

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

Panel: Recent Developments in NAFTA and CAFTA

*Andrea K. Bjorklund, Moderator**

The North American Free Trade Agreement (NAFTA)¹ was hardly the first regional trade agreement, rather the Association of Southeast Asian Nations (ASEAN) and Mercosur both preceded it, but NAFTA was, and is, one of the most controversial. From Ross Perot's warning of the "giant sucking sound" of jobs shifting from the United States to Mexico, to fears of labor abuses in the *maquiladoras*, to allegations of environmental hazards should Mexican trucks be allowed to operate in the United States, to worries on the part of Canadians that Canada would become the fifty-first state of the United States, predictions about the deleterious effects of NAFTA on all three member countries, Canada, Mexico, and the United States, were dire. One concern was that NAFTA would lead to a race to the bottom in terms of environmental and labor protections. Another was that trade and investment obligations represented an unwise abdication by the member states of sovereignty and, more particularly, of their ability to regulate to protect the health and safety of their residents.

Notwithstanding those criticisms, reducing trade and investment barriers remains the goal of most countries. The vehicles for those reductions are often investment treaties or regional or bilateral trade agreements, many of which contain an investment component. In fact, the number of investment treaties has skyrocketed since the late 1980s, increasing from 385 in 1989 to 2,392 in late 2004.² Although the Doha Round of multilateral trade negotiations appears to

* Andrea K. Bjorklund is an Acting Professor at the University of California, Davis, School of Law. She teaches courses in international arbitration and litigation, international trade, conflict of laws, and contracts. Ms. Bjorklund was an attorney-adviser in the Office of the Legal Adviser at the U.S. Department of State, where she defended the United States in investor-State arbitrations brought under Chapter Eleven of NAFTA. She has also served as Senior Counsel to Commissioner Thelma J. Askey at the U.S. International Trade Commission and has published numerous scholarly works on NAFTA.

1. North American Free Trade Agreement, Dec. 8, 1993, U.S.-Can.-Mex., 107 Stat. 2057, 32 I.L.M. 289.

2. United Nations Conference on Trade and Development (UNCTAD), *Recent Trends in International Investment Agreements*, UNCTAD/WEB/ITE/IIT//2005/1, <http://www.>

have stalled, as have negotiations for a Free Trade Area of the Americas, regional trade agreements continue to be the focus of inter-governmental negotiations.

NAFTA entered into force in 1994. Just over ten years later, the United States signed DR-CAFTA, another Western-hemisphere multilateral agreement, whose members, in addition to the United States, are Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and the Dominican Republic. Many of the concerns expressed by critics of NAFTA also animated critics of CAFTA and the many other free trade agreements the United States concluded in the years between NAFTA and CAFTA.

Over twelve years of experience with NAFTA should make possible a real, rather than a rhetorical, assessment of the effects of free trade agreements. Would governments continue to enter into trade and investment agreements if they did not confer some benefits? To what extent are the critics right about negative effects on public health and welfare? Have free trade agreements prevented the passage of more stringent environmental protections? How have free trade agreements affected domestic politics on the federal, state, and local levels?

These are not questions with easy or pat responses. However, the panelists have undertaken to attempt to give some answers by analyzing NAFTA-related trade and investment disputes that were resolved by international tribunals and the implementation and effects of those decisions domestically. Meg Kinnear, Senior General Counsel and Director General of the Trade Law Bureau of the Government of Canada, provided an illuminating examination of the various kinds of dispute mechanisms available to the NAFTA governments and their nationals, and the effectiveness, or lack thereof, of those mechanisms. She also assessed the actual effects of NAFTA on "regulatory chill": the reluctance of governments to legislate for fear of violating international commitments by impeding trade or investment. Sergio Puig, a Mexican trade specialist and a J.S.D. candidate at Stanford Law School, gave a penetrating assessment of the effect of trade agreements, and in particular NAFTA, on the behavior of Mexican government authorities. He concluded that NAFTA has encouraged the development in Mexico of a desirable, legalized response to political crises. Todd Grierson-Weiler, a Canadian investment law specialist, cogently examined the renaissance of international economic law as evidenced by the spate of investor-state arbitrations in the past several years. In particular, he examined the development of the doctrines of good faith and transparency in the context of investment

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

arbitration, and the salubrious effect those doctrines can have on the states party to investment treaties.

The penetrating analyses of these scholars and practitioners address only some of the issues surrounding trade and investment agreements. Trends to date suggest that such agreements will continue to play significant roles in the foreign, economic, and social policies of both developed and developing countries. Indeed, our fourth projected speaker, Roberto Echandi, could not join us because he was named both Costa Rica's Ambassador to the European Union and the chief negotiator of the projected EU-Central American Free Trade Agreement. The domestic effects of these agreements are only part of the picture. As regional agreements proliferate, their relationships with each other and with the Marrakesh Agreements of the World Trade Organization will become more complicated and will warrant further scrutiny from panels such as this.

*Meg Kinnear, Panelist**

I have been asked to speak on the topic of "NAFTA, Rhetoric or Reality" but would like to first start with the caveats that the views I express are personal, and may or may not coincide with those of the government of Canada. Secondly, not only are they personal views, but they are also the views of a lawyer. I recognize that while lawyers may have something to say about rhetoric, and hopefully something to say about reality, they are not always expert in many of the related disciplines that might be useful in such a study. Thirdly, I recognize that people have different perspectives and different assessments on whether NAFTA is delivering the goods. Fourthly, it is incredibly difficult to isolate the impact of NAFTA. Specifically, it is almost impossible to come to a conclusion that says, "But for NAFTA, here is what the world would have looked like." That is because we are in this incredible, complex environment where many different things play a role: peso crises, currency issues, political policy and elections. There are so many variables that play into it that a final conclusion is hard to arrive at. Finally, have in mind a fair expectation of NAFTA. To my mind, free trade agreements are a useful policy tool, but just one policy tool. So a rhetoric that says they are

* Meg Kinnear is the Senior General Counsel and Director General of the Trade Law Bureau, a joint unit of the Departments of Justice and International Trade Canada. In that capacity she has appeared as counsel before international trade dispute panels, participated in the negotiation of trade agreements and advised on Canada's international trade obligations. In 2002, Ms. Kinnear was the Chair of the Negotiating Group on Dispute Settlement for the FTAA. Prior to joining the Trade Law Bureau, Ms. Kinnear was Executive Assistant to the Deputy Minister of Justice, from Oct. 1996 – Apr. 1999. Ms. Kinnear has written various publications and has also spoken at a variety of conferences on matters related to dispute settlement in international trade, in particular NAFTA Chapter 11.

disappointing should be analyzed to see if it is based on a fair expectation.

For those of us who deal with the minutiae of trade agreements, it is often difficult to understand how such dry and technical text can produce so much exciting rhetoric. A free trade agreement, by definition, is a very mechanical document. It deals with some really important things for the people it affects, but otherwise, it is a pretty basic document. Issues such as the elimination of tariffs, rules of origin, and customs administration are all technical things that many would expect to be very boring and non-controversial on the face of things. In addition, the foundational principles of these agreements are quite universal. They are things like national treatment, requiring that goods, services or investments from one country not be discriminated against by the other trade partner on the basis of nationality. To me, this seems to be a fairly basic principle of fairness, and, sometimes I wonder how such complicated rhetoric can result from such very basic principles.

The rhetoric around NAFTA started from its earliest days and, in fact, I might say it started even before NAFTA's inception. The Canada–United States Free Trade Agreement,³ which preceded NAFTA, caused many of these issues and a lot of the same concerns to be examined in the public media. So it comes as no surprise that in 1991, when they announced that Canada, Mexico and the United States were jointly negotiating the North American Free Trade Agreement, that kind of rhetoric continued. I think there are at least five big areas that raised intense discussion: economic effects, effect on sovereignty, effect on employment, effect on the environment, and the effect on immigration.

In terms of economics, there was a lot of concern about whether the economies of Canada and Mexico could actually stay on an even keel with the United States. That kind of rhetoric probably has not withstood the test of time. There is consensus that all three partners have become more competitive and that in turn they have increased their productivity. Since NAFTA, our Canadian merchandise trade has increased 122%, our trade in services is up 6% a year, our foreign direct investment has doubled from our two NAFTA partners⁴, and there are similar statistics from the United States and from Mexico. I think that goes right back to the fundamental theory behind the Free Trade Agreement. Overall trade agreements are beneficial, but the benefits are not universally felt. It is recognized that there are what people call “winners” and “losers,” especially at the beginning

3. Canada-U.S. Free Trade Agreement, U.S.-Can., Jan. 2, 1988, 19 U.S.C. § 2112.

4. NAFTA @ 10, 11 (John M. Curtis & Aaron Sydor eds., Minister of Public Works and Government Services Canada, 2006).

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

of an Agreement's entry into force. The whole idea is that everyone will do what they do best and that overall it will result in net benefit.⁵ But there is no doubt that there are those who will question the benefits of free trade because their sectors have fared worse than others initially.

On the sovereignty front, the issue was what you might expect. In Canada, commentators asked questions like: are we going to be the fifty-first state; will we lose control over our currency; will we have an E.U.-type common currency; will we have the ability to maintain our independence in terms of our fiscal and monetary policy? There was a lot of concern about that, but I think that one can fairly quickly dismiss these issues. Obviously, free trade has not led to a political merger and it has not led to common currency. So the ability to maintain sovereignty and maintain the ability to make independent decisions does not seem to have been impacted by NAFTA in the way some were very concerned about in the beginning.

The next issue is the question of employment. Of course, employment is always one of the big selling points of a free trade agreement. At the beginning of NAFTA, Bill Clinton, who was then President, predicted that NAFTA was going to create more than 200,000 U.S. jobs in the first two years of its implementation.⁶ One should compare that prediction to one of the most famous pieces of NAFTA rhetoric: presidential candidate Ross Perot's talking about the giant sucking sound, which was good American jobs supposedly being moved to Mexico.⁷ Ironically, Ross Perot's own company announced last fall that it was going to set up a technology center in Guadalajara, Mexico, where it would employ at least 270 engineers.⁸ Among the reasons cited for the move were the lower salaries of engineers in Mexico, in addition to Mexico's strategic location with respect to Central and South America. In terms of broader statistics and how they compare to the anecdotes, the numbers basically show that there has been a very small net gain in terms of employment in Mexico, and the jobs created have mainly been in the export manufacturing sectors. There have also been a lot of jobs lost in the Mexican agricultural sector due in part to competition from large American

5. *Id.* at 9-10, 73-96.

6. JOHN J. AUDLEY ET AL., *NAFTA'S PROMISE AND REALITY* 9-10, 73-96 (CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE, 2004), available at <http://www.carnegieendowment.org/files/nafta1.pdf> [hereinafter *NAFTA'S PROMISE*].

7. Ross Perot with Pat Choate, *SAVE YOUR JOB SAVE OUR COUNTRY: WHY NAFTA MUST BE STOPPED NOW* 41-42, 47 (Hyperion Books 1993).

8. Elisabeth Malkin, *Company Ross Perot Built is Now Hiring in Mexico*, N.Y. TIMES, November 13, 2006, available at <http://travel.nytimes.com/2006/11/13/business/worldbusiness/13perot.html>.

agriculture businesses and subsidized agriculture. That controversy continues to this day.⁹

The United States probably has made a small net gain or stayed stable in terms of the number of jobs. In Canada, there was originally a reduction in jobs that seemed to be related to NAFTA, although now there seems to be a modest increase. So yes, there have been some employment gains. Numerically, productivity has increased, but it is neither the wildly negative scenario nor the wildly positive scenario talked about in the early days of NAFTA's inception. There are also more qualitative assessments relating to employment that are harder to make but are nonetheless important. There has been an increasing wage gap between highly skilled and low skilled workers, there has been a loss of rural agricultural jobs, and the latter has had an impact on communities. These and similar issues are harder to assess.¹⁰

The next hot button issue is that of immigration. Many proponents of NAFTA, including former Attorney General Janet Reno, originally argued that there would be an increase in jobs and the movement of some good jobs to Mexico; therefore, the whole problem of illegal immigration would be reduced or wiped out. And it seems fair to say that this has not happened following NAFTA. There is still a large problem of unauthorized immigration across the U.S.-Mexico border. Some studies estimate that unauthorized Mexican workers in the United States doubled between 1990 and 2000, and most of that growth was post-NAFTA, i.e. post-1994.¹¹ On the other hand, was this increase caused by NAFTA? There are numerous factors that are important, like historic migration networks between the United States and Mexico, the need for low-wage employees in the United States, and the lack of high paying jobs in Mexico. Another important factor is the stunning demographic statistics which show that the Mexican labor force grew by a million workers per year in the 1990s; that seemed to plateau around 2001. It is an almost impossible challenge for any economy to absorb that many people into the labor force and provide people with jobs.¹² At the end of the day, while NAFTA has not been a panacea for immigration problems, its implementation is part of a set of complex factors that affect immigration.

The debate surrounding the impact of NAFTA on the environment is not only

9. NAFTA'S PROMISE, *supra* note 6, at 11-35.

10. *Id.* See also, NAFTA @ 10, *supra* note 4 at 10, 105-122.

11. See, e.g., Philip Martin and Elizabeth Midgley, *Immigration: Shaping and Reshaping America*, 58 POPULATION BULLETIN 2, 29-31 (June 2003).

12. NAFTA'S PROMISE, *supra* note 6, at 39-44.

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

heated, but it is also very complex. President Clinton said NAFTA was “one of the greenest trade agreements” because it was the first to include a mechanism used in many American trade agreements — an environmental side agreement.¹³ On the other hand, there were critics who argued that NAFTA was going to be responsible for what they called a race to the bottom. This was meant to suggest that governments would reduce or eliminate environmental regulation in order to attract investment in business. Another common idea is that even if environmental standards were strengthened, the result would be polluters going to non-regulated or poorly regulated countries to continue polluting, and ultimately having an adverse effect on everybody. Again, if you look thirteen years forward, the record is a lot more complex, and I think that it is impossible to segregate the issues of causation and NAFTA.

There are, obviously, some difficult and scary outcomes. One of them, for example, is air pollution spikes on the Canada-U.S. and Mexico-U.S. border where 80% of the total NAFTA trade is done through truck transportation at border crossings. Similarly, there are studies that conclude that increased cross-border electricity trade due to NAFTA has led to increased carbon dioxide emissions. On the other hand, there are some interesting good news stories. For example, foreign direct investment increased in the Mexican cement and steel industries, resulting in some more efficient and less polluting technologies.¹⁴

Much rhetoric has surrounded the dispute resolution mechanisms. There are in fact three. There is the state-to-state or Chapter 20 mechanism,¹⁵ which is similar to the WTO’s mechanism. There is the Chapter 19 binational panel review for antidumping and countervailing duties¹⁶. And there is Chapter 11, which permits investor-state arbitration.¹⁷

In terms of Chapter 20, the basic state-to-state dispute mechanism, there was some rhetoric in the beginning. In particular, people were very concerned that NAFTA panels might overturn environmental measures taken by state and

13. North American Agreement on Environmental Cooperation, U.S.-Can.-Mex., 10 U.S.C. §3472, 32 I.L.M. 289 (1993).

14. NAFTA’S PROMISE, *supra* note 6, at 61-82.

15. North American Free Trade Agreement, Chapter 20: Institutional Arrangements and Dispute Settlement Procedures, U.S.-Can.-Mex., Dec. 17, 1992, 19 U.S.C. § 3431.

16. North American Free Trade Agreement, Chapter 19: Review and Dispute Settlement in Antidumping and Countervailing Duty Matters, U.S.-Can.-Mex., Dec. 17, 1992, 19 U.S.C. § 3432.

17. North American Free Trade Agreement, Chapter 11: Review and Dispute Settlement in Antidumping and Countervailing Duty Matters, U.S.-Can.-Mex., Dec. 17, 1992, 19 U.S.C. §3438.

municipal governments in the United States. The fact is Chapter 20 has been used very infrequently. There have been three cases in thirteen years,¹⁸ and there are a lot of reasons for this. One reason may be that an agreed-upon roster of arbitrators was very hard to finish. Another issue may be because when people think about starting disputes they may ask themselves, “Do I start in a NAFTA context where I have three partners? Or do I start in a WTO context where there are 145 parties?”

A more difficult situation deals with the use and effect of NAFTA Chapter 19. Chapter 19 is a very interesting device. It was inserted into the Canada-U.S. Free Trade Agreement at the insistence of Canada. In fact, at one point when Canada first put it on the table and the United States refused to agree to it, Canada walked away from the table; it was a deal breaker and almost dissolved the entire Canada-U.S. Free Trade Agreement. Chapter 19 is a mechanism whereby determinations by domestic agencies as to the imposition of antidumping or countervailing duties can be challenged before a binational panel, rather than before domestic courts. The binational panel is made up of five members. If there is a dispute between Canada and the United States, there will be two Canadians, two Americans, and a fifth panelist selected by lot. The reason for Chapter 19 comes from a very strong perception, certainly in Canada, and I suspect in Mexico as well, that American antidumping and subsidies determinations were imposed in a very protectionist manner and in a way that responded to domestic political pressures. Some Canadians felt they would never get a fair shot before U.S. agencies or courts. It was really a drop-dead issue in the Canada-U.S. free trade negotiations. It was then brought into the NAFTA and it has, compared to Chapter 20, been used quite frequently. There have been 110 cases.

Even binational panel review is potentially inadequate in hard cases. For Canada, the hardest cases to solve were the *Softwood Lumber* cases. Canada just negotiated a comprehensive treaty to solve the case, but a lot of issues came out of the Chapter 19 proceedings that caused people to be very concerned. In particular, the United States took the position that if you went to the binational panel and the panel determined the duties never should have been imposed in the first place, that decision had only prospective effect; the United States could keep all duties that had been wrongly imposed. If you took the same case to domestic court, you would get the duties back from day one. The result ought to be the same before either tribunal.¹⁹

18. See Sergio Puig's preceding article, Footnote 47.

19. JON JOHNSON, THREATS TO NAFTA CHAPTER NINETEEN ARISING FROM THE SOFTWOOD LUMBER DISPUTE (Goodmans 2005), available at <http://www.goodmans.ca/index.cfm?>

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

The final area of dispute settlement that I want to touch upon is NAFTA's Chapter 11 device of investor-state arbitration. The interesting thing about Chapter 11, compared to the other things I mentioned, is that all the other things were accompanied by rhetoric at the beginning of NAFTA, but people hardly noticed Chapter 11 investor-state arbitration. And that is why it is ironic that Chapter 11 has become one of the big issues that you read about in the popular media and has been accompanied by a fair amount of rhetoric. Here I think there are at least four main areas where the rhetoric has been centered. The first one is transparency. The second is regulatory chill. The third is the theme of lost sovereignty. And fourth is the whole issue of NAFTA Chapter 11 arbitration being a tool only for wealthy multi-national corporations.

On transparency, the concern basically is that these tribunals are operating behind virtual closed doors. These arbitrations were governed by private and commercial arbitration rules which allowed an investor or a government to insist that the matter be held in confidence. After all, one of the great things about confidentiality in arbitration has been that people could essentially agree to arbitrate away from the public view. It is a very different thing in the context of investor-state arbitration dealing with government issues. So the NAFTA parties have taken the steps that they can and have issued notes of interpretation²⁰ clarifying that there is no overriding duty of confidentiality. They have thus established that these arbitrations should be public, except for something specific like confidential business information. That is similar to the rules found in domestic courts in the United States or Canada. It seems to be appropriate and it seems to be working.

The next question is the whole question of regulatory chill. Regulatory chill is basically the concern that regulators will be so concerned about potential liability under Chapter 11 that they will be scared to even advance appropriate legislation. The concern, not surprisingly, comes mainly in the environmental and health areas. It is obviously a concern that is both difficult to prove and difficult to disprove. But I suggest that the evidence, to date, tends to disprove it. First of all, there have been many such regulations passed by the governments since NAFTA was put in place. Secondly, Chapter 11 of NAFTA contains various provisions that specifically give some precedence to particular environmental agreements that say

fuseaction =PublicationDetail&primaryKey=418.

20. MEG N. KINNEAR, ANDREA K. BJORKLUND & JOHN F.G. HANNAFORD, INVESTMENT DISPUTES UNDER NAFTA – AN ANNOTATED GUIDE TO NAFTA CHAPTER 11, Appendix 1, 3 (The Netherlands: Kluwer Law International 2006).

the agreements should not be construed to prevent people from becoming providers of social services, such as health care.²¹ There is also an Article in Chapter 11 that says it is inappropriate to encourage investment by lowering standards of environmental protection. So even the agreement itself takes specific measures to prevent regulatory chill. The other, perhaps more important point, is that no Chapter 11 case so far has found liability based on a country's environmental, health, or other social service regulation.

In regards to sovereignty, there is no evidence that countries will have to give up their ability to make policies because they have to adhere to international agreements. As in any kind of international agreement, a country makes an assessment and agrees to be bound by certain norms in exchange for having treaty partners bound by the same norms. This is in itself an exercise of sovereignty. The agreement is approved because the government thinks that it will be for the greater good.

Finally, there has been the whole question of whether NAFTA Chapter 11 gives too much power to multinational corporations. It is not just multinational corporations that are interested in these; a lot of smaller corporations and individuals also bring claims under NAFTA Chapter 11.

To conclude, I think that if you look at the evidence, and our experiences of the last thirteen years, NAFTA has neither been as bad nor as good as its respective detractors and advocates had originally contended. So perhaps a middle-of-the-road view is the best way to evaluate it.

Sergio Puig, Panelist

Please see Mr. Puig's article immediately preceding this panel for his views on how NAFTA has affected the development of Mexican politics. Mr. Puig's comments during this panel are not reproduced here as they are echoed in his article.

*Todd Grierson-Weiler, Panelist**

I should begin by saying that the views I express are my own personal views. It is important to keep in mind that investor claims against governments are a much

21. See, e.g., NAFTA, *supra* note 1, art. 104, 1101 (4), 1114.

* Todd Grierson-Weiler is a Canadian lawyer who specializes in investment treaty arbitration under the NAFTA and under investment protection treaties. Since 1999 he has served as counsel and consultant to numerous public and private sector clients on NAFTA Chapter 11, the Energy Charter Treaty and bilateral investment treaties. In 2006 Mr. Grierson-Weiler was named one of the world's "45 Under 45 Leading Lights" in International Arbitration by the Global Arbitration Review. He is published extensively on this topic, serving also as editor to numerous trade and business law publications. Please see Mr. Grierson-Weiler's extensive CV at www.toddweiler.com.

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

larger phenomenon than just NAFTA Chapter 11. Specifically, there are over 2,500 other treaties that contemplate some form of investor claims against a state.

In international law, states are traditionally regarded as the alpha and the omega; they write the law, they are actors of the law, and they are even adjudicators of the law. But over time the rights of private actors have either been, some say developed, others say recognized. Yet there is still some question as to exactly what those rights might be. There are three primary international law sources of these rights. There is customary international law, there are general principles of international law, and then there is treaty law. Private parties enjoy rights and those rights will take the form of one of those three sources. But they need a remedy, too. How exactly is it that they make use of a right that makes them whole under international law? There are really two ways of doing that. The traditional one is espousal of the claim, which is essentially where the home state goes to the other state and says: You did not treat my citizen well and I think we need to have a talk about this. I am not going to continue our international relationship until you talk about this or I am going to put a gun boat beside your lovely beach until you work this out.

So one way or the other the state can espouse a claim and, ideally, they will do it in a way that does not involve gun boats. The result of the espousal claim request could sometimes be one of arbitration involving, probably, a very wealthy and well connected individual who had the wherewithal to be able to convince its state to pursue its case. Traditionally, another espousal option was to settle these disputes in claims commissions. These mixed claims tribunals would hear a whole set of claims, which were often quite small. The most recent example of this would be the Iran/U.S. Claims Tribunal, which, contrary to popular belief, technically is actually still ongoing. As Judge Brower would tell you, "I am still a judge on the tribunal."

Another more recent example of the espousal approach is WTO dispute settlement. The WTO is considered an entity that only provides state-to-state dispute settlement, but what is the nature of the proceeding? Well, most often the nature of the WTO dispute settlement is a commercial dispute between business rivals championed by their "home" governments.

The other means of recourse, which is only about forty to fifty years old, is direct recourse to arbitration by an individual claimant against a respondent state. Originally such arbitrations were the product of a state making a contract with an individual private company, usually to mine minerals or develop oil, or some other sort of resources-based concession. The arbitration clauses often took the dispute

out of what would have been the local courts and put it somewhere else where both parties felt comfortable. And then about thirty or forty years ago, a related idea developed to take an existing treaty, which was known as a friendship, navigation, and commerce treaty (FCN), and add an arbitration clause to it. There is a commercial arbitration angle to investor-state settlement because they initially borrowed the mechanism wholesale from the private arbitration model. Instead of calling them modified FCNs, they started calling them BITS, Bilateral Investment Treaties, unless you are in Canada in which case you call them Foreign Investment Protection and Promotion Agreements (FIPA).

Whether you go by the espousal model or whether you go by this access to direct arbitration, the bottom line is the state remains the gatekeeper. The state remains the gatekeeper to espousal because the state will decide whether to establish the dispute mechanism, the dialogue with the “offending” country. In the arbitration format, the state is still the gatekeeper — it needs to create the existence of the individual right to arbitration in international law. So without these international tribunals or agreements, there basically is no remedy. There may be a right, but no remedy.

Not only do NAFTA, the European Energy Charter Treaty, and over 2,000 investment treaties contain disputes mechanisms that permit direct recourse to arbitration, they also contain substantial obligations that give rights to people. So how do we determine the meaning and scope of these rights? Well, to begin with, the terms say what they say. We look at the ordinary meaning of the terms, the context of the treaty, and remember the scope, object and purpose of the treaty. This is the test that was detailed in the Vienna Convention.²² It is not that different from statutory interpretation; ordinary meaning within the context with the object and purposes kept in mind. For the most part, this approach will help you articulate the rights that the text of any of these treaties provides. I would caution, however, that these obligations can be a little vague. For example, NAFTA Chapter 11, Article 1105 is entitled “Treatment in accordance with international law,” and includes the concept of “fair and equitable treatment and full protection of security.” What does fair and equitable treatment mean?

On a practical level, interpretation of such terms is more than just a mechanical application of the basic method found in the *Vienna Convention on the Law of Treaties*. There is also this thing called doctrine. International law doctrine is usually included by oblique reference somewhere in the treaty. The treaty may say

22. Vienna Convention on the Law of Treaties, May 22, 1969, 1155 U.N.T.S. 331.

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

that the tribunal will determine the rights in dispute, for example under Article 1131(1) of the NAFTA, by recourse to “the applicable rules of international law.” This is a common reference and it is one way in which doctrine can enter the analysis.

The influence of doctrine on tribunal decision-making can appear mysterious at times. Litigators commonly stress to their clients that facts win a case; end of story. Unless we’re involved in a particular case, we don’t have the same command of the facts as the litigators and we only have the reasoning provided in the award to guide us as to the result. Sometimes the award conforms to our appreciation of the law; sometimes not. Sometimes too, the award appears to conform to the applicable law but the lawyers involved express resentment about the facts, as found, not being supported by the evidence. This is one reason why awards are not treated as precedent, but instead as final determinations of a dispute submitted to the tribunal by the parties.

Where does this leave us with doctrine? We have substantive law as found by the tribunal applied to the facts of the case as found by the tribunal. As we review the larger number of awards emanating from tribunals, we can’t help but attempt to synthesize the results against some objective standard. We cannot help but apprehend the appearance of doctrine. It develops with this accumulation of awards; the facts may change but the applicable rules appear to stay the same. At the margins, where there appears to be differences of opinion amongst tribunals about the applicable rules, that’s where we see the same doctrinal debate we might see within any domestic system of law.

This is important because treaties typically contain language stating that there is no *stare decisis*, and custom supports this position. Similarly, I signed a lease with a tenant yesterday and he asked why the lease contained a “time is of the essence” clause. I said, “That clause is always included in a lease.” Well, it is the same thing with treaty language: the treaty says there is no *stare decisis*. Notwithstanding that language, that is not the way the human mind works, civil or common.

So where do these tribunals get their reasoning? First, there is a legal text interpreted properly in accordance with the Vienna Convention rules. You have the legal text and its ordinary meaning.

Second, there are two secondary international law sources: the decisions of previous tribunals and the writings of the most highly qualified publicists in the field. These two sources are alternative secondary sources of international law that create and shape doctrine over time. Along with the three primary sources –

custom, treaty and general principles – these subsidiary sources of law shape the work of most, if not all, international tribunals.

There are three basic obligations found in virtually all of these treaties: first, national treatment; second, the minimum standard of treatment; and third, compensation for expropriation. Compensation for expropriation involves application of a formula, largely agreed to be a matter of customary law, which compensates a person when they are deprived of the use of their investment. If a business is effectively rendered useless as a result of government treatment, that business owner will be compensated according to the accepted formula.

The obligation pertaining to national treatment can best be conceived of as a three-part test. First, you determine your comparators – usually two competitors in the same industry or engaged in commercial competition. Next you determine whether the two competitors are receiving different treatment. Evidence is an important factor for this part of the test; there must be proof that the difference in treatment is significant and that it provides “treatment less favorable” to the claimant. Finally, one tries to determine whether there is a reasonable, or sometimes just a rational, basis for the differing treatment.

An example of the application of this test would be to compare foreign and local participants in the same industry to determine which is receiving better treatment and why. The formulation of this national treatment standard is similar in WTO law and investment law. Both compare the level of treatment received by one party to that received by another party, although for investment obligations the third prong of the test is often implied in the substantive obligation, whereas in the trade context the third prong stands as a separate exemption clause (and the substantive obligations are treated as only addressing the first two prongs of the test).

The minimum standard of treatment, the second obligation mentioned above, is basically a baseline minimum test. The inquiry is whether a claimant is receiving the treatment to which all persons are entitled as a matter of customary international law. There is no bright line that defines the minimum standard of treatment in any given context, and there is often much debate as to where that line should be drawn. There nonetheless appears to be general agreement that a line essentially defined by an objective apprehension of “fairness” does exist. There’s not enough time to enter into a substantive analysis here, but the doctrine appears to confirm that the minimum standard requires procedural fairness of states, and probably some level of substantive fairness, although this second aspect of the standard is less developed than the first. The minimum standard test is not the

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

same as the national treatment test because it does not compare how different people were treated to see who received the best treatment. The minimum standard test is about whether specific treatment falls below the ultimate line of state responsibility in any given case.

In summary these are the three obligations: comparative (or national treatment), minimum standard, and expropriation compensation. These are three different concepts. When drafters write treaties, they often include all three obligations because they think all three are necessary.

Yet, some of the work that is coming out of recent tribunals seems to show that one concept, rather than three, is attaining considerable prominence over time and is effectively being applied in the case of all three tests. That concept is the general international law principle of good faith.

Whether or not good faith has been accorded by a state can be manifest in its treatment of the investment or the investor. Most often it arises in situations of legitimate expectation or detrimental reliance, although it is also known under the (primarily) civil law concept of abuse of rights, which has also found its way into international law. A claim of detrimental reliance must be supported by an investor's legitimate expectation to receive some kind of treatment. There are two ways this reliance develops. There is a global conception of an investor being entitled to a certain degree of procedural fairness and transparency when it invests in another country, or in the economic zone created by that treaty. When there is a treaty that promises fair treatment, an investor can point to it if such treatment is not forthcoming. Then there are cases of specific reliance where an individual seeks advice from a state official and receives assurance that his activity is fair and legal practice, only to later find that the official advice was purposefully misleading.

Good faith, manifested in the presence of detrimental reliance upon legitimate expectation, can be seen in the reasoning of recent tribunals, regardless of which obligation is under consideration: national treatment; the minimum standard or compensation for expropriation.

So how do these ideas of reliance come out in the three treaty obligations discussed earlier? In national treatment, it is found in the application of a rule of reason, or proportionality, theory. Under the model described above, these concepts are seen in the third prong of the national treatment test. Take the example of comparing bricklayers who work in an industry in which there is a regulation that says one of the bricklayers, but not the other, may use cheaper and better bricks. The question is whether a reason exists why one bricklayer, rather

than both, is allowed to use these better bricks. The rule of reason, as it relates to reliance, is applied to decide whether bricklayers should generally expect that when they establish themselves in the treaty's economic area they should be entitled to expect to receive treatment no less favorable than that which other bricklayers receive.

In this example, the relationship between the minimum standard and reliance is rather obvious because both are defined by an inquiry into the claimant's legitimate expectation. The case of *Saluka v. The Czech Republic* represents such a case.²³ For all intents and purposes, it was a national treatment case, but the treaty provided only for fair and equitable treatment. The tribunal recognized the complaint as a breach of fair and equitable treatment because competing banks received better treatment than that which was received by the claimant's bank, and which the tribunal apparently concluded was to be expected.

And what of the expropriation obligation? The obligation to provide compensation for expropriation appears very clear cut on its face. The typical provision basically says the bottom line is that a government must pay for what it takes. However, this is a hard obligation to apply in practice. Rather than applying a hard and fast "take and pay rule," many tribunals are resorting to an analysis of whether there was even a reasonable or legitimate expectation to enjoy the fruits of that which was taken from the claimant. In a sense, applying the principle of good faith takes the edge off of what might otherwise appear, to some, to be a harsh obligation. .

Question from the audience: Just this week I was wondering whether the effect of the NAFTA decision-making process in Mexico leads to greater power of Congress vis-à-vis the executive, and whether that is a good thing. In the United States we would look at those questions as matters regarding the separation of powers. How would such an analysis work in Mexico?

Sergio Puig: That is a very good point. This question should be analyzed as a separation of powers issue in Mexico as well; however, understanding how international law plays a role in this dynamic is an interesting phenomenon. I think most of the claims are that in Mexico the executive has tried to enjoy more powers by relying on international law, especially when they've tried to advance liberalization. Obviously, this has caused a reaction in the Mexican Congress. Thus, we will very likely see in the coming years a Constitutional debate around the powers of Congress and the effect of the treaty-making power of the executive

23. *Saluka v. Czech Republic*, (Perm. Ct. Arb. 2006), available at <http://www.pca-cpa.org/upload/files/SAL-CZ%20Partial%20Award%20170306.pdf>.

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

on those powers.

Question from Audience: Are there issues with enforcement of the judgments that come out of these panels?

Todd Grierson-Weiler: When the NAFTA was signed, neither Mexico nor Canada was party to the ICSID Convention. Canada has recently ratified, but questions remain as to the Convention's enforceability and effect until each of Canada's provinces has implemented the treaty, along with the Federal Government. Thus far, only five provinces have passed the necessary legislation. Accordingly, all of the arbitrations thus far have either proceeded under the UNCITRAL Rules or the ICSID Additional Facility Rules. This means that once an award has been delivered, it can be challenged by either side before the local court having responsibility for the place of the arbitration. The standards to be applied in review of an award are very narrow, falling along the same lines of the UNCITRAL model law on arbitration, which has been designed to ensure that local courts do not unduly interfere with arbitration. There is a review mechanism in the district court and then a court of appeals after that. Depending upon the parties and the courts in question, judicial review of an award can string out the proceedings for as many as a few more years. Under the ICSID model, similar standards apply to an application to annul the award, but the reviewing body is internal to the ICSID system, and thus an ICSID award is generally not believed to be reviewable before any local court. Either way, the annulment process can be used to string out a case of an additional one to three years, depending upon whether appeal is available from the reviewing court. At the end of the day, however, if the award has not been struck down, I think the governments will pay.

Meg Kinnear: There has never been a damage award that was not paid. For example, Mexico paid the damages award in *Metalclad*.²⁴ Countries pay awards to make sure that people feel confident in investing, and part of that confidence is enhanced if they think a judgment will be paid. It has never been an issue. No one has ever had to go to formal enforcement.

Andrea Bjorklund: Russia has not paid awards that are enforceable under the New York Convention.²⁵ Investors who have prevailed in collecting awards owed to them by Russia have succeeded by allowing the German government to seize Russian assets in Germany and sell those assets to pay the awards. It often takes years to collect an award in this manner because not all courts have interpreted the

24. *Metalclad v. Mexico*, ICSID Case No. ARB(AF)97/1 (2000).

25. *New York Convention on the Recognition and Enforcement of Arbitral Awards*, June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 3.

New York Convention to waive sovereign immunity in such cases. There have been a few courts that have refused to enforce awards against a state on the grounds of sovereign immunity, but, generally speaking, that should not happen.

Todd Grierson-Weiler: There is a problem concerning the connection between the local law and the international law, and there is always a strain between the arbitral world and the domestic courts. There is a question when an award is subjected to review by a local judge as to what the capabilities and knowledge of the local judge might be with regard to the applicable rules and the deference they are meant to impose.

Question from Audience: Mr. López Obrador attacked NAFTA as part of his presidential campaign. Did that generate a lot of obvious sentiment in the people and how was it responded to?

Sergio Puig: Mr. López Obrador campaigned by raising a defiant voice against NAFTA. Some of those arguments have proven to be wrong. But his strong voice generated great concern in Mexico about NAFTA, especially around the opening of trade in corn and beans between Mexico and the United States. Carrying on with these obligations will be difficult for Mexico. Congress is the branch of the government that is most likely to carry on the anti-NAFTA discourse. My sense is that Mexico will keep complying with NAFTA but protectionist sectors will keep pushing. López of course will use this for political gains, and he will bring many more questions.

Question from Audience: I was interested in your discussion about transparency at the level of the arbitration, arbitral transparency. There is, of course, another kind of transparency issue which arose in one of the Mexican cases. This involves the transparency of government action. I wondered if the standards that are emerging for transparency are the same at these two different levels.

Mrs. Kinneer: Interestingly, that transparency decision was taken on review to a British Columbia Court and what they found was that the substantive standard of treatment obligation did not include an obligation of transparency.

Todd Grierson-Weiler: Meg is discussing the *Metalclad* decision. It is interesting that in the wake of that decision we moved to have the *UPS* arbitration located in DC instead of Canada because in *Metalclad* it was clear that the judge had overstepped the bounds of the typical standard of review that courts apply to arbitral decisions and was looking into the substantive question of whether the arbitrators were right or wrong. The *UPS* tribunal moved the arbitration to DC as a result of our request, although its award did not say that the *Metalclad* result was determinative.

5 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 2 (2007)

Sergio Puig: While NAFTA does not directly incorporate a transparency obligation, Article 1802 is clear that states should ensure a certain level of clarity and that administrative rulings should be promptly published or otherwise made available to interested persons. Article 1802 establishes that one of the principles of interpretation of NAFTA is transparency.

Meg Kinnear: I think there is a difference between the transparency obligations in NAFTA and transparency of the factual situation that you are bringing an arbitration under the NAFTA.

Andrea Bjorklund: There is a recent case from the Inter-American Court of Human Rights, the *Reyes* case, which has established the principle of right of access to information.²⁶ This may have a broader effect on the availability of information.

Question from Audience: There have been efforts to create accounting standards and engineering standards with respect to NAFTA. What is happening on the services front; are there any live controversies that have risen to your attention and are being settled?

Sergio Puig: The only professional standards that I can tell you about are those in the legal profession. There is a push in Mexico to increase the level of competency and a push towards mandatory certification. As of today, there is no mandatory bar affiliation in Mexico. In 2008 there is going to be recognition of degrees between U.S., Mexico and Canada. So if you have a law degree from the U.S., you can practice in Mexico. Conversely, a person who receives an LL.B. in Mexico must still pass the Bar in the United States to practice here. So, some groups are using this argument to advocate in favor of the bar.

Meg Kinnear: That is right. Under NAFTA there are technical committees for almost every profession you can think of trying to harmonize the expectations and the educational requirements. The goal is to be able to cross borders and practice without any problems. It has been an agonizingly slow process. There are many technical committees forming to address this, and legal practice is one of the controversial ones.

Andrea Bjorklund: I have a question about damages. Todd, you were talking about convergence on the substantive fronts. In many of these treaties there is little guidance with respect to the measure of damages, and many tribunal decisions have been rather opaque on that front. The expropriation provision in NAFTA is very clear as to how fair market value is to be calculated. Are tribunals borrowing

26. *Reyes v. Chile*, 2006 Inter-Am. Ct. H.R. (ser. C) No. 151 (Sept. 19, 2006).
408

that provision to measure damages under the other obligations?

Todd Grierson-Weiler: From the perspective of the onlooker, sometimes it may appear that the tribunal arrives at a number and works backwards from it. The *S.D. Myers* tribunal did a good job with damages.²⁷ It started with *Chorzow Factory*, which as you know says you should be put back in the position you were in before the breach.²⁸ I think we are years away from having a whole area of law on the topic, but at least the *Myers* tribunal explained the steps it was taking. For example, the *Metalclad* tribunal actually had explicit directions as to how to calculate damages, under Article 1110, but it chose not to follow them. It only gave the investment back, plus interest. The level of economic and financial analysis is really quite good these days, and so the parties can expect to rely on excellent work from their experts. In general, I think the tribunals may decide that a case either appears more like a contract case, or more like a tort case, and they can extract principles from domestic systems of contract and tort law to fill in some of the answers.

Question from Audience: What happens when claimants delay bringing a claim to wait until things get really bad? How do you measure those damages?

Todd Grierson-Weiler: It is always hard to know when to bring a case. There is a three-year limitation period, so you have to bring it within that time. But applying it in a given case can be difficult. Moreover, sometimes you think you know what your case is, but things change as the case progresses. I had one case in which we thought we knew the government measure that was at issue, but only after the case had been going on for a few years did the primary injury occur, because the measure was tweaked by the respondent government.

Meg Kinnear: Another interesting thing is that many of the measures are ongoing, but tribunals have no power to order that the measure be repealed; they can only order damages arising from the measure. But tribunals are not going to say, your damages are over because you filed your case on November 1; they are going to give you damages up to the date they decide the case. So your tendency is to get in as early as possible.

Todd Grierson-Weiler: You can always do a present-day analysis of future loss. As a general rule, you don't want to wait until your damages are greater before you bring a claim, because there are dangers in waiting, for example estoppel, that might affect your case.

27. *S.D. Myers v. Canada*, (UNCITRAL 2000).

28. *The Factory at Chorzów*, 1927 P.C.I.J., Ser. A, No.9 (July 26).