). The U.S. Supreme Court has held that a trial court's action can constitute an act of the state. *See id.* (holding that the court enforcement of a racist restrictive covenant was state action and violated federal civil rights laws). However, courts generally have not followed *Shelley* outside the restrictive covenant area. Thus, as Laurence Tribe describes, state action cases are a conceptual disaster area, as there are no general rules dictating when the state is responsible for certain acts of officials. *See generally* LAURENCE H. TRIBE, AMERICAN CONSTITUTIONAL LAW 1688–1720 (2d ed. 1988).

[151] 2 CHARLES CHENEY HYDE, INTERNATIONAL LAW CHIEFLY AS INTERPRETED AND APPLIED BY THE UNITED STATES 933 (2d rev. ed. 1945) (arguing that for one to state that a sovereign can never be liable for the

conventions.[152] For example, the International Law Commission's *2001 Draft Articles on Responsibility of States for Internationally Wrongful Acts* states,

> The conduct of any State organ shall be considered an act of that State under international law, whether the organ exercises legislative, executive, *judicial* or any other functions, *whatever position it holds in the organization of the State*, and whatever its character as an organ of the central government or of a territorial unit of the State.[153]

Similarly, according to the 1961 Harvard Law School *Draft Convention on the International Responsibility of States for Injuries to Aliens*, adverse decisions and judgments of courts that clearly discriminate against the alien, unreasonably depart from international principles of justice, or otherwise violate treaties are considered "wrongful acts" that create international responsibility.[154]

Several commentators also have written that state responsibility arises immediately upon the commission of a judicial act contrary to international law. According to Freeman, "To anyone who admits that minor officials are capable of violating international law . . . it would be inconsistent to hold that internationally illegal conduct on the part of inferior courts does not produce the same consequence."[155] Similarly, Don Wallace, Jr., Chairman of the International Law Institute, recently stated, "A state responsibility is engaged by the actions of any of its agencies, including the judiciary . . . . I don't think that's a question." He seemed to agree that judicial decisions create state responsibility when he continued, "If . . . denial of justice can mean a grossly disproportionate result . . . if there's no question but that a court can be an instrumentality of the state which engages responsibility . . . how does it work?"[156]

In sum, "finality" is not a separate requirement due to its being substantive as opposed to the local remedies rule being procedural. A primary denial of justice in violation of the standards of customary international law or a treaty,

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act of an inferior court improperly assigns responsibility based on "the grade of the actor rather than the quality of his act").

[152] For a counterexample, however, see Borchard, *supra* note 77, at 166, which states that "the acts of inferior judges or courts do not render the state responsible . . . ." As the rest of this discussion will demonstrate, such sentiments have since been abandoned.

[153] International Law Commission, *supra* note 65, at art. 4(1) (emphasis added).

[154] Sohn & Baxter, *supra* note 72, art. 8, 3(1)(c)–(1), at 548–50.

[155] FREEMAN, *supra* note 13, at 445.

[156] Don Wallace, Jr., *State Responsibility for Denial of Substantive and Procedural Justice Under NAFTA Chapter Eleven*, 23 HASTINGS INT'L & COMP. L. REV. 393, 397 (2000).

such as NAFTA, should be seen as an internationally wrongful act, and the underlying injurious act of the court should be treated similarly to the injurious acts of other government officials in secondary cases. In a primary denial of justice case, state responsibility arises as soon as the lower court imposes an unjust judgment on the alien, but the claim lies inchoate until the alien exhausts all available local remedies, namely, the opportunity to appeal to higher levels of the judicial system. During that time, the host state has the opportunity to correct its original wrong. Once the alien's available domestic remedies are exhausted, the alien's denial of justice claim becomes active, and the alien can then seek relief in the international forum. In these types of cases, the local remedies rule—including the tribunal's finality requirement—is procedural.

The only situation in which the local remedies rule is substantive is in secondary denial of justice claims involving an extrajudicial act that does not incur immediate state responsibility—that is, the conduct of a nonstate actor. The local remedies rule, including the finality requirement, is procedural in all other primary and secondary cases—that is, all primary denial of justice claims and all secondary denial of justice claims in which the offending act was the act of any state actor, including a lower court. Because in most primary and secondary cases a state's international responsibility arises immediately upon the occurrence of an underlying act, international law does not need a substantive exhaustion requirement, like the one proposed in *Loewen*, except in the case of injurious acts by individuals.

C. Conclusion: Summary of the Law

It makes little sense to call the requirement to appeal adverse court decisions the "local remedies rule" in one situation but not in the other. However, even though the *Loewen* tribunal's decision that finality is separate from the local remedies rule was incorrect, the tribunal was at least partly correct in recognizing that the rule applies slightly differently in different cases. To misunderstand or ignore this difference is to oversimplify the local remedies issues brought up in *Loewen*. This Section provides a useful summary of a correct understanding of the law.

In the classic case of secondary denial of justice, an original wrong occurs either in the act of an individual or in some branch of government outside the judiciary. The local remedies rule requires that the injured foreigner seek all available local remedies, including any remedies offered in the national courts

or administrative bodies of the host nation. If the claim is predicated on the act of an individual, there is no immediate responsibility, and the exhaustion of local remedies is necessary to invoke state responsibility. In that case, and only in that case, the local remedies rule is substantive. However, when the claim is based on a wrongful act of a government agent, state responsibility exists immediately, and the local remedies rule is merely a procedural requirement that must be satisfied before the alien can bring an international claim. Once the alien exhausts all remedies (including "finality," the pursuit of the claim to the highest available court) without obtaining adequate relief, the alien's claim becomes active, and the alien can then bring that claim against the foreign nation at the international level.

In the case of a primary denial of justice as in *Loewen*, however, the alien is first injured by an improper court decision at some level of the host nation's judicial system. This original wrong also constitutes a denial of justice and incurs immediate state responsibility. The local remedies rule acts as a procedural requirement and requires that the alien seek all available local remedies, including appeals to the host country's highest court. If the alien exhausts all remedies within the judicial system without finding adequate relief for the injury caused in the court below, the alien's claim becomes active, and the alien can then bring its international claim for denial of justice. In sum, the local remedies rule requires exhaustion of all local remedies, including any available appeals through the nation's judicial system, and regardless of whether the original wrong occurred in a court or in another branch of the host state's government.

The purpose of this Part was to illustrate the errors of *Loewen* and suggest a better definition of the local remedies rule based on pre-*Loewen* authority: The local remedies rule includes what the *Loewen* tribunal called "finality," a denial of justice claimant's obligation to appeal adverse court decisions. In practical terms, the effect of accepting this broader formulation is not great. In most cases, whether "finality" or "the local remedies rule" requires appeal to higher courts makes little real-world difference. However, as *Loewen* showed, and as the remainder of this Comment explores, under the current understanding of Article 1121, these different definitions can lead to different conclusions about whether exhaustion is required when parties have waived the local remedies rule.

IV. THE ARTICLE 1121 WAIVER DEBATE

Part III demonstrated that finality should not be defined as a separate concept from the local remedies rule. Of course, that issue is merely a question of how broadly one defines those terms, and in the absence of Article 1121, it would be easy to dismiss this Comment's hypothesis as trivial. Article 1121, however, brings the issue into sharp relief. The definition becomes important in determining whether Chapter Eleven waived, and, if so, to what extent it waived, the rule. Because finality is merely a subset of the local remedies rule, and because finality is actually part of the procedural function of the local remedies rule in most cases,[157] it follows that if Chapter Eleven waived the rule, it also waived the finality requirement. If Article 1121 provides such a waiver, the NAFTA parties need to acknowledge it—along with all its consequences—and either accept it or adjust accordingly.[158]

The local remedies rule is not a hard and fast rule, and it does not apply in certain cases. For example, exhaustion is not required when there are no available remedies or where resort to available remedies would be obviously futile.[159] Likewise, it is not required when the parties have waived the protection of the rule by treaty.[160] According to the International Court of Justice, there is "no doubt that the parties to a treaty can therein either agree that the local remedies rule shall not apply to claims based on alleged breaches

[157] The tribunal's finality requirement is procedural in all cases except for secondary claims premised on the acts of nonstate actors. For a complete discussion on why this is so, see *supra* Parts III.B.2, III.C.

[158] Although the options available to Canada, the United States, and Mexico are beyond the scope of this Comment, if Article 1121 does waive the local remedies rule, they could follow any of several courses of action. First, any of the parties could urge the FTC to issue an interpretation under Article 1131 clarifying that Article 1121 is not intended as a waiver of the local remedies rule. Second, any of the parties could propose an amendment to Chapter Eleven that would either eliminate Article 1121 or otherwise make it clear that the local remedies rule applies to Chapter Eleven claims. Third, any of the parties could propose an amendment so that Chapter Eleven would encourage exhaustion of domestic appeals but still allow direct review to remain an option. William S. Dodge, Loewen v. United States*: Trials and Errors Under NAFTA Chapter Eleven*, 52 DEPAUL L. REV. 563, 572–77 (2002). Fourth, if the first three options fail, any of the parties might consider withdrawing from NAFTA, regardless of the costs involved. Such a decision would be drastic, but if the parties hope to avoid potential liability for every unpalatable trial court decision that adversely affects a foreign investor, such a step might be impossible to avoid.

[159] *E.g.*, Dodge, *supra* note 124, at 362. For example, the rule has been excused when local tribunals were of such a nature that no confidence could be placed in them, where there were no duly established courts, and where the judges were controlled by a local mob. Borchard, *supra* note 77, art. 7 cmt. a, at 157–58.

[160] *E.g.*, AMERASINGHE, *supra* note 123, at 251–75.

of that treaty; or confirm that it shall apply."[161] The majority view is that the local remedies rule is not presumed to be waived unless it is expressly revoked or reserved.[162]

The text of Article 1121 seems to embody an express waiver of the local remedies rule in Chapter Eleven claims. Article 1121 states that in order to submit a Chapter Eleven claim for arbitration, an investor, and where applicable an injured enterprise that the investor owns or controls, must:

> waive [the] right to initiate or continue before any administrative tribunal or court under the law of any Party, or other dispute settlement procedures . . . except for proceedings for injunctive, declaratory or other extraordinary relief, not involving the payment of damages, before an administrative tribunal or court under the law of the disputing Party.[163]

The article requires a claimant to give up any pending or possible future claims in the host nation's national court as a condition precedent to bringing the NAFTA claim, which also appears to waive the local remedies rule: A claimant cannot be expected to exhaust domestic remedies if Article 1121 requires the claimant to give up the opportunity to pursue those remedies.

Professor William S. Dodge maintains that the best reading of Article 1121 is as a waiver of the local remedies rule.[164] According to Dodge, the foremost advocate of the Article 1121 waiver conclusion, the words of the article expressly require waiver of domestic proceedings, which "strongly suggests that an investor is not required to complete any suit it may have filed in domestic court or even to initiate one at all before bringing its claims before a NAFTA tribunal."[165] However, Article 1121 is permissive. Even though the article does not require exhaustion of local remedies, it allows the injured party

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[161] Case Concerning Elettronica Sicula S.p.A. (ELSI) (U.S. v. Italy), 28 I.L.M. 1109, 1125 (1989) (rejecting, however, the United States' argument that the rule did not apply because there had been no explicit waiver).

[162] AMERASINGHE, *supra* note 123, at 256 ("[N]either State practice nor judicial opinion warrants the opposite view."); *see* A.A. CANÇADO TRINDADE, THE APPLICATION OF THE RULE OF EXHAUSTION OF LOCAL REMEDIES IN INTERNATIONAL LAW 133 (1983) ("The lesson to be drawn . . . is that implied waiver of the local remedies rule is not properly to be followed as a general policy of treaty-making and interpretation.").

[163] NAFTA, *supra* note 1, art. 1121(1)(b), 2(b), at 643.

[164] Dodge, *supra* note 124, at 360; *see also* William S. Dodge, The Loewen Group, Inc. v. United States *and* Mondev International Ltd. v. United States, 98 AM. J. INT'L L. 155, 161–62 (2004) (noting that "[a]s desirable as an exhaustion requirement may be in theory, however, the *Loewen* award is in considerable tension with the text of NAFTA and the decisions of other Chapter 11 tribunals," and that other NAFTA tribunals have unanimously concluded that Article 1121 waives the local remedies rule).

[165] Dodge, *supra* note 124, at 374.

to seek local remedies first as long as the alien completes or gives up those state court claims before filing a NAFTA claim; furthermore, it does not allow the alien to seek NAFTA relief first and then seek local relief later.[166]

In addition to the express language of Article 1121, Dodge provides three other arguments supporting the claim that Article 1121 waives the local remedies rule. First, according to Article 1115, one purpose of Chapter Eleven is to ensure "the principle of international reciprocity and due process before an international tribunal."[167] Although the local remedies rule does not deny this access or due process, it does delay access for the period of exhaustion.[168] Therefore, to require exhaustion would be in tension with Article 1115. Second, Articles 1116(2) and 1117(2) create a statute of limitations: A foreign investor cannot bring a NAFTA claim if more than three years have elapsed since the foreigner knew or should have known about the alleged breach of NAFTA.[169] But there is no provision for tolling the limitation period while the alien pursues the claim in national courts, which, as Dodge writes, "one might have expected if the exhaustion of local remedies were required."[170] Third, the fact that NAFTA parties do not raise the nonexhaustion of local remedies as a defense to claims shows that they do not require exhaustion before hearing a claim.[171]

Other commentators agree that Article 1121 most likely waives the local remedies rule for Chapter Eleven claims. For example, Don Wallace stated, "[M]y own view is . . . that there is clearly no requirement of exhaustion of local remedies, because, in fact, 1121 talks about having to waive . . . so exhaustion is out."[172] Similarly, Jack Coe wrote, "It may well be true that Article 1121 . . . is not aimed at the exhaustion requirement specifically, but within Chapter 11's overall architecture, it is difficult to see how one can both exhaust local remedies and waive their initiation or continuance."[173]

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[166] *Id.* at 371, 375–76.

[167] NAFTA, *supra* note 1, art. 1115, at 642.

[168] Dodge, *supra* note 124, at 375.

[169] NAFTA, *supra* note 1, art. 1116(2), 1117(2), at 643.

[170] Dodge, *supra* note 124, at 375.

[171] *Id*. at 360. Dodge offers three examples of NAFTA cases in which the defendant nation failed to raise the nonexhaustion defense: *Ethyl Corp. v. Canada*, *S.D. Myers, Inc. v. Canada*, and *Azinian v. Mexico*, which are all available at http://www.naftalaw.org. *See* Dodge, *supra* note 124, at 375 n.86.

[172] Wallace, *supra* note 156, at 394.

[173] Jack J. Coe, Jr., *Taking Stock of NAFTA Chapter 11 in Its Tenth Year: An Interim Sketch of Selected Themes, Issues, and Methods*, 36 VAND. J. TRANSNAT'L L. 1381, 1423 (2003).

Furthermore, other NAFTA tribunals have concluded that Article 1121 waives the local remedies rule for Chapter Eleven claims: In *Feldman v. Mexico*, *Waste Management, Inc. v. Mexico*, and *Metalclad v. Mexico*, NAFTA tribunals noted that Chapter Eleven does not require exhaustion of local remedies.[174] Even the *Loewen* tribunal acknowledged that although the article's purpose "is not altogether clear, it requires a waiver of domestic proceedings as a condition of making a claim to a NAFTA tribunal."[175] But the tribunal stopped short of ruling on whether the article waived the rule in all cases. Instead, it held that, even if the article waived the local remedies rule, nothing in the article explicitly waived the finality requirement.[176]

The tribunal's conclusion is incorrect because there is no substantive difference between the local remedies and finality requirements: If the rule is waived for secondary cases of denial of justice, it must be waived for primary cases as well. Even if one accepts the proposition that finality is separate from the local remedies rule, it is still a stretch to conclude from the words of Article 1121 that Article 1121 waives the requirement to pursue local remedies but not the requirement to appeal. Article 1121 requires a claimant to waive the right "to initiate *or continue*" any suits for money damages before a tribunal under national law.[177] The fact that a claimant must give up the right to "initiate" a national court proceeding requires the claimant to forgo local remedies in secondary cases. Likewise, the requirement of giving up the right to "continue" a national court claim seems to require the claimant to forgo appeals to higher courts, which seems to explicitly waive finality in primary denial of justice cases. Therefore, the text of Article 1121 requires waiver of both what the *Loewen* tribunal called the "local remedies rule" and what it called the "finality requirement."[178]

However, the language of Article 1121 also suggests that the NAFTA drafters came to the table with assumptions that were different from those

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[174] Dodge, *supra* note 164, at 162 (noting, however, that unlike in *Loewen*, the awards cited in those three cases "did not involve challenges to domestic court decisions").

[175] The Loewen Group, Inc. v. United States, ICSID Case No. ARB(AF)/98/3, 42 I.L.M. 811, ¶ 161, at 837 (NAFTA Ch. 11 Arb. Trib. 2003).

[176] *Id*. Thus, "Article 1121 involves no waiver of the duty to pursue local remedies . . . [for] a breach of international law constituted by a judicial act." *Id*. ¶ 164, at 838.

[177] NAFTA, *supra* note 1, art. 1121(1)(b), 2(b), at 643 (emphasis added).

[178] The *Loewen* tribunal stated that its finality rule is a substantive requirement. The issue of whether substantive requirements for state responsibility can be waived is beyond the scope of this Comment. However, adopting the argument of Part III.B.2, *supra*, the requirement to appeal is actually procedural, and part of the local remedies rule, so it can be waived.

underlying the local remedies rule. As this Comment shows, the traditional rule functions as a procedural hurdle that the injured plaintiff must overcome before bringing an international claim. Although state responsibility arises immediately from the original act of the judiciary or other government official, the alien cannot bring a claim in an international tribunal until he or she satisfies the rule. Article 1121, on the other hand, not only waives the alien's requirement to first seek local remedies but also requires the alien to give up the opportunity to seek local remedies. While the traditional rule treats local remedies as a burden on the alien that the alien is obligated to pursue,[179] Chapter Eleven apparently assumes that local remedies are a benefit that the alien must give up. Article 1121 seems to be aimed more at preventing double recovery than waiving a procedural bar. The *Loewen* tribunal took this difference in assumptions to mean that Article 1121 "is not about the local remedies rule."[180] Another understanding of this difference is that perhaps the parties did not fully understand the implications of Article 1121 when they included it. Regardless of the drafters' underlying assumptions about the local remedies rule, however, the language of Article 1121 is still an express waiver of the rule.

CONCLUSION

As the preceding discussion demonstrates, the tribunal's primary mistake was segregating the requirement to appeal adverse judgments from the local remedies rule and calling it a separate, substantive finality requirement. This error led to the tribunal's failure to consider whether Article 1121 waives the local remedies rule in its entirety. Instead, the tribunal came to the incorrect conclusion that even if Article 1121 waives the local remedies rule—which is procedural—it cannot waive the finality requirement for primary denial of justice cases—which is substantive. Additionally, the opinion was written in a confusing way, leaving it unclear which standards the tribunal was applying.

But that leaves the question of why the tribunal made these errors. It was surely not an issue of haste or mistake. Inadvertence seems implausible in light of the fact that the tribunal was composed of expert arbitrators who had

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[179] *See, e.g.*, FREEMAN, *supra* note 13, at 404 (noting that under the local remedies rule, a claimant's complaint will be rejected if "*the claimant has failed to exhaust his local remedies*") (emphasis in original).

[180] *Loewen*, 42 I.L.M. ¶ 161, at 837 (quoting Professor Greenwood and Sir Robert Jennings).

several years to consider the issues.[181] Moreover, even if the tribunal had insufficient time, there was no reason why it could not have avoided these issues altogether. Most obviously, the tribunal could have stopped with its decision on the continuous nationality issue. Instead, it spent multiple pages discussing the substantive standards of denial of justice under Article 1105 and the scope of the local remedies rule under all of Chapter Eleven, presumably intending to contribute to the international community's understanding of how these longstanding international rules apply under NAFTA. Thus, the tribunal's incorrect decisions must have been deliberate.

As such, the tribunal's mischaracterization of the local remedies rule most likely stemmed from its desire to vindicate the local remedies rule in NAFTA jurisprudence while avoiding a head-on confrontation with Article 1121. According to the tribunal, if Chapter Eleven had no exhaustion requirement,

> it would encourage resort to NAFTA tribunals rather than resort to the appellate courts and review processes of the host State, an outcome which would seem surprising, having regard to the sophisticated legal systems of the NAFTA Parties. Such an outcome would have the effect of making the State potentially liable for NAFTA violations when domestic appeal or review, if pursued, might have avoided any liability on the part of the State. Further, it is unlikely that the Parties to NAFTA would have wished to encourage recourse to NAFTA arbitration at the expense of domestic appeal or review . . . .[182]

In short, the tribunal felt that Chapter Eleven could not function without an exhaustion requirement.

Even though the tribunal knew Chapter Eleven needed an exhaustion requirement, it also understood that the parties waived the local remedies rule in Article 1121. In this view, the *Loewen* decision was most likely the tribunal's way of telling the United States that it needed to do something because, whether the NAFTA parties had intended it to do so, Article 1121 waived the local remedies rule. The tribunal basically told the United States: "There is no exhaustion requirement in Chapter Eleven. You got lucky *this* time because of continuous nationality, but *next* time you better be ready to

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[181] The United States first suggested that Loewen failed to satisfy a separate finality requirement in February 2000, the tribunal specifically deferred on the issue in January 2001, and the final award was released in July 2003. *See supra* notes 43–44, 53–55 and accompanying text. Therefore, the tribunal had at least two and a half years to consider the issue.

[182] *Loewen*, 42 I.L.M. ¶ 162, at 837.

pay for the errors of a state trial court." Arguably, this is a worthy policy goal: The tribunal decided to take a more incremental approach rather than imposing liability on the United States due to a waiver of which it might not have been fully aware. It gave the United States—and the other NAFTA parties—a chance to consider the true meaning of Article 1121 so that it could react accordingly.[183] Had the tribunal imposed liability on the United States this time, it may have provoked a backlash against NAFTA.[184]

Yet this still does not answer the question of why the tribunal established an obviously flawed finality requirement when it had other options that would have achieved the same result. For example, it could have held that Article 1121 waives the local remedies rule, but still ruled for the United States because of the nationality issue, thereby ignoring the "finality" requirement altogether. Alternatively, even if the tribunal wanted to keep its finality requirement, it could have held that its discussion of finality was mere dicta. Either of these options would have sent the United States the same message.

One possible answer to the "why" question is that the tribunal bowed to public pressure because it hoped to allay the fears of those critics who argued that Chapter Eleven, without some sort of exhaustion requirement, would turn NAFTA tribunals into supernational courts of appeals, which would in turn harm the United States' national sovereignty.[185] Other than public pressure, perhaps the only answer is that there is no rational reason for the tribunal's decision. Regardless of the reasons, *Loewen* was definitely a step in the wrong direction. *Loewen* leaves us with a separate finality requirement and more uncertainty: We now live in a world in which future explicit waivers of the local remedies rule may not—and perhaps *cannot*—completely waive the local remedies rule.

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[183] For several possible courses of action that the United States could take, see *supra* note 158.

[184] For a few examples of the flavor of the discontent that might have resulted if the tribunal had found the United States liable in *Loewen*, see the sources cited in *supra* note 7.

[185] *See, e.g.*, sources cited *supra* note 7.

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