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NAFTA Chapter 11 Investor-State Cases: Lessons for the Central America Free Trade Agreement

MAJOR FINDINGS

Foreign Investors Will Use the Investor-State System to Seek Compensation for Adverse Domestic Court Rulings:

A growing number of NAFTA cases seek to challenge adverse domestic court rulings. In the Loewen funeral home case, the NAFTA tribunal indicated that potentially all U.S. domestic court decisions, including those of the U.S. Supreme Court, could be subject to NAFTA review. This expansive holding led to protests from jurists and legal scholars. However, the investment terms in the proposed CAFTA would prevent complicated domestic court cases from being “reheard” in trade tribunals.

Increasing Questions Regarding the Constitutionality of Investor-State Tribunals:

Article III of the U.S. Constitution creates an independent judiciary. Congress cannot delegate the “essential attributes” of the judiciary to tribunals or other such institutions. Yet, just such a delegation appears to have occurred under the investor-state system. While organizations representing jurists have demanded an examination of the constitutionality of trade tribunals before the United States expands investor rules via new FTAs such as CAFTA, the administration has failed to provide such an analysis and instead simply replicated the flawed investor-state system in CAFTA.

Foreign Investors Can Bring “Regulatory Takings” Cases Not Allowed Under Domestic Law:

While the U.S. Supreme Court has long held that “mere diminution” in the value of property does not constitute a taking, NAFTA panels have held that “incidental interference” with the use of a property might constitute a takings. One “fix” the USTR attempted in CAFTA was to eliminate the phrase government actions “tantamount to” an expropriation that appears in the NAFTA text as activity requiring compensation. However, that change is merely cosmetic. The new FTAs still require compensation for “indirect” expropriations which is the operative term.

NAFTA Definition of “Investment” Does Not Conform to Compensable Property Under U.S. Law, CAFTA Makes Bad Situation Worse:

In NAFTA the definition of a compensable investment is not limited to the category of “real” property (i.e., real estate) implicated by regulatory takings jurisprudence under the U.S. Constitution. Indeed, most types of investments for which the U.S. government could be sued under NAFTA generally constitute intangible “personal” property that would not be eligible to establish the existence of a regulatory takings claim under U.S. law. NAFTA panels have extended this textual definition further in deciding that domestic court decisions, “market access” and “market share” are compensable investments. CAFTA negotiators failed to heed the calls of Congress to provide “no greater substantive rights” to foreign investors than U.S. firms, and CAFTA expands the investment category by including: “the assumption of risk,” “expectation of gain or profit,” intellectual property rights, as well as “licenses, authorizations, permits” increasing U.S. liability and putting more local government actions in jeopardy.

Potential Cost to the Taxpayers Could Reach the Billions:

In the first 11 years of NAFTA, with only 11 cases decided or settled, investors have succeeded five times with at least some of their claims and \$35 million in public funds have been paid in compensation to foreign investors by governments. As an increasing number of cases are filed, billions in taxpayer dollars are being sought by NAFTA firms. Additionally the costs of defending cases are mounting. With 10 cases completed or pending against the United States, and just one case costing \$3 million to defend, U.S. taxpayers may be billed an approximate \$30 million for lawyers fees alone. If CAFTA were to be approved by Congress and go into effect, the liability and costs of the investor-state system will increase further.

The Investor-State Mechanism Eviscerates the Sovereign Immunity Shield: NAFTA's Chapter 11 and CAFTA's proposed investor protections include no sovereign immunity shield. This constitutes a radical revision of longstanding U.S. sovereign immunity protections. As one legal scholar put it, "[b]y assenting to the terms of NAFTA, the United States, Canadian and Mexican governments essentially have waived whatever rights of sovereign immunity they may have enjoyed prior to signing." That foreign investors can sue the federal government when domestic citizens and firms are barred from bringing such suits is yet another example of how foreign investors are granted greater rights than U.S. businesses operating under U.S. law.

State and Local Governments Are Not Safe From the Reach of Investor-State Tribunals: Not only have federal policies been challenged by investors in NAFTA Chapter 11 tribunals, but an increasing number of actions taken by state, provincial and municipal governments have been challenged as well. These include state and local land use decisions, state environmental and public health policies, adverse state court rulings and state and municipal contracts. While the federal government is liable for any compensation awarded in investor-state tribunals, federal governments have a variety of avenues under domestic law to pressure state and local governments to alter their policies to reduce or avoid such liability.

Public Disputes, Private Tribunals: When investors demand taxpayer funds as compensation in investor-state tribunals, the cases are heard in arbitration bodies, which were designed to arbitrate private cases between contractual parties in narrow commercial disputes. Now, however, these private arbitral bodies are dealing with significant issues of public policy. While the CAFTA text provides for such tribunal proceedings to be open to public observation (if interested parties can afford to fly to distant venues to observe), citizens still cannot be party to a suit. Even the ability to submit an amicus brief is at the discretion of the panel. Under NAFTA, these cases can still be closed to the public upon the demand of the plaintiff corporation.

Threat of Investor-State Challenges Chills Public Interest Policies: Threatened cases continue to chill public interest policies. In 2004, a proposal by New Brunswick, Canada, to develop its own public auto insurance program in response to skyrocketing rates was scuttled after it was noted that the idea could prompt legal action on the part of foreign firms that might consider a public auto insurance plan an "expropriation" of their market share under NAFTA. It is impossible to calculate the real toll of threatened investor-state cases because communication regarding such cases most often takes place behind closed doors.

Number of Investor-State Cases Against Public Services Could Increase: The UPS case against the Canadian Postal Service encapsulates one of the most disturbing trends in the NAFTA cases taken as a whole, which is that some corporations are utilizing these rules to carve out more favorable market conditions for their firms. If the UPS suit is successful, few public services offered on a competitive basis would be safe from a NAFTA challenge of this type. CAFTA contains no language to safeguard nations from this type of case.

Environmental Text Has Not Protected Investor-State Environmental Measures: The provisions in NAFTA Chapter 11 purporting to protect the environment have been given such short shrift by NAFTA investor-state tribunals as to render them meaningless. In the Metalclad toxic waste case, there was no evidence that the tribunal even considered Chapter 11's environmental provisions before reaching a final decision. In the S.D. Myers PCB case, Canada's obligations under an environmental treaty that regulates trade in hazardous waste, called the Basel Convention, was considered by the NAFTA tribunal, but in the end was completely discounted. Nothing in CAFTA remedies this problem.

No Appeals in NAFTA, Appellate Proposal for CAFTA Deeply Flawed: There is no standing appellate body or other mechanism for appealing a NAFTA investor-state tribunal ruling. Thus NAFTA signatory governments are subject to adhoc rulings by an ever changing cast of adhoc panelists. The result has been contradictory rulings on a variety of issues. The Bush administration is working on a proposed framework for an appellate mechanism for CAFTA. While the 2002 Fast Track statute required such a mechanism to establish "coherence," the administration proposal calls for an adhoc appellate mechanism drawing panelists from a roster, not a standing appellate body. The lack of permanent professional staff will ensure that panels will continue to strike out on their own in interpreting the complex investment rules, a recipe for further arbitrary, contradictory rulings, which will be out of step with U.S. law and jurisprudence. Worse, the proposal eliminates the narrow, domestic court review allowed of some investor-state cases.