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Cover Page Footnote
Ai-Li Chiong-Martinson graduated from Seattle University School of Law magna cum laude in May 2017, with a focused study in international law. Ms. Chiong-Martinson served as the Managing Editor for the Seattle Journal of Environmental Law. She would like to thank her family and friends for their unrelenting support and encouragement, as she pursued her interest in international business litigation and arbitration.

Environmental Regulations and the Trans-Pacific Partnership: Using Investor-State Dispute Settlement to Strengthen Environmental Law

Ai-Li Chiong-Martinson[†]

ABSTRACT

The highly publicized Trans-Pacific Partnership (TPP) trade agreement has reignited a long-running debate between environmentalists and free trade advocates about the impacts of the investor-state dispute settlement (ISDS) system on the global economy and environmental preservation. The ISDS provision potentially gives foreign investors the right to challenge domestic regulations intending to protect the environment if those regulations discriminate against foreign investors and result in substantial monetary loss to the investors' property. Critics of the TPP argue that we should learn from the troubling legacy of the North American Trade Agreement (NAFTA), which, according to critics, overwhelmingly favored investors over states and domestic environmental concerns. Given the similarities between the TPP and NAFTA, critics argue that the TPP will similarly favor the rights of foreign investors over environmental regulations. Proponents of ISDS argue that the ISDS system as a whole provides much needed recourse to investors, fosters economic development, and strengthens the rule of law. Furthermore, many proponents argue the TPP provides far greater protections than NAFTA to host-state governments regulating for the public good, and, nonetheless, NAFTA jurisprudence is not as investor-friendly as critics contend. The purpose of this article is to examine the relationship between ISDS and environmental regulations pursued by host-states in an effort to determine whether member countries can realistically enact legislation to protect the environment when they are signatories to the TPP.

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TABLE OF CONTENTS

INTRODUCTION

On October 5, 2015, following years of negotiations, the United States and eleven other Pacific Rim nations reached a final agreement on arguably the largest regional trade agreement in history – the Trans-Pacific Partnership (TPP).[1] The TPP is one of the most ambitious free trade agreements ever signed, aiming to foster trade, boost domestic growth, and forge closer relationships on economic policies and regula-

[1] Jackie Calmes, *Trans-Pacific Partnership Is Reached, but Faces Scrutiny in Congress*, N.Y. TIMES (Oct. 5, 2015), http://www.nytimes.com/2015/10/06/business/trans-pacific-partnership-trade-deal-is-reached.html?_r=0.

tion between the twelve participating member countries.[2] Although trade ministers have reached an agreement on the trade deal, this is only the first step in a looming and complex political fight; the twelve nations have two years to ratify or reject the pact, and the agreement will face months of scrutiny in Congress.[3] While numerous aspects of the TPP have become the subject of great contention, there is one facet of the agreement that has received an exorbitant amount of criticism – the investor-state dispute settlement (ISDS) provision.[4] In short, ISDS is a legal mechanism that gives foreign investors the right to challenge government regulations by suing host-state governments through ad hoc arbitration proceedings, rather than domestic administrative and judicial channels, on the grounds that the government violated the rights guaranteed to the investor under a particular trade agreement or treaty.[5] At its most basic level, ISDS enables a foreign investor to sue the government of a country where the investor does business if the government is signatory to a trade agreement that includes an ISDS provision, and the government implements regulations that violate the investor's rights as negotiated and established in the agreement.

Although ISDS mechanisms already exist in many other trade and investment treaties, the highly publicized TPP agreement has reignited a long-running debate between environmentalists and advocates of free trade about the impacts of ISDS on the global economy and environmental preservation. Both critics and proponents of ISDS tend to concede that the ISDS system has opened the door for corporations to sue state governments over newly enacted regulatory frameworks, such as those aimed at environmental protection and sustainability.[6] Where the critics and proponents differ, however, is in their assessment of the potential costs or benefits this modern right to arbitration will have on foreign investors, host-state governments, and the environment in general. The ISDS debate became a feature of mainstream political discourse following the ratification of the North American Free Trade Agreement (NAFTA) in the '90s, and has recently been revived on account of the TPP and the 2016 presidential election. As governments and policy mak-

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[2] *TPP: What is it and why does it matter?,* BBC, http://www.bbc.com/news/business-32498715.

[3] Mara Liasson, *Obama Begins Sales Pitch To Congress On Trans-Pacific Partnership*, NPR (Oct. 06, 2015), http://www.npr.org/2015/10/06/446370835/obama-begins-sales-pitch-to-congress-on-trans-pacific-partnership.

[4] Alan Morrison, *Is the Trans-Pacific Partnership Unconstitutional?*, THE ATLANTIC (Jun. 23, 2015), http://www.theatlantic.com/politics/archive/2015/06/tpp-isds-constitution/396389/.

[5] Lisa Johnson, Lisa Sachs and Jeffrey Sachs, Columbia Center on Sustainable Development, CCSI Policy Paper, *Investor-State Dispute Settlement, Public Interest and U.S. Domestic Law* (May 2015), *available at* http://ccsi.columbia.edu/files/2015/05/Investor-State-Dispute-Settlement-Public-Interest-and-U.S.-Domestic-Law-FINAL-May-19-8.pdf.

[6] Tamara L. Slater, *Investor-State Arbitration and Domestic Environmental Protection*, 14 WASH. U. GLOBAL STUD. L. REV. 131 (2015).

ers become increasingly focused on protecting the environment, the number of environmental regulations that impact foreign investors will most likely intensify, resulting in an increase in ISDS claims brought by investors against host-states.[7] For all of these reasons, the ISDS debate has perhaps never been as relevant as it is today.

While there are strong arguments to be made from either side of the ISDS debate, much of the discussion surrounding the legitimacy of ISDS is based on somewhat skewed and limited information, rather than facts and balanced representations. On one hand, critics argue that the inclusion of ISDS provisions in trade agreements allow multinational corporations to override government policy and undermine state sovereignty.[8] Critics of the ISDS system often identify ISDS cases brought under the NAFTA where tribunals found in favor of foreign investors challenging the host-state's environmental regulations as evidence of the dangerous impacts ISDS can have on the environment.[9] According to critics, the ISDS provision in the TPP mirrors the provision in NAFTA, suggesting that the TPP will similarly empower foreign investors to freely challenge host-state environmental regulations.[10] On the other hand, according to ISDS proponents, ISDS does not limit the ability of governments to regulate, but rather gives foreign investors much needed redress if they are unfairly treated, representing a major advance in the fair treatment of foreign businesses and the peaceful resolution of disputes.[11] Rather than abdicating sovereignty, proponents of ISDS argue that entering into trade and investment agreements is an exercise of the sovereign's right to decide which obligations they wish to include in a treaty.[12]

The purpose of this article is to examine the relationship between ISDS, as a mechanism of free trade, and environmental regulations pursued by host-states in an effort to determine whether member countries can realistically enact legislation to protect the environment when they are signatories to the TPP. The overall utility of ISDS, or conversely the potential dangers it poses to the environment, depends on the resolution of a few essential questions. First, how should we assess whether ISDS is

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[7] *Id.*

[8] James Surowiecki, *Trade-Agreement Troubles*, NEW YORKER (Jun. 22, 2015), http://www.newyorker.com/magazine/2015/06/22/trade-agreement-troubles.

[9] *Setting the Record Straight: Debunking Ten Common Defenses of Controversial Investor-State Corporate Privileges*, PUBLICCITIZEN, http://www.citizen.org/documents/ustr-isds-response.pdf.

[10] Mark Weisbrot, *Lessons from NAFTA for the TPP*, HUFFINGTON POST: THE WORLD POST (Oct. 22, 2015), available at http://www.huffingtonpost.com/mark-weisbrot/lessons-from-nafta-for-th_b_8315512.html.

[11] Scott Miller and Gregory N. Hicks, *Investor-State Dispute Settlement: A Reality Check* CENTER FOR STRATEGIC & INT'L STUDIES (Jan. 2015), https://csis-prod.s3.amazonaws.com/s3fs-public/legacy_files/files/publication/150116_Miller_InvestorStateDispute_Web.pdf.

[12] Morrison, *supra* note 4.

an effective tool for balancing foreign investment and environmental protection? Second, what rights does the TPP preserve for investors and for governments intending to pass environmental legislation? Lastly, does or can the TPP protect the interest of both? Bringing together both sides of the ISDS argument, this paper concludes that the ISDS provision contained in the TPP has some significant differences from NAFTA, and that NAFTA investment arbitration jurisprudence isn't necessarily as pro-investor as some critics might believe. Given these determinations, it is the opinion of the author that the ISDS provision in the TPP actually has the potential to strengthen host-state environmental regulations, but only if there are a few significant reforms made to the existing system.

First, with the aim of enhancing legal certainty and predictability, the international community should make serious efforts to harmonize the rules governing international investment arbitration. Second, in the area of procedural reforms, foreign investors should always be required to carry the burden of paying the host-state's legal fees if the arbitrators decide the case is frivolous or rule in the government's favor; this would discourage investors from pursuing frivolous claims against host-states and strengthen the utility of investment arbitration as a more economical and efficient alternative to litigation. Finally, there must be greater transparency so arbitral decisions can begin to create precedent, or customary international law, which would provide the current system a framework for more consistent investor arbitration jurisprudence. With these procedural and substantive reforms, the ISDS provision in the TPP has the potential to protect and strengthen each member state's ability to enact or maintain environmental regulations.

This article seeks to facilitate a robust, even-handed, and careful discussion about ISDS and the environment, with a particular emphasis on the foreseeable benefits and dangers posed to future environmental regulations pursued by parties to the TPP. Parts II through V of this article establish the overarching historical and legal framework of the ISDS system, focusing specifically on NAFTA and the TPP, in an effort to contextualize the current ISDS debate. Part II explores the rise of ISDS and establishes the theoretical and doctrinal framework for ISDS that arose out of its historical context. Part III examines the legal framework applicable to ISDS, which consists of international trade law, investor arbitration, and free trade agreements. Building upon the legal framework, Part IV looks specifically at the Investment Chapters and ISDS provisions in both NAFTA and the TPP, comparing the important similarities and difference between the agreements. Part V shifts focus to environmental law disputes that were brought under the auspices of NAFTA in an effort to establish the current state of NAFTA arbitration jurisprudence.

Having established the historical and legal foundation for the TPP's ISDS provision, Part VI gets to the substance of the ISDS debate, summarizing the arguments for and against the ISDS system, consolidating the most compelling arguments, and proposing specific reforms that may potentially enable the ISDS system to actually strengthen environmental reforms and free trade.

I. BACKGROUND TO ISDS

In the 1980s and '90s, foreign-direct investment by private sector corporations emerged as a dominant source of capital for developing countries and remains one of the leading sources of economic activity in our increasingly borderless world.[13] As global economic activity has continued to expand, resulting in larger levels of international investment activity, international investment law has evolved into an increasingly relevant body of law for both the public and private sectors.[14] One of the most significant developments within the quickly expanding area of international investment law was the emergence of a variety of trade agreements seeking to promote foreign direct investment by providing foreign investors with greater security and transparency, such as multilateral "free trade" agreements formed between multiple countries and bilateral investment treaties formed between two countries. International investment treaties, whether bilateral or multilateral, offer substantive investment rights to corporations and contain provisions requiring states to arbitrate substantive violations, commonly known as ISDS provisions.

ISDS provisions enable foreign investors to file claims against governments in an international arbitration forum, as long as the investor is covered by a trade agreement between the investor's home country and the host country that includes an ISDS provision.[15] Perhaps the most well-known ISDS provision is found in the Investment Chapter of NAFTA (hereinafter Chapter 11), which specifically identifies the minimum standards for treatment of investors, enables corporations to sue host-state governments for laws or judicial decisions that infringe upon their rights, and establishes procedures for ISDS arbitration.[16] The text of Chapter 11 is largely reflected in both the TPP and the Transatlantic

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[13] Howard Mann and Konrad von Moltke, *NAFTA's Chapter 11 and the Environment: Addressing the Impacts of the Investor-State Process on the Environment*, INT'L INST. FOR SUSTAINABLE DEV., (1999), http://www.iisd.org/pdf/nafta.pdf.

[14] Susan D. Franck, *Conflating Politics and Development? Examining Investment Treaty Arbitration Outcomes*, 55 VA. J. OF INT'L L. 13, 18 (2014).

[15] Slater, *supra* note 6, at 133.

[16] Charles N. Brower II, *Investor-State Disputes Under NAFTA: The Empire Strikes Back*, 40 COLUM. J. TRANSNAT'L L. 43, 48 (2001).

Trade and Investment Partnership (T-TIP)[17] that is currently being negotiated.

Historically, investors had few options for resolving disputes arising from lost profits caused by government activity.[18] Prior to ISDS, the options available to investors were generally quite limited; the investor could accept lost profits as a cost of doing business, obtain political risk insurance, or rely on its home state to invoke its diplomatic rights on the investor's behalf.[19] In essence, prior to the emergence of ISDS, disputes involving government regulations and the resulting decrease in the value of property owned by foreign investors were treated as domestic conflicts.[20] Against this unsatisfactory backdrop, states and investors began using ISDS provisions to permit international arbitration of international investment law obligations.

In theory, ISDS was intended to benefit both host-states and foreign investors by leveling the investment playing field and fostering the neutral adjudication of investment disputes in a manner designed to minimize commercial risk and political risk, while maximizing the rule of law.[21] Through the establishment of a trans-national system for dispute resolution, foreign investors were able to avoid the potential difficulties they might face in a host-state domestic court system, such as ineffective domestic judicial systems or political influence.[22] Essentially, at its inception, the net objective of the ISDS system was to encourage foreign investment by protecting the rights of foreign investors and shielding host-states from incurring liability.[23]

The procedural qualities of the ISDS arbitration system are quite straightforward. Trade agreements that include ISDS provisions provide clear dispute resolution rights to foreign investors, such as the right to binding arbitration. In general, trade agreement with ISDS provisions include certain jurisdictional prerequisites that must be met before an investor is permitted to bring a claim against a host-state to a tribunal.[24] For example, most trade or investment agreements require an investor to first attempt to amicably resolve the dispute and comply with the proper

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[17] USTR, *White House Fact Sheet: Transatlantic Trade and Investment Partnership (T-TIP)* (June 2013), https://ustr.gov/about-us/policy-offices/press-office/fact-sheets/2013/june/wh-ttip.

[18] Franck, *supra* note 14, at 19.

[19] *Id.*

[20] Sergio Puig, *Recasting ICSID'S Legitimacy Debate: Towards a Goal-Based Empirical Agenda*, 36 FORDHAM INT'L L. J. 465, 478-79 (2013).

[21] Franck, *supra* note 14, at 20.

[22] William Park & Guillermo Aguilar Alvarez, *The New Face of Investment Arbitration: NAFTA Chapter 11*, 28 YALE J. INT'L L. 365, 369 (2003).

[23] Franck, *supra* note 14, at 20.

[24] *Id.* at 22.

notification requirements for instigating a dispute before the investor may bring an ISDS claim against a state.[25]

The substantive qualities of trade agreements involve promises from states to foreign investors that investors will receive certain minimal treatment, such as the right to freedom from expropriation and discrimination, and guarantees of fair and equitable treatment.[26] These rights are explicitly stated in the trade agreement, usually in the agreement's Investment Chapter, and are protected through the agreement's requirement that host states must refrain from violating the investor's substantive treaty rights. When an investor believes the host-state has violated its rights, the trade agreement permits direct redress against the host state through the ISDS mechanism if the challenged government action or regulation fails to meet certain standards of treatment required under the agreement and results in economic harm to the investor.[27] In sum, a cause of action brought under the ISDS provision of a trade agreement generally involves an investor's claim that the host state violated the investor's protected rights, and the violation caused monetary damage to the investor.

Before delving directly into the legal framework in which ISDS is situated, it is important to note that the ISDS system implicates various bodies of international and domestic law. While it is more straightforward to evaluate the ISDS system through one lens rather than many, whether it be from the perspective of environmentalists or trade advocates, the unique positioning of the ISDS system at the intersection of various bodies of law makes this almost impossible. Therefore, in continuing to build the ISDS framework as the foundation for the ISDS debate, the following three sections discuss ISDS from three important and interrelated standpoints: Part III discusses international trade law, free trade agreements, and investment arbitration; Part IV compares the Investment Chapters of NAFTA and the TPP; and Part V shifts to environmental law and NAFTA arbitration jurisprudence.

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[25] *Id*. at 20.

[26] Joseph Stiglitz, *In 2016, let's hope for better trade agreements – the death of TPP*, THE GUARDIAN (Jan. 10, 2016), http://www.theguardian.com/business/2016/jan/10/in-2016-better-trade-agreements-trans-pacific-partnership.

[27] Daniel J. Ikenson, *A Compromise to Advance the Trade Agenda: Purge Negotiations of Investor-State Dispute Settlement*, CATO INSTITUTE (Mar. 4, 2016), http://www.cato.org/publications/free-trade-bulletin/compromise-advance-trade-agenda-purge-negotiations-investor-state.

II. THE APPLICABLE LEGAL FRAMEWORK

A. International Trade Law and Free Trade Agreements

On October 30, 1947, twenty-three countries signed the General Agreements on Tariffs and Trade (GATT), which is considered to be the moment at which modern international trade law was first codified.[28] The GATT was the governing document for international trade until the parties to the GATT established the World Trade Organization (WTO) and incorporated the GATT therein.[29] The ultimate purpose of the WTO was to provide uniform trade laws, aid in resolving trade disputes, and to facilitate global trade.[30] Thus, to avoid disputes and assure uniformity, the WTO requires that all members treat other members with "most favored nation" status, meaning the lowest tariff rate one WTO member gives any country is the tariff rate that all WTO members shall receive.[31] There was one important exception to the "most favored nation" requirement explicitly written into the WTO regime – the specific exception for contracting parties to avoid the "most favored nation" requirement when entering into free trade agreements.[32] Under the WTO, free trade agreements are effectively permitted to allow for preferential treatment among contracting countries.

The WTO's allowance for preferential treatment in free trade agreements resulted in a rapid increase in the number of free trade agreements, growing international unrest about the terms of these agreements, and the rise of ISDS provisions. As of June 2014, 585 regional trade agreements have been reported to the WTO, with 379 in force.[33] As of 2012, there were nearly 3,200 bilateral trade agreements, and a comparable increase in multilateral trade agreements.[34] While some commentators maintain that free trade agreements provide stability for commercial transactions, many of the recently negotiated free trade agreements have sparked major protests by activists concerned about labor rights, environmental sustainability, exploitation of developing nations, and a range of other social issues.[35]

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[28] Raj Bhala, INTERNATIONAL TRADE LAW: INTERDISCIPLINARY THEORY AND PRACTICE, 641-42 (LEXISNEXIS, 3d ed. 2008).

[29] *Id.* at 607.

[30] *What is the World Trade Organization?*, WORLD TRADE ORG., https://www.wto.org/english/thewto_e/whatis_e/tif_e/fact1_e.htm (last visited Nov. 14, 2016).

[31] Bhala, *supra* note 29, at Chapter 11.

[32] According to GATT Article XXIV, "the provisions of this Agreement shall not prevent, as between the territories of contracting parties, the formation of a customs union or of a free-trade area …" General Agreement on Tariffs and Trade, Jan. 1, 1948, 2 U.S.T. 1583, 55 U.N.T.S. 187, https://www.wto.org/english/docs_e/legal_e/gatt47_01_e.htm.

[33] Regional Trade Agreements Gateway, WORLD TRADE ORG., http://www.wto.org/english/tratop_e/region_e/htm.

[34] Slater, *supra* note 6, at 136.

[35] *Id.*

B. Investment Arbitration: ISDS Provisions and Procedures

The applicability of international trade law to investment disputes is expressly derived from the terms of a free trade agreement and inclusion of an ISDS provision. For example, imagine that the United States and Chile are parties to a multilateral trade agreement that contains an ISDS provision, such as the TPP or NAFTA. An American company decides to invest in a timber manufacturer in Chile that will stimulate the Chilean economy by exporting timber products worldwide. The American company satisfies all government regulations, obtains the requisite permits, and invests millions of dollars to construct the facilities for timber production and manufacturing. Months after the company commences operations, the Chilean government enacts environmental regulations that make it nearly impossible for the company to pursue its business objectives. The regulations require foreign-owned timber companies to limit exports to a government-approved number and pay a 25 percent assessment on all revenues to fund domestic research into sustainable development projects. The American company believes that the new regulations damage the company's investment by minimizing expected profits, while providing Chilean timber companies with an unfair advantage to carry out their business without being limited by the regulations. Under international trade law, the American company would most likely pursue recourse through binding arbitration, bringing a claim against the Chilean government on the grounds that the government violated the company's rights under the applicable trade agreement.

While international trade agreements vary in their terms and content, foreign investors pursuing ISDS claims are generally permitted to elect to arbitrate before a variety of tribunals. The most commonly used forum for international investment arbitration is the International Center for Settlement of Investment Disputes (ICSID), and the second most commonly used forum is the United Nations Commission on International Trade Law (UNCITRAL).[36] Although each forum has its own set of rules, amendable by contract, the rules generally follow the same pattern and establish baseline requirements for each stage of arbitration, such as the proper method for filing pleadings, selecting a tribunal or challenging arbitrators, gathering evidence, and issuing a final award.[37]

Nearly all free trade agreements provide investors with a private right of action through ICSID arbitration, in accordance with the arbitration rules established by the ICSID or UNCITRAL.[38] Under both the ICSID and UNCITRAL rules, consent to arbitration occurs when a sov-

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[36] *Id.* at 138.

[37] Franck, *supra* note 14, at 22-3.

[38] Kate M. Supnik, *Making Amends: Amending the ICSID Convention to Reconcile Competing Interests in International Investment Law*, 59 DUKE L. J. 343, 351 (2009).

ereign state signs a free trade agreement that contains an ISDS provision allowing investors from another state to submit claims against it, such as in the timber manufacturer example discussed above.[39] The standard ISDS tribunal is comprised of three arbitrators, one appointed by each party to the dispute and the third appointed by the party-selected arbitrators.[40] Where an investment dispute is submitted under either the ICSID or UNCITRAL rules, as a default position, tribunals are required to decide disputes in accordance with the host state's domestic laws and the applicable "rules of international law."[41] Under both the ICSID and UNCITRAL rules, much deference is given to the arbiters in almost every aspect of the proceeding.

C. Free Trade Agreements: Substantive Rules and Principles

Arguably the most ambitious and controversial characteristic of free trade agreements, in terms of both their purposes and goals, is their attempt to strike a balance between protecting the rights of foreign investors and maintaining a narrow police powers carve-out for participating governments. On one hand, the overwhelming majority of trade agreements include provisions that promote non-discrimination and require host states to compensate investors in the event that expropriation or regulatory measures negatively impact the value of the investor's investment. On the other hand, most trade agreements also protect host-states from compensating investors if the government's conduct falls within the scope of the police powers carve-out for regulations designed to protect the public good. Additionally, as seen in the more recent trade agreements such as the TPP, drafters may even include specific provisions that address the environment and specifically the host's right to regulate in this area.[42]

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[39] *Id.* at 352.

[40] Nathalie Bernasconi-Osterwalder and Diana Rosert, *Investment Treaty Arbitration: Opportunities to Reform Arbitral Rules and Processes*, INT'L INST. FOR SUSTAINABLE DEV. (Jan. 2014), http://www.iisd.org/pdf/2014/investment_treaty_arbitration.pdf.

[41] Convention on the Settlement of Investment Disputes between States and Nationals of Other States, art. 42, Oct. 14, 1966, 17 U.S.T. 1270, 575 U.N.T.S. 159 [hereinafter ICSID Convention]. The United States is a Contracting State to the ICSID Convention. A list of signatories is available at https://treaties.un.org/pages/showDetails.aspx?objid=080000028012a925. The enabling legislation in the United States is embodied in 22 U.S.C. §§1650, 1650a (1982).

[42] *See* Office of the U.S. Trade Representative, Text of the Trans-Pacific Partnership, Chapter 9, Article 9.10(3)(d), available at https://ustr.gov/sites/default/files/TPP-Final-Text-Investment.pdf [hereinafter TPP]. According to this provision, a Party is not prevented from adopting or maintaining measure, including environmental measures:

> (i) necessary to secured compliance with laws and regulations that are not inconsistent with this Agreement;
>
> (ii) necessary to protect human, animal or plant life or health; or
>
> (iii) related to the conservation of living or non-living exhaustible natural resources.

At the most basic level, trade agreements provide two areas of protection for investors and one for the government. The first level of protection offered to investors is found in expropriation clauses, which prohibit host-states from expropriating or nationalizing an investor's investment. These clauses appear in almost all of the more than 2,200 bilateral and multilateral trade agreements, including NAFTA, the Dominican Republic – Central American Free Trade Agreement, and the TPP.[43] The second level of protection offered to investors is comprised in three extremely common non-discrimination provisions, namely the "National Treatment," "Most-Favored-Nation," and "Minimum Standard of Treatment" clauses.[44] Under the "National Treatment" clause, host-states must treat foreign investors no less favorably than domestic investors in similar circumstances.[45] In a similar vein, the "Most-Favored-Nation" clause guarantee investors treatment at least as good as that received by investors from any other foreign country.[46] The "Minimum Standard of Treatment" clause simply reiterates that investors are guaranteed "fair and equitable treatment."[47]

The most explicit protection provided for host-state governments is found in the form of exceptions to expropriation clauses. Under most free trade agreements, the host-state has the right to regulate for a public purpose, in a non-discriminatory manner, so long as compensation is duly paid to investors.[48] While this has traditionally been the full extent of the police powers carve out, modern ISDS jurisprudence has acknowledged that certain non-discriminatory regulations, when exercised within the state's police powers, might not require compensation when the government is acting solely in the public interest.[49] Furthermore, there is certainly an argument to be made that modern trade agreements have expanded the boundaries on what qualifies as a non-compensatory regulation by explicitly including provisions recognizing a host's ability to regulate on public welfare objectives, such as public health and the environment.

Having generally established the international trade law framework for the ISDS system, the following section will discuss and compare the rights reserved for both investors and host-states under NAFTA

TPP, Article 9.10(3)(d).

[43] *See* North American Free Trade Agreement, art. 1110, 1106, Dec. 17, 1992, 107 Stat. 2057, 32 I.L.M. 289 [hereinafter NAFTA]; TPP, *supra* note 42, art. 9.8.

[44] Anthony B. Sanders, *Of All Things Made in America Why are We Exporting the Penn Central Test*, 30 NORTHWESTERN J. OF INT'L LAW & BUSINESS 339, 355-7.

[45] *Id.* at 355.

[46] Rahim Moloo and Justin Jacinto, *Environmental and Health Regulation: Assessing Liability under Investment Treaties*, 29 BERKELEY J. INT'L LAW. 1, 57 (2011).

[47] NAFTA, *supra* note 44, art. 1105(1); *see* Sanders, *supra* note 45, at 356-7.

[48] Moloo, *supra* note 47, at 11.

[49] *Id.* at 16.

and the TPP. This comparative analysis will provide another layer of foundation to the ISDS debate concerning the potentially damaging or beneficial impacts ISDS may have on a host-state's ability to protect the environment.

III. A COMPARATIVE ANALYSIS: NAFTA AND THE TPP

This section develops a comparative analysis between NAFTA and the TPP, which will provide the foundation for analyzing whether environmental regulations will thrive or be chilled under the TPP. Because the TPP has largely been modeled after NAFTA, including the ISDS provision, many of the criticisms surrounding the TPP are based on the presumption that the TPP will follow in NAFTA's footsteps.

A. The North American Trade Agreement

In ratifying NAFTA, Canada, Mexico, and the United States resolved to "ensure a predictable commercial framework for business planning and investment,"[50] "increase substantially investment opportunities in their territories,"[51] and "create effective procedures for . . . the resolution of disputes."[52] Chapter 11 of NAFTA, arguably one of the most well known Investment Chapters of any free trade agreement, identifies the standards for treatment of investors and establishes procedures for arbitration of investor-state disputes. If an investor chooses to move forward with arbitration, the proceedings employ rules from either UNCITRAL or ICSID.[53] Under NAFTA, respondent states are responsible for the actions of both the state and their subdivisions that amount to a violation of any of the investor rights contained in Chapter 11.

1. Non-Discrimination

The first five guarantees in Chapter 11 of NAFTA provide investors with substantive non-discrimination rights. Articles 1102 and 1103 require NAFTA parties to treat each others' investors in accordance with the relative standards of "National Treatment" and "Most-Favored-Nation" treatment.[54] Article 1104 reaffirms that parties must accord investors and their investments the "better treatment" required by Articles 1102 and 1203,[55] while Article 1105 establishes a "Minimum Standard of

[50] NAFTA, *supra* note 44, at Preamble, para. 6.
[51] *Id.* art. 102(1)(c).
[52] *Id.* art. 102(1)(e).
[53] *Id.* art. 1117(1). "An investor of a Party, on behalf of an enterprise of another Party that is a juridical person that the investor owns or controls directly or indirectly, may submit to arbitration under this Section a claim that the other Party has breached an obligation."
[54] *Id*. arts. 1102, 1103.
[55] *Id.* art. 1104.

Treatment," mandating treatment in accordance with customary international law, including fair and equitable treatment.[56]

Article 1106 contains the fifth guarantee under Chapter 11, and is also where NAFTA's first reference to a fairly indiscrete police power carve-out is located. Article 1106 expressly prohibits certain "Performance Requirements," including requirements to export a given level or percentage of goods or services, or to achieve a given level or percentage of domestic content.[57] Following an extensive list of requirements, commitments, or undertakings that would constitute an illicit performance requirement under the agreement, the final paragraph of Article 1106 states that "nothing . . . shall not be construed to prevent any Party from adopting or maintaining measures, including environmental measures," that are "(a) necessary to secure compliance with the laws and regulations that are not inconsistent with . . . this Agreement; (b) necessary to protect human, animal or plant life or health; or (c) necessary for the conservation of living or non-living exhaustible natural resources."[58]

2. Expropriation and Compensation

Articles 1110 and 1106 comprise NAFTA's expropriation regime. Article 1110 explicitly permits expropriation and measures tantamount to expropriation so long as the host-state's conduct was done solely for a public purpose, on a nondiscriminatory basis, in accordance with due process of the law and the minimum standard of treatment required under Chapter 11, and upon prompt compensation equal to the fair market value for the expropriated investment.[59] Given the "public purpose" and "fair market value" requirements, Article 1110 has been described as strikingly similar to the Takings Clause of the Fifth Amendment of the U.S. Constitution, with the "public purpose" requirements taken directly from the text and the "fair market value" imported from Fifth Amendment jurisprudence.[60]

3. Arbitration Rules and Procedures

Section B of Chapter 11 secures the obligations under Section A by "establish[ing] a mechanism for the settlement of investment disputes that assures both equal treatment among investors and the Parties . . . and due process before an impartial tribunal."[61] Thus, under Section B, NAFTA parties have consented to investor-state arbitration; their consent

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[56] *Id.* art. 1105(1).
[57] *Id.* art. 1106(1)(a)-(b), 1106(3)(b).
[58] *Id*. art. 1106(6).
[59] *Id.* art. 1110(1)-(6).
[60] Jordan C. Kahn, *A Golden Opportunity for NAFTA,* 16 N.Y.U. ENVTL. L.J. 380, 412-13 (2008).
[61] NAFTA, *supra* note 43, art. 1115.

represents a standing offer to foreign investors to resolve their disputes via binding arbitration under the ICSID or UNCITRAL rules.[62] Although the arbitration rules selected by the investor will govern the proceedings, Section B modifies the rules by creating a limited right of audience for non-disputing NAFTA Parties, identifying the proper law for Chapter 11 disputes, and imposing strict limits on the form of interim and final relief that Chapter 11 tribunals may award.[63] In their final awards, tribunals may only grant compensatory damages plus interest, restitution of property, and the cost of arbitration.[64]

B. The Trans-Pacific Partnership

According to the website recently launched by the U.S. Trade Office for the sole purpose of explaining and clarifying the TPP, the purpose of the treaty's ISDS provision is to strengthen the rule of law in the Asia-Pacific region, deter foreign governments from imposing discriminatory or abusive requirements on American investors, and to protect the right to regulate in the public interest.[65] To accomplish these objectives, the TPP's Investment Chapter ensures that American investors will have effective remedies in the event of breach of their rights through the ISDS system.[66]

1. Non-Discrimination

Chapter 9, Section A of the TPP contains non-discrimination rules that are almost identical to the rights contained in the text of NAFTA, specifically the rights of "National Treatment," "Most Favored Nation," and "Minimum Treatment."[67] According to Article 9.4, the right of "National Treatment" requires member states to treat foreign investors no less favorably than the state treats its own investors in similar circumstances.[68] Article 9.5 is the TPP's "Most-Favored-Nation Treatment" provision, according to which "[e]ach party shall accord to investors of another Party treatment no less favorable than it accords . . . to investors of any other party."[69] Finally, Article 9.6 establishes the right to a minimum standard of treatment, requiring host-states to treat foreign invest-

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[62] Brower, *supra* note 16, at 48.
[63] *See* NAFTA, *supra* note 43, arts. 1120(2), 1127, 1129; *see also id.* at 51.
[64] *See id.* art. 1135(1).
[65] USTR, Trans-Pacific Partnership (TPP) Ch. 9, *available at* https://medium.com/the-trans-pacific-partnership/investment-c76dbd892f3a.
[66] *Id.*at Chapter Summary.
[67] *Id.*
[68] *Id.* art. 9.4.
[69] *Id.* art. 9.5.

ments in accordance with customary international law, including fair and equitable treatment, and full protection and security.[70]

Although the TPP largely resembles NAFTA in this area, the TPP expands upon NAFTA's rules of non-discrimination by clarifying key concepts in the non-discrimination and minimum standard of treatment obligations. In particular, the TPP clarifies that a legitimate public welfare objective is significant in the non-discrimination analysis. The TPP also expands upon NAFTA's performance requirements provisions in important ways. Similarly to NAFTA, the TPP prohibits certain performance requirements, such as requirements to export a given level or percentage of goods or services, to accord preference to goods produced in a signatory's territory, or achieve a certain level of domestic content. However, unlike NAFTA, the TPP adds a new element of protection for governments by permitting parties to adopt certain performance requirements, including environmental measures. According to the performance requirements provision, provided that the government measures are not applied in an arbitrary or unjustified manner, and do not constitute a "disguised restriction or international trade or investment," host-states are not prevented from adopted or maintaining measures, "including environmental measures":

> (i) Necessary to secure compliance with laws and regulations that are not inconsistent with this Agreement;
> (ii) Necessary to protect human, animal or plant life or health; or
> (iii) Related to the conservation of living or non-living exhaustible natural resources.[71]

In regards to the non-discrimination analysis and performance requirements, TPP expands NAFTA's police power carve-out by acknowledging the importance of public welfare objectives and allowing for host-states to adopt or maintain environmental measures as performance requirements.

2. Expropriation and Compensation

Similarly to NAFTA, the TPP permits expropriation for a public purpose, in a non-discriminatory manner, in accordance with due process of law, and upon prompt payment of adequate and effective compensation.[72] Where the TPP differs, however, is in its further elaboration upon this right. The TPP provides stronger safeguards to host-states by underscoring that countries can regulate in the public interest, including health,

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[70] *Id.* art. 9.6.
[71] *Id.* art. 9.9(1) and art. 9.10(3)(d).
[72] *Id.* art. 9.7.

safety, financial stability, and environmental protection. According to Annex 9-B, "Non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, do not constitute indirect expropriations, except in rare circumstances."[73]

3. General Welfare Regulatory Objectives

Unlike NAFTA, Article 9.16 of the TPP preserves the right for participating governments to adopt, maintain or enforce any measure, otherwise consistent with Chapter 9, which the government considers appropriate to ensure that investment activity within its territory is undertaken in a manner sensitive to environmental, health and other regulatory objectives.[74] Although this marks a significant departure from NAFTA, Article 9.15 only speaks to environmental or regulatory measures that are consistent with the TPP's Investment Chapter, which does appear to place the right to enact such legislation as secondary to the rights afforded to investors. Even so, Article 9.15 is notable because it is an independent acknowledgement of a host-state's right to regulate investment activity for environmental, health, and other general welfare purposes.

4. Arbitration Rules and Procedures

Finally, the TPP further diverges from NAFTA in regards to its procedural requirements for ISDS claims. The TPP raises the procedural standards by explicitly discouraging and requiring the dismissal of frivolous suits, and clarifying that the claimant initially bears the burden of proving all elements of its claims.[75] Additionally, the TPP departs from the generally inaccessible and closed-off nature of ISDS tribunals under NAFTA by requiring arbitration proceedings to be fully open and transparent, and allowing for the participation of civil society organizations and other parties not a direct party to the dispute.[76] If a party brings forth a preliminary question on the legal merit of a claim, the TPP also permits arbiters to award the prevailing disputing party reasonable costs and attorney's fees.[77] In regards to the final award, the arbiters have the final say in how the tribunal should award costs and attorney's fees incurred by the disputing parties in connection with the proceeding.[78]

Having established a comparative framework of the differences and similarities between NAFTA and the TPP, the following section will

[73] *Id.* annex 9-B.
[74] *Id.* art. 9.16.
[75] *Id*. art. 9.23.
[76] *Id.*
[77] *Id.* art. 9.22(6).
[78] *Id.*

examine several ISDS cases brought under NAFTA and, specifically, involving claims that the host-state's environmental regulations impinged on the investor's rights. Is the NAFTA arbitration jurisprudence as pro-investor as ISDS opponents maintain? If so, given the similarities and differences between the Investment Chapters in NAFTA and the TPP, will future ISDS claims brought under the TPP produce the same results as cases brought under NAFTA?

IV. NAFTA'S ISDS JURISPRUDENCE: INVESTOR RIGHTS AND ENVIRONMENTAL REGULATIONS

Although the decisions made by investment arbitration tribunals are not binding as precedent, each decision does, in fact, contribute to the growing body of arbitral jurisprudence that continues to guide the interpretation of the substantive principles of investment protection.[79] Investment treaty tribunals might use precedent in different ways, either citing, following, or distinguishing cases from earlier arbitral awards, but what has emerged is a static and constantly evolving overarching regime for international investment relations.

In the several decades that have passed since the emergence of NAFTA, foreign investors have pursued their fair share of ISDS cases under NAFTA's Investment Chapter. Over the years, the accumulation of ISDS cases has produced a considerable amount of arbitral jurisprudence, which has become increasingly relevant in the current debate over whether the ISDS provision in the TPP is likely to produce the same results as ISDS claims under NAFTA. Given the striking similarities and significant differences between NAFTA and the TPP, this section will discuss four popularly cited investment cases brought under NAFTA in an effort to build an understanding of NAFTA arbitration jurisprudence and extrapolate doctrine that will likely be applicable to future claims brought under the TPP. The cases discussed in this section involved environmental regulations and claims by foreign investors that the regulations violated their treaty-based rights.

Ethyl Corporation v. Canada is one of the first settled, and most popularly cited, NAFTA Chapter 11 cases.[80] In 1996, Ethyl Corp., an American corporation, initiated a Chapter 11 action against Canada following Canada's adoption of a law banning the import of the gasoline additive MMT.[81] Ethyl, which was the sole supplier of MMT in Canada,

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[79] Stephan Schill, *System-Building in Investment Treaty Arbitration and Lawmaking*, 12 GER. L. J. 1083, 1095 (2011).

[80] *Ethyl Corp. v. Canada*, Award on Jurisdiction, UNCITRAL (1976), available at http://www.italaw.com/sites/default/files/case-documents/ita0300_0.pdf.

[81] Howard Mann & Konrad von Moltke, International Institute for Sustainable Development, *NAFTA's Chapter 11 and the Environment: Addressing the Impacts of the Investor-State Process on the Environment* (1999), available at http://www.iisd.org/pdf/nafta.pdf.

claimed the Canadian government's ban on MMT violated the national treatment, performance requirements, and expropriation provisions under NAFTA. First, Ethyl argued the MMT ban violated the national treatment requirement in Article 1102 on the grounds that the ban on MMT imports discriminated against MMT in favor of Canadian producers of alternative octane enhancers.[82] Second, Ethyl asserted that the ban on MMT also created a de facto performance requirement, prohibited under Article 1106, to use Canadian sourced MMT or a Canadian produced alternative.[83] Finally, under the prohibition against expropriation, Ethyl argued that the ban on importing MMT erased about 50 percent of the corporation's business in Canada, constituting a de facto expropriation of its assets, good will, and future earnings.[84]

In response to Ethyl's claims, the Canadian government argued that the ban was motivated by health risks associated with manganese emissions as well as air quality concerns.[85] Additionally, Canada noted that the much of the United States and Europe had also banned the use of MMT as a gasoline additive. Ultimately, Canada's decision to ban the import and transport of MMT, as opposed to banning its use, weakened the government's position that health and environmental concerns were truly the primary motivations behind the regulation; the MMT ban clearly permitted domestic corporations to continue using and potentially manufacturing MMT, so long as importation and interprovincial transportation was not involved.

The *Ethyl* case is commonly brought into the ISDS debate as evidence supporting the assertion that investor-state arbitration essentially enables investors to compel governments to change their environmental laws if threatened with weighty arbitration fees and damages. Although no decision was ever reached by the *Ethyl* tribunal, anticipating that the UNCITRAL arbitration panel was likely to decide against it, the Canadian government reversed the ban on MMT import and transport and paid Ethyl $13 million in legal fees and damages.[86] While it is certainly true that NAFTA does not allow arbiters to require host-states to change their domestic laws, the result in the *Ethyl* case undoubtedly suggests that the mere opportunity to arbitrate disputes has the potential to influence governmental decisions, particularly in the realm of environmental and health regulations. In essence, a host-state may decide that the potential costs of losing in arbitration greatly outweigh the costs of reversing the

[82] *Ethyl Corp. v. Canada*, Notice of Arbitration, paras. 19-21, NAFTA, UNCITRAL (1998).
[83] *Id*. at para. 45.
[84] *Id.* at paras. 35-7.
[85] *Id.* at para. 10.
[86] Konrad von Moltke, *The Need for an International Investment Regime*, in TRADE AND ENVIRONMENT: DIFFICULT POLICY CHOICES AT THE INTERFACE 169 (Shahrukh Rafi Khan ed., 2002).

challenged regulation and negotiating a smaller settlement outside of arbitration.

In *Metalclad v. Mexico*, the claimant was a U.S. waste disposal company that had acquired property in the state of San Luis Potosi, Mexico, to operate a landfill in 1993.[87] Prior to the Metalclad's acquisition of the waste disposal plant, Mexico and the state of San Luis Potosi had struggle to cope with the extreme amounts of hazardous waste being generated each year, and opened negotiations with Metalclad to build a new hazardous waste landfill for the San Luis Potosi area.[88] The negotiations resulted in Metalclad receiving approval from the Mexican government to proceed with developing the landfill, which Metalclad completed and opened on March 10, 1995.[89] The dispute between Metalclad and the Mexican government arose shortly after the project's completion. Initially, the city of Guadalcazar, where the landfill was located, denied Metalclad's municipal construction permit, even though the permit had been approved thirteen months earlier.[90] A few months later, following failed negotiations between Metalclad and the State of San Luis Potosi to resolve the permitting issues, the Governor of San Luis Potosi issued an Ecological Decree declaring a Natural Area for the protection of rare cactus, which effectively, and permanently, precluded the operation of the landfill.[91]

Metalclad filed a Chapter 11 NAFTA complaint against the Mexican government in January 1997, asserting that the Mexican State of San Luis Potosi's ecological zoning law prohibited Metalclad from reopening the waste disposal plant that it has recently purchased, therefore constituting an expropriation of Metalclad's assets.[92] Metalclad submitted a claim for approximately $43 million on the grounds that actions of the local and state government wrongfully refused to permit Metalclad's subsidiary to open and operate a hazardous waste facility that Metalclad had built.[93] Perhaps the most important of Metalclad's assertions was that it had invested in the property in response to the invitation of Mexican officials, and that the project had met all of the government's relevant legal requirements.[94] Metalclad based its claim in Article 1100 of NAFTA's Chapter 11, arguing that the ecological zoning law amounted to expropriation, or indirect expropriation, of Metalclad's investment.

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[87] *Metalclad Corp. v. Mexico*, Notice of Claim, para. 4(c), NAFTA, ICSID Case No. ARB(AF)/97/1 (2000).

[88] *Id*.

[89] *Id*.

[90] *Metalclad Corp. v. Mexico*, Award, para. 50, NAFTA, ICSID Case No. ARB(AF)/97/1 (2000).

[91] *Id*.at para. 59.

[92] *Id*.

[93] Notice of Claim, *supra* note 88, para. 4(e).

[94] *Id*. at para. 4(c).

Applying the ICSID rules, the arbitration tribunal concluded that the Mexican government's conduct amounted to an expropriation and awarded Metalclad $16.7.[95] In its statement of award, the tribunal clarified that "expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property … but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use of reasonably-to-be-expected economic benefit of property ... "[96] The decision in Metalclad is notable because the tribunal seemingly adopted a broad interpretation of expropriation under Chapter 11, and held the Mexican government liable for the actions of its political subdivisions, namely the municipal agency charged with granting permits and the State governor who declared the ecological decree.[97]

Five years after the *Metalclad* ruling, the arbitration tribunal in *Methanex v. United States* declared that governments were exempt from paying compensation for bona fide regulations for the public good.[98] Methanex Corporation, a Canadian marketer and distributor of methanol, contended that a California ban on the use or sale of the gasoline additive MTBE in California, which uses Methanol as an ingredient, expropriated parts of Methanex's investments in the United States. According to Methanex, the California ban on MTBE violated Article 1110 and of Chapter 11, denying it fair and equitable treatment in accordance with international law, and denying it National Treatment under Article 1102.[99] California, through the United States, claimed that the MTBE ban was enacted to protect public health and to prevent water pollution.[100] In response, Methanex contended that the regulations were not justified on environmental grounds, but merely a creation of political lobbying by a major competitor in the gasoline additive market — the domestic ethanol industry.[101]

Applying the UNCITRAL rules and rejecting Methanex's claim, the tribunal emphasized the absence of assurances against regulatory change:

> [A]s a matter of general international law, a nondiscriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alias, a foreign investor or investment is not deemed ex-

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[95] Award, *supra* note 91, para. 131.
[96] *Id.*at para. 103.
[97] *Id.*
[98] *Methanex Corp. v. United States*, 44 I.L.M. 1345, Final Award, pt.IV, ch. F, 4 5-6 (NAFTA Arb. Trib. 2005), available at http://www.state.gov/documents/ organization/51052.pdf.
[99] *Id.* at pt.II, ch. D, 26-8.
[100] *Id*. at 33.
[101] *Id*. at 25.

> propriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation.[102]

Thus, in dismissing all of Methanex's claims, the tribunal clarified that Chapter 11 did not foreclose upon the possibility of non-compensable regulations so long as the regulation enacted was done for the public good and in accordance with due process of law. Unlike *Metalclad*, where the government appeared to have misled the investor, no such lack of due process or transparency was at issue in the claim against California's MBTE ban.

In *Glamis Gold, Ltd. v. United States*, having been frustrated in its efforts to mine a portion of the California desert in the vicinity of Native American sacred sites, a Canadian investor filed a Chapter 11 arbitration claim against the United States, alleging injuries relating to a proposed gold mine in southeastern California.[103] According to Glamis, it had invested approximately $15 million in gold mining operations, and spent 13 out of the 15 million on the project after receiving favorable signals from various regulatory bodies; however, following its investment in the mining project, California enacted regulations requiring complete backfilling for all open-out mines in California and for mining projects located within "one mile of any Native American sacred site," which Glamis contended constituted a violation of its rights under Chapter 11.[104] Glamis asserted that California and the Department of the Interior had "failed to approve the plan of operation and erected barriers that have effectively destroyed all economic value of Glamis Imperial's established mineral rights."[105]

The unanimous 355-page decision of the *Glamis* tribunal has made a particularly important contribution to NAFTA arbitration jurisprudence. First, in addressing Glamis' expropriation claim, the tribunal extensively analyzed the value of the mining project in light of the additional costs that would be required to meet the environmental criteria demanded by the California regulations, and concluded that the complained of measures would not constitute a sufficient economic impact

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[102] *Methanex Corp. v. United States*, Final Award, 44 I.L.M. 1345, pt.IV, ch. F, 4 5-6 (NAFTA Arb. Trib. 2005), available at http://www.state.gov/documents/ organization/51052.pdf.

[103] *Glamis Gold Ltd. v. United States*, Award, para. 1 (NAFTA Arb. Trib. 2009), available at http://www.state.gov/documents/organization/125798.pdf; *See also* Glamis Gold Ltd. v. United States, Notice of Arbitration, para. 7 (Dec. 10 2003).

[104] 55 CAL. PUB. RES. CODE § 2773.3(a) (West 2006); 2003 Cal. Stat. ch. 3 at 1.

[105] *See Glamis Gold Ltd. v. United States*, Notice of Arbitration at 7.

on Glamis to effect an appropriation of its investment.[106] The tribunal reiterated that the first factor in an expropriation claim analysis, namely sufficient economic impact, had not been met because the calculations from the enacted measures indicated that the project would maintain a significant position valuation.

Finally, in addressing Glamis' final claim, the tribunal concluded that Glamis had failed to meet the high threshold required to prove a breach of "fair and equitable standard".[107] The tribunal held that a violation of this right "must be sufficiently egregious and shocking – a gross denial or justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination, or a manifest lack of reasons …".[108]

Ultimately, both critics and proponents of ISDS find fodder for their arguments in the previous decisions of NAFTA tribunals, citing to examples of cases as either emblematic of the demise of environmental law or the strengthening of each host-states' ability to regulate environmental concerns unencumbered.[109] While NAFTA's earlier arbitral jurisprudence arguably appeared to favor investors, a closer look at the facts and more recent cases reasonably suggests that perhaps an investor-friendly reading of NAFTA jurisprudence is not entirely accurate. The facts of the earlier cases indicate that host-states could have done more to avoid misleading or disfavoring investors, and the more recent cases, such as *Glamis*, depict a much more challenging threshold for investors to meet if submitting a claim against a host-state's environmental policies or regulations.

Having established the historical and legal framework for ISDS, consisting of the ISDS system's doctrinal, substantive, and procedural background, a comparative analysis between the Investment Chapters of NAFTA and the TPP, and the current state of NAFTA arbitration jurisprudence, this discussion now turns to the substance of the ISDS debate. In considering the strongest arguments on each side of the debate, the question then becomes whether the ISDS provision in the TPP will serve to benefit the financial interests of foreign investors to the detriment of the local environment, or whether investment arbitration under the TPP has the potential to benefit both investors, host-states, and the environment.

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[106] *See* Glamis, Award, 8, at para. 17.

[107] *See id.* at para. 18.

[108] *See id.* at para. 22.

[109] *See* Lise Johnson et al., *Investor-State Dispute Settlement, Public Interest and U.S. Domestic Law*, CCSI Policy Paper 5 (2015), http://ccsi.columbia.edu/files/2015/05/Investor-State-Dispute-Settlement-Public-Interest-and-U.S.-Domestic-Law-FINAL-May-19-8.pdf; Jordan C. Kahn, *Striking NAFTA Gold: Glamis Advances Investor-State Arbitration*, 33 Fordham Int'l L. J 101 (2009).

V. THE ISDS DEBATE: SEARCHING FOR A MIDDLE GROUND

Given the divisiveness of the ISDS debate, it is easy to engage in a discussion about ISDS provisions, NAFTA, or the TPP from one side of the debate or the other. However, the purpose of this discussion is to engage with the multiple dimensions of the ISDS system, ranging from its history to current arbitration jurisprudence, so the various arguments can be contextualized and considered objectively. This section seeks to bring together the differing perspectives about ISDS by addressing some of the strongest arguments and opinions from environmentalists and free trade advocates alike.

A. Arguments Against ISDS

The most common concerns about ISDS involve the legitimacy of arbitration tribunals, arbitrator accountability, costs, transparency, award consistency, and more generally the preferential treatment of the interests of corporations over those of states.[110] For most critics, the vague substantive treaty standards, such as "national treatment" and "most favored nation," in addition to the ISDS mechanism through which they are interpreted and applied, have given foreign investors greater rights than they would otherwise enjoy under domestic law.[111] At the most basic level, critics view ISDS provisions as giving greater power to foreign investors than nations by permitting investors to file claims against governments and allowing multinationals to override environmental government policy, as was seen in the *Metalclad* claim.[112]

In allowing multinationals to override government regulations, critics argue ISDS provisions enable corporations to undermine state sovereignty. As described by Senator Bernie Sanders, the ISDS provision contained in the TPP undermines the sovereignty of the United States and "subverts democratically passed laws including those dealing with labor, health, and the environment."[113] Because ISDS enables foreign investors to challenge a host-state's police powers, critics further argue that ISDS results in a "regulatory chill," caused by the reluctance of host-states to impose new regulations when there is a risk foreign investors will challenge the regulations with investment arbitration.[114]

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[110] Supnik, *supra* note 38, at 355.

[111] Joseph Stiglitz, *In 2016, let's hope for better trade agreements – and the death of TPP*, THE GUARDIAN (Jan. 10, 2016), http://www.theguardian.com/business/2016/jan/10/in-2016-better-trade-agreements-trans-pacific-partnership.

[112] Slater, *supra* note 6, at 138.

[113] Bernie Sanders, *The Trans-Pacific Trade (TPP) Agreement must be Defeated,* http://www.sanders.senate.gov/download/the-trans-pacific-trade-tpp-agreement-must-be-defeated?inline=file.

[114] Lise Johnson et al., *Investor-State Dispute Settlement, Public Interest and U.S. Domestic Law*, CCSI Policy Paper 5 (2015), http://ccsi.columbia.edu/files/2015/05/Investor-State-Dispute-Settlement-Public-Interest-and-U.S.-Domestic-Law-FINAL-May-19-8.pdf.

Additionally, in determining whether the actions of the host-state constitutes a "regulatory taking" that requires compensation, or whether it falls within the host's "police powers carve-out" for non-compensatory policies designed to protect the public good, an international arbitration tribunal may determine the criteria for a regulatory taking according to the trade agreement and relevant arbitral jurisprudence, which may differ from what qualifies as a regulatory taking under the host-state's domestic laws. In this regard, some policies that would be exempt from compensation under domestic law may be compensatory under the terms of the investment treaty or prior arbitral decisions. Therefore, according to critics, the inclusion of an ISDS provision in trade agreements arguably gives foreign investors greater protections than those available under domestic law.

In regards to the financial benefits allegedly stimulated by free trade agreements and received by developing countries, some scholars argue that there is little conclusive evidence that free trade agreements actually promote foreign direct investment as proponents contend.[115] Furthermore, there is a similar lack of conclusive evidence that foreign investors actually need greater protections than domestic laws provide; while historically concerns about the impartiality of domestic judicial systems and politics may have been a valid concern, there appear to be little research or evidence to support this today.[116] In this regard, if investors and states are truly concerned about bias, it seems ironic that what appears to assuage their fears is a dispute resolution system that lacks uniformity, impartiality, and consistency. In the views of many, "the alleged neutrality of arbitration is . . . a myth."[117]

Critics of ISDS have suggested a range of ways to avoid these difficulties. The first is obviously to remove ISDS provisions from future agreements entirely. Stemming from this suggestion, in absence of ISDS, investors have access to political risk insurance that protects them from losses arising out of expropriation, breach of contract, and denial of justice; the same types of losses that are covered under investment treaties. In general, critics of ISDS contend that the system as a whole should be

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[115] *See* Jennifer Tobin and Susan Rose-Ackerman, *Foreign Direct Investment and the Business Environment in Developing Countries: the Impact of Bilateral Investment Treaties*, ASPEN INSTITUTE (William Davidson Institute Working Paper No. 587) (finding that there is weak relationship between BITs and foreign-direct investment).

[116] *See* Eric Neumeyer & Laura Spess, *Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries?,* 33(10) World Development, 1567–1585 (2005); MIT, *Are Foreign Firms Privileged by their Host Governments? Evidence from the 2000 World Business Environment Survey* (MIT Sloan Working Paper No. 4538-05) (providing mixed evidence concerning foreigners' need for international protection).

[117] Pia Eberhardt & Cecelia Olivet, *From Injustice: How law firms, arbitrators and financiers are fuelling an investment arbitration boom,* Corporate Europe Observatory Report Profiting, at 71 (2012), https://corporateeurope.org/sites/default/files/publications/profiting-from-injustice.pdf.

removed from its current stature as a supposed facilitator of international trade.

B. Arguments in Favor of ISDS

According to proponents of ISDS, arbitration provisions are a necessary and beneficial aspect of the international community's increasingly globalized trade regime. ISDS provisions strengthen the rule of law by requiring host-states to comply with their obligations and providing legal remedies for disputes, deters governments from imposing discriminatory or abusive requirements on foreign investors, and protects the rights of governments to regulate in the public interest by reserving the police power carve-out in both NAFTA and the TPP.[118] Essentially, proponents argue that the ISDS system simply gives foreign investors much needed redress if they are treated unfairly; by protecting the rights of foreign investors, free trade agreements make host-states more credible and, resultantly, promote foreign direct investment in less developed and accessible local economies. Counter to the assertion that ISDS results in a "regulatory chill," proponents argue that an international trade system without ISDS would result in an "investment chill" much to the detriment of the international community. Because ISDS provisions encourage foreign investors to invest in countries without robust legal systems, thereby fueling economic growth, foreign investments without the guarantee of investment arbitration would act as an important disincentive for continued foreign investment in the future.

In response to the argument that ISDS undermines state sovereignty, proponents counter that entering into international treaties of any kind is a core exercise of sovereign responsibility, rather than an abdication of sovereignty. States have historically negotiated and selected the terms of international agreements as an exercise of sovereignty. Furthermore, states have also consistently entered into a large variety of treaties, including trade and investment agreements, because it is not just a nation's sovereign right to do so, but also the nation's sovereign duty. In this regard, investment treaty arbitration ensures that states honor their obligations to other nations and to their foreign investors, thereby strengthening the rule of law both domestically and internationally.

Looking to the text of the Investment Chapters in NAFTA and the TPP, there is a strong argument to be made that the TPP significantly departs from the NAFTA arbitration regime. First, unlike NAFTA, the TPP explicitly states that a host-state's legitimate public welfare objec-

[118] Letter from Paym Akhavan, Associate Professor, McGill University Faculty of Law, et al., to Mitch McConnell, Senate Majority Leader, et al. (April 20, 2015) (on file with Fortier Chair In International Arbitration & International Commerce Law), https://www.mcgill.ca/fortier-chair/isds-open-letter.

tives may qualify as exceptions to the host-state's non-discrimination and minimum standard of treatment obligations. For example, the TPP provides stronger safeguards to host-states by underscoring that countries can regulate in the public interest, and by permitting host-states to adopt certain performance requirements, such as environmental measures, that are necessary to protect human, animal, or plant life or health, or are related to the conservation of living or non-living exhaustible resources. Second, the TPP also raises the procedural bar for foreign investors by explicitly stating that frivolous suits will be dismissed, clarifying that the claimant bear the burden of proving all elements of its claim at the outset of the proceeding, requiring transparency, and permitting the participation of civil society organizations. In general, the text of the TPP does in fact differ from NAFTA is significant ways, particularly where the host-state police powers are concerned.

Finally, when specifically looking at NAFTA arbitral jurisprudence, ISDS cases are generally quite rare and corporations do not always come out victorious when arbitrating environmental claims. While foreign investors are permitted to sue host-state governments for a number of reasons under NAFTA's Investment Chapter, recent NAFTA jurisprudence has clarified that governments will not be held liable for just any insignificant monetary loss, and that the threshold for establishing a Chapter 11 claim requires an egregious breach of the investor's rights.[119] Furthermore, in many of the cases where host-states have been required to pay damages to foreign investors, the host-state government generally made prior commitments to the foreign investor, which misleads the investor into believing that the investment was protected. Building upon this jurisprudence, the *Metalclad* tribunal emphasized that a nondiscriminatory regulation is not compensable unless the government has given specific commitments to the foreign investor that it would refrain from such regulation.[120] In light of NAFTA's recent jurisprudence, ISDS provisions arguably strengthen domestic environmental regimes by requiring governments to forecast and plan around environmental regulations before approving any plans submitted by potential foreign investors.

C. Comparing the Arguments

Considering these arguments together, it is clear that the debate between environmentalists and advocates of free trade is incredibly challenging because there are valid arguments on each side of the spectrum. On one hand, it is generally true that investor arbitration provides foreign investors, mainly multinational corporations, the ability to challenge le-

[119] *See Metalclad*, *supra* note 83; *Glamis*, supra note 90.

[120] *Metalclad Corp. v. United Mexican States* (Award), ICSID Case No. ARB(AF)/97/1 para. 103 (Aug. 30, 2000).

gal and regulatory systems and policy choices of the contracting states. Furthermore, early NAFTA jurisprudence attests to the fact that ISDS has been used to influence the ability of states to govern in the public interest, as seen in the *Metalclad* case. However, it is also true that it is the sovereign duty of states to enter into international treaties, and a robust investment arbitration system will likely reinforce the rule of law. In regards to NAFTA's troubling history, the more recent environmental claims indicate that investors challenging environmental, health, and safety regulations must meet a fairly high threshold to establish that a government's conduct was arbitrary, discriminatory, or would otherwise violate investment guarantees. Additionally, because the text of the TPP differs from NAFTA in that it does provide host-states with greater flexibility when it comes to environmental regulations, it is entirely possible that investors will face increasing difficulties in establishing a claim against host-states under the TPP.

In seeking to resolve the ISDS debate, it is the opinion of this author that the TPP has the potential to further the interests of both environmentalists and free trade advocates, through both its text and by building upon NAFTA jurisprudence.

D. Proposed Reforms

A comparative analysis of the texts of NAFTA and the TPP suggests many similarities, but a few important distinctions. As it relates to this discussion, the TPP mindfully addresses the ability of governments to regulate in the public interest, and includes several new provisions that specifically address environmental rights and protections. In regards to procedural changes, the TPP also explicitly places the burden of bringing the case against the government on the claimant, who must prove all elements of its claims. Additionally, unlike NAFTA, TPP permits governments to seek expedited review and dismissal of claims that are "manifestly without legal merit."[121] The final portion of this discussion will suggest a few additional measures that would transform the current investment arbitration system into one that can simultaneously pursue goals of environmental protection and foreign economic growth.

First, the international community should work towards developing one harmonized set of rules governing investment arbitration, in contrast to the currently fragmented system that permits investors to use a variety of different arbitration rules, such as UNCITRAL or ICSID. The multitude of free trade agreements, investment arbitration rules, arbitration forums, and arbiters themselves, clouds the entire investment arbitration system with confusion and inconsistency. The investment com-

[121] TPP, *supra* note 42, chapter 9, art. 9.22(4).

munity should work towards developing a model international investment law, which would include a unified collection of the common rights provided to investors, obligations of host-states, and a clear description of the police power carve-out for governments. In addition to a model international investment law, model rules should also be created for investment arbitration proceedings, which would define unified procedural and jurisdictional requirements for ISDS cases.

Second, as a procedural change, foreign investors should simply be required to carry the burden of paying the host-state's legal fees if the arbitrators rule in the government's favor. According to the UN Center on Trade and Development, which maintains a database of disputes arbitrated under ISDS provisions for all free trade agreements on record, of the forty-six cases that involved environmental disputes, seven were awarded in favor of the investor, four in favor of the state, twenty-five were settled, twenty-four are pending, and three are unknown.[122] These facts clearly indicate that a disproportionate number of these claims are being settled, likely the result of the prolonged length of these cases, and arbitration and attorneys' fees generally being extremely high. The fear is that governments without ample resources will settle with investors purely to avoid the costs incurred from arbitration. To diminish the growing trend in settlements, investment arbitration should require the losing party to pay all attorneys' fees, while splitting the arbitration fees with the other party. This procedural requirement has the potential to deter corporations from pursuing frivolous lawsuits, and encourage governments to refrain from reaching quick and expensive settlements.

Finally, addressing substantive reforms, legitimate environmental regulations should be recognized as a non-compensable regulatory taking, in both the text of free trade agreements and within customary international law. While it is true that the TPP carves out a much broader police power for governments regulating in the public interest, environmental regulations that are enacted out of this power should be explicitly recognized as non-compensable. For example, in the context of free trade agreements, drafters could include a provision that states environmental regulations are non-compensable and take precedence over the rights of foreign investors if that policy was found to be consistent with the findings and recommendations of a recognized international environmental body, such as the Intergovernmental Panel on Climate Change, or consistent with governing principles of customary international law.

[122] Slater, *supra* note 6, at 146.

CONCLUSION

A robust ISDS system has the potential to strengthen environmental regulations and increase foreign investment, particularly when applied to free trade agreements, such as the TPP, that have already expanded the power of host-states to regulate for environmental purposes. First, because NAFTA jurisprudence suggests that states might be liable under ISDS provisions if they renege upon "specific assurances" given to prospective investors, host-states should be encouraged to give more consideration to forecasting future environmental regulation before entering into agreements with investors.[123] Second, the expropriation provision in NAFTA and the TPP does not require compensation for all government regulations, only those that are not for a public purpose and administered in a discriminatory manner. Although this has been applied inconsistently to environmental regulations, NAFTA jurisprudence suggests that environmental regulations that have been adopted openly and applied equally to all investors do not require compensation.

In conclusion, if free trade agreements included a provision allowing any environmental policy to take precedent over the rights of foreign investors if the policy was found to be consistent with the findings and recommendations of a recognized international environmental body, such as the Intergovernmental Panel on Climate Change, governments would be more incentivized to engage with international recommendations and legislate in pursuit of environmental goals. For these three reasons, in the context of ISDS, it is beneficial for governments to be forthright, transparent, informed, and proactive when implementing or even considering environmental regulations.

[123] Jordan C. Kahn, *Striking NAFTA Gold: Glamis Advances Investor-State* Arbitration, 33 FORDHAM INT'L L. J. 101, 114 (2009).