NAFTA's Investor "Rights"
A Corporate Dream, A Citizen Nightmare

by Mary Bottari

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The North American Free Trade Agreement (NAFTA) includes an array of new corporate investment rights and protections that are unprecedented in scope and power. NAFTA allows corporations to sue the national government of a NAFTA country in secret arbitration tribunals if they feel that a regulation or government decision affects their investment in conflict with these new NAFTA rights. If a corporation wins, the taxpayers of the "losing" NAFTA nation must foot the bill. This extraordinary attack on governments' ability to regulate in the public interest is a key element of the proposed NAFTA expansion called the Free Trade Area of the Americas (FTAA).

NAFTA's investment chapter (Chapter 11) contains a variety of new rights and protections for investors and investments in NAFTA countries. Specifically, Article 1110 of NAFTA guarantees foreign investors compensation from the NAFTA governments for any direct government expropriation (i.e., nationalization) or any other action that is "tantamount to" an "indirect expropriation." In addition, Article 1102 provides for "national treatment," which means that governments must accord to companies of other NAFTA countries no less favorable treatment than they give to their own companies. Article 1105 contains a "minimum standard of treatment" provision, which includes vague prose about fair and equitable treatment in accordance with international law.

If a company believes that a NAFTA government has violated these new investor rights and protections, it can initiate a binding dispute resolution process for monetary damages before a trade tribunal offering none of the basic due process or openness guarantees afforded in national courts. These so-called "investor-to-state" cases are litigated in the special international arbitration bodies of the World Bank and the United Nations, which are closed to public participation, observation and input. A three-person panel composed of professional arbitrators listens to arguments in the case, with powers to award an unlimited amount of taxpayer dollars to corporations whose NAFTA investor privileges and rights they judge to have been impacted.

Corporate investors have used these unprecedented NAFTA investment protections to challenge national and local laws, governmental decisions and even governmental provision of services in all three NAFTA countries. To date, companies have filed more than a dozen cases, claiming damages of more than US$13 billion [see "The Chapter 11 Dossier"].

"Tantamount to Extortion"

In the largest Chapter 11 suit yet brought against the United States, the Canadian corporation Methanex in 1999 sued the U.S. government for $970 million because of a California executive order phasing out the sale of a Methanex product. Methanex claims that

California’s phase-out of methyl tertiary butyl ether (MTBE), a gasoline additive, violates the company’s special investor rights granted under NAFTA because the California environmental policy limits the corporation’s ability to sell MTBE. If a NAFTA tribunal decides that California’s environmental policy violates NAFTA’s investor protections, the U.S. government can be held liable for the corporation’s lost profits from not selling MTBE.

The case is "a clear threat to California state sovereignty and democratic governance," says Martin Wagner of the California-based Earthjustice Legal Defense Fund. If Methanex succeeds, California will be under pressure to rescind its executive order, to lessen the damage award.

Associated with human neurotoxicological effects, such as dizziness, nausea and headaches and found to be an animal carcinogen with the potential to cause human cancer, MTBE has been found in ground water and drinking wells around California. On March 25, 1999, California required the removal of MTBE from gasoline sold in the state by December 31, 2002. Governor Gray Davis declared that "on balance, there is significant risk to the environment from using MTBE in gasoline in California."

Methanex claims that adding MTBE to gasoline reduces air pollution. However, a 1998 University of California at Davis (UC-Davis) report, which informed the government action, found that "there is no significant additional air quality benefit to the use of oxygenates such as MTBE in reformulated gasoline." The report found "significant risks and costs associated with water contamination due to the use of MTBE." The report noted that "MTBE is highly soluble in water and will transfer readily to groundwater from gasoline leaking from underground storage tanks, pipelines and other components of the gasoline distribution system." It also noted that the use of MTBE in motor boat fuel results in contamination of surface water. The report concluded that "[w]e are placing our limited water resources at risk by using MTBE."

On the basis of the UC-Davis findings, California moved to ban MTBE. Methanex’s response was to drag the California policy into NAFTA Chapter 11 litigation, demanding MTBE be allowed or $970 million be paid.

In its amended claim, Methanex alleges that the California ban discriminates against MTBE in favor of ethanol, a similar U.S. product, and is therefore a violation of NAFTA’s national treatment rules. As evidence, Methanex cites the executive order which requires the California Energy Commission to look into development of a California ethanol facility. Methanex alleges that Archer Daniels Midland (ADM), a principal producer of ethanol in the United States, influenced the governor’s decision with $210,000 in campaign contributions, arguing that the ban stands in violation of NAFTA’s fair and equitable treatment rules. Finally, Methanex claims that the ban was not the "least trade restrictive" method to fix the water contamination problem, and thus violates NAFTA requirements that companies be treated fairly and "in accordance with international law." The relevant laws cited by Methanex are the rules of the World Trade Organization, which require countries to use the least trade restrictive means to achieve environmental and public health goals.

"These cases are tantamount to extortion," says Martin Wagner. "This is a situation in which someone is causing a harm and then making the assertion that they will stop that harm only upon payment of a fee. In the California case, Methanex is selling a chemical and saying to the U.S. government, 'If you want us to stop, you have to pay us.' This is even more appalling when you consider that the victims of this extortion are the people of California, who don't want their drinking water contaminated by MTBE."

The California case has drawn comparisons to the 1998 case brought against Canada by the U.S.-based Ethyl Corporation [see "Another NAFTA Nightmare," Multinational Monitor, October 1996]. In that case, Ethyl sued Canada for $250 million after Canada banned the gasoline additive methylcyclopentadienyl manganese tricarbonyl (MMT) because of health risks. The state of California had banned MMT and the U.S. Environmental Protection Agency (EPA) was working on a similar regulation. Ethyl claimed the Canadian ban violated NAFTA because it "expropriated" future profits and damaged Ethyl's reputation. After learning that the NAFTA tribunal was likely to rule against its position, the Canadian government revoked the ban, paid Ethyl $13 million for lost profits to date, and, as part of a settlement with Ethyl, agreed to issue a public statement declaring that there was no evidence that MMT posed health or environmental risks.

Methanex brought its NAFTA case to the United Nations Commission for International Trade and Law (UNCITRAL), the arbitration regime of the United Nations. The case is now pending. Under UNCITRAL rules, not only are the citizens of California shut out of this proceeding, but so are the governor and the attorney general of California, the state whose policy is in question. California officials must rely on the Office of the U.S. Trade Representative (USTR) to defend the interests of California residents in this closed tribunal.

Deliver This

In a case that seeks to push the limits of Chapter 11, the U.S.-based United Parcel Service (UPS) is pursuing a NAFTA Chapter 11 case against Canada for $100 million, arguing that the fact of the Canadian postal service's involvement in the courier business infringes upon the profitability of UPS operations in Canada.

In this case, the first NAFTA investor-to-state case against a public service, UPS is attempting to stretch the NAFTA Chapter 11 provisions in an entirely new direction. Canada Post is a "Crown corporation" owned by the people of Canada. Canada Post has not received direct taxpayer support for about a decade and has been paying income tax since 1994.

UPS claims that by integrating the delivery of letter, package and courier services, Canada Post has cross-subsidized its courier business in breach of NAFTA rules. For example, UPS argues that permitting consumers to drop off courier packages in Canada Post letter mail postal boxes unfairly advantages Canada Post as against other courier services. Other alleged forms of cross-subsidization include:

- Using letter carriers to pick up courier packages from the mail boxes and "transport them in vehicles that form part of the infrastructure of the Canada Post monopoly."
- Sorting courier packages at "Canada Post's letter mail monopoly sorting facilities across Canada."
- Transporting courier packages on airplanes and trucks chartered by the mail service.
- Selling courier services at post offices.
- "Precluding franchisees at Canada Post retail outlets from selling of any courier

product other than Canada Post’s."

- Permitting courier consumers to use postal stamp meters on courier packages.
- "Having the regulatory definition of ’letter’ changed from 450 grams to 500 grams in order to expand its letter mail monopoly."

"UPS is entitled to receive the best treatment available in Canada with respect to the treatment of its investment," UPS argues in its claim. "This treatment would include having equal access to the postal distribution system provided" to the postal service’s courier operations. Failure to provide such equal treatment, UPS alleges, violates the national treatment obligations of Chapter 11.

In a cable by the U.S. Embassy in Ottawa that Public Citizen obtained under a Freedom of Information Act request, UPS Canada Legal and Public Affairs Vice President Allan Kaufman was characterized as "very confident the Government of Canada stood to lose its fourth and largest Chapter 11 challenge with the UPS case," and Kaufman signaled that the corporation would be open to settlement.

Former Canadian Foreign Minister Don Mazankowski responded to these arguments in a February 2001 column in the Globe & Mail. He argued that Canada treated UPS with an even hand by allowing UPS access to the market on the same terms as any Canadian corporation, that UPS is not subject to any additional taxes or duties and that the company is governed by the same laws as any Canadian corporation.

"The UPS claim is unique. Unlike the other NAFTA-based foreign investor claims which have sought to recoup investments, UPS is using NAFTA Chapter 11 provisions in a strategic offensive to secure a greater share of the Canadian market," asserts Canadian trade attorney Steve Shrybman. "UPS is arguing that because Canada Post provides public mail services, it shouldn’t also be providing integrated parcel and courier services. In an era when monopoly and commercial service delivery is commingled, few public services including health care and education would be immune from similar corporate challenges."

This case is also proceeding under UNCITRAL rules and the Canadian Union of Postal Workers and other interested parties are attempting to intervene.

The Fast Track to Expanded Chapter 11

The "expropriations" that have been challenged under Chapter 11 are nothing like the government seizure of property that is generally conveyed by the term. Instead, corporations have used the provision to challenge or seek compensation for what are called "regulatory takings" in the United States - regulations which supposedly take away the entire value of a property. While a conservative legal movement has worked for two decades to espouse the theory of regulatory takings, with some success, regulatory takings suits continue to face significant judicial hurdles in U.S. courts. The Chapter 11 cases take this "regulatory takings" logic to a new extreme.

While these expansive investor rights currently are included only in NAFTA, plans are underway to incorporate similar provisions in the FTAA. FTAA is a proposed NAFTA expansion to all 34 countries of the Western Hemisphere (but for Cuba). The Bush administration has signaled that it wants the controversial fast-track trade negotiating authority in order to negotiate the FTAA. Once Congress delegates its trade negotiating authority to the president via fast track, it limits its own role to a single up-or-down vote on trade agreements' implementing legislation, which cannot be amended.

There is no guarantee the Bush administration will succeed in its effort to win fast track, or in its attempts to impose investment provisions in the FTAA.

Canada, which has been badly burned in a series of Chapter 11 cases, is no longer a believer. Canadian Trade Minister Pierre Pettigrew has declared that Canada will not sign FTAA if investor-to-state enforcement of broad regulatory takings rights are included, and Canada has called for a review of Chapter 11 within NAFTA.

Whether Canada will hold to these positions, and whether it can organize other countries to join it amidst the complex FTAA negotiations in which the United States is the dominant player, remains to be seen. In the meantime, environmentalists, public health groups, California residents and many others concerned about the broad regulatory takings provisions will continue to press for their removal from NAFTA and their exclusion from the FTAA.

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The Chapter 11 Dossier: Corporations Exercise Their Investor "Rights"

Corporations have filed more than a dozen cases under NAFTA's Chapter 11 investment provisions, which enable corporations to sue governments for infringements of their "investor rights." Since they are conducted in confidential arbitral processes, inaccessible to public scrutiny and participation (in contrast to open proceedings in domestic courts), information on ongoing cases is sketchy. Available information on 15 of the cases is summarized below.

Suits against Canada

Ethyl Corporation
In this first investor-state case, Ethyl Corporation of the United States sued the Canadian government for $250 million and obtained, in 1998, a settlement of $13 million for the Canadian ban on the gasoline additive, MMT, a nerve toxin [see "Another NAFTA Nightmare," Multinational Monitor, October 1996]. The ban was reversed.

S.D. Myers
In October 1998, U.S.-based S.D. Myers Inc., which treats transformers containing toxic PCBs, filed a claim for $30 million for losses it claims to have incurred during a one-and-one-half-year ban (1995 to 1997) on the export of PCB wastes from Canada. The Canadian federal government states that Canada is bound by international conventions that stipulate that PCBs must be destroyed in an environmentally sound manner, and that U.S. standards for PCB disposal are not as high as Canada's. The wastes were destroyed in a Canadian facility in Alberta, and the export ban was revoked in 1997. The U.S. government also controls cross-border movement of PCBs. In November 2000, the arbitral tribunal found that the ban did contravene the investment chapter regarding national treatment and minimum standards of treatment of foreign investors, and it is now determining whether S.D. Myers suffered

damages. In the meantime, the Canadian government has applied to the (domestic) Federal Court to have the tribunal's partial award set aside, arguing that the case concerned cross-border trade, not a Canadian investment, and that the award conflicts with a well-established Canadian policy requiring disposal of PCBs and PCB wastes in Canada to comply with the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal.

Sun Belt Water Inc.
This California-based company is suing Canada for the decision of the provincial government of British Columbia to refuse consent for the company to export bulk water from BC. The government subsequently enacted the Water Protection Act, which bans bulk water exports and inter-basin diversions by domestic and foreign investors alike. In a colorful claim which alleges a decade of "smelly" actions by successive BC governments, Sun Belt Water expounds on the growing world-wide demand for water, assumes that water export must be a positive benefit (ignoring environmental and conservation requirements) and makes extreme claims of improprieties by the BC government and BC courts. In a BC court action, Sun Belt did not achieve its desired result. It is therefore using NAFTA Chapter 11 to seek damages of "between" $1 billion and $10.5 billion. Besides using the investment chapter for very dubious business practices, the case raises the fundamental issues of the uses of the investment chapter to evade the result of an action in a domestic court, and to challenge a non-discriminatory policy and legislation by a subnational (provincial) government.

Pope and Talbot
The US-based lumber company Pope and Talbot has sued Canada, claiming approximately $510 million for alleged breaches of the NAFTA investment chapter related to changes in the profitability of its timber export business in Canada. Softwood lumber exports from Canada to the United States have been a source of contention and repeated trade disputes for decades. Forest products are among the most important exports from Canada, representing billions of dollars in export earnings, and over 90 percent of these products are exported to the United States. In 1996, in yet another attempt to resolve the ongoing timber wars, the Canadian and U.S. federal governments signed the Canada-US Softwood Lumber Agreement, governing exports of softwood lumber from four Canadian provinces, British Columbia, Alberta, Ontario and Quebec. The agreement, which will expire at the end of March 2001, establishes quotas for exports for each province, and requires producers to provide certain information regarding exports and pay an export levy if their exports exceed their particular quota. In arriving at such export agreements, the Canadian government consults extensively with industry.

Pope and Talbot claimed that Canada has breached the NAFTA investment requirements regarding national treatment, most-favored nation treatment, minimum standard of treatment and performance requirements. The company's lawyers are critical of the Canadian government for its public release of the Notice of Intent to Submit a Claim, calling the release a "serious breach of international procedure."

Pope and Talbot's operations are located in British Columbia. During the period of the softwood memorandum, BC's share of total softwood exports has declined relative to total Canadian softwood exports; Pope and Talbot argue that this decline is related to the agreement, and amounts to a breach of the NAFTA chapter. (Others point to the loss of BC's traditional markets in Asia, related to the Asian economic crisis.) In an interim award, the tribunal rejected the claim that expropriation had occurred, but decided to continue hearings on claims relating to national treatment and minimum standards of treatment.

This case is an important indication of how far-reaching the impacts of the NAFTA investment chapter are and of how broadly multiple governmental powers and decisions may be challenged by an individual corporation for a huge compensatory claim.

United Parcel Service
UPS has filed a notice of intent to sue Canada for $100 million, alleging that Canada favors the public postal service, Canada Post, regarding provision of courier services [see "NAFTA's Investor "Rights""].

Ketcham Investments
and Tysam Investments
U.S.-based Ketcham Investments and Tysam Investments jointly own West Fraser Mills, a timber

company. Ketcham and Tysam allege in a December 2000 notice of intent to file a claim that their timber quota under the U.S.-Canada Softwood Lumber Agreement was arbitrarily cut, denying them rights afforded Canadian companies. They are seeking C$10 million in damages.

Suits Against the United States

Loewen

The B.C-based Loewen Group is suing for compensation arising from alleged discrimination, denial of minimum standard of treatment and expropriation, claiming that a $500 million Mississippi state court verdict against it amounts to a breach of NAFTA. The verdict came in a suit brought against Loewen by a Mississippi company, O'Keefe, alleging fraudulent practices and other anti-competitive practices. Loewen was denied an appeal of the court decision due to a state law which requires an appellant to post 125 percent of the damage award ($625 million in this case) which Loewen could not post. (Loewen eventually settled the claim for $175 million.)

The company seeks to recover $775 million in damages, interest and legal expenses through this investor-state claim and alleges that the Mississippi decision against it was based on anti-Canadian bias. A tribunal has agreed to hear the case.

This case demonstrates, as does Sun Belt, the use by a corporation of the NAFTA Investment chapter to essentially reverse the results of domestic court proceedings, and to circumvent the course of normal commercial civil litigation. Having lost to a competitor in the courts, it claims compensation from the U.S. federal government.

Methanex Corp.

In June 1999, this Vancouver-based company announced that it will sue the U.S. government for $970 million due to a California order to phase out use of the chemical MTBE (methyl tertiary butyl) a methanol-based gas additive, by late 2002 [see "NAFTA's Investor "Rights""].

Mondev

In September 1999, Mondev International Ltd., a Montreal-based real estate development firm, filed a claim against the U.S. government for $16 million. The case arises from the refusal of the city of Boston to permit it to expand a mall into a vacant lot in the 1980s although Mondev had a contract with the city. Mondev successfully sued the city and its redevelopment authority for $16 million, but the court decision was reversed on appeal due to state law protecting the redevelopment authority from liability. Mondev seeks to recover the damages through the NAFTA Chapter 11 investor-state route.

ADF Group

ADF, a Canadian fabricator of structural steel for complex structures, is suing the United States, seeking $90 million in compensation. ADF entered into a contract with Shirley Contracting Corporation to provide materials for construction of a Virginia highway interchange. ADF sought to fabricate products in Canada, using U.S.-made steel. U.S. federal government authorities held that this arrangement ran afoul of a "Buy America" requirement. ADF proceeded to attempt to fulfill the contract using its U.S. facilities and subcontracting to other U.S. facilities. It alleges the Buy America rules violate Chapter 11 requirements for national treatment and for bans on performance requirements.

Suits Against Mexico

Metalclad

This case involves a claim by U.S.-based Metalclad, a waste-disposal company, that the Mexican state of San Luis Potosi breached Chapter 11 of NAFTA in refusing permission for a waste disposal facility.

The governor deemed the plant an environmental hazard to surrounding communities, and ordered it closed down on the basis of a geological audit performed by environmental impact analysts at the University of San Luis Potosi. The study had found that the facility is located on an alluvial stream and therefore would contaminate the local water supply. Eventually, the governor declared the site part of a 600,000 acre ecological zone.

Metalclad sought compensation of some $90 million for expropriation and for violations of national treatment, most favored nation treatment and prohibitions on performance requirements. This figure is larger than the combined annual income of every family in the county where Metalclad's facility is located.

In August 2000, a tribunal found that Mexico had breached the Investment chapter and awarded Metalclad $16.7 million, the amount it had spent in the matter. In this case, Metalclad proceeded to begin construction of the facility without having local approvals, claiming that it had assurances from the Mexican federal government. The case raises important questions about whether governments retain the authority to enact environmental controls on foreign investors and about the powers of local governments.

The Mexican government has appealed the award to the Supreme Court of British Columbia, since hearings of the case were held in British Columbia, and the Canadian government and government of Quebec have intervened.

Waste Management Inc.

This case involves a claim filed in 1998 against the Mexican government for $60 million by Waste Management, Inc. It concerns an exclusive 15-year concession to its subsidiary to provide solid waste management to Acapulco. The company claims that it was guaranteed payment by the state of Guerrero and the Mexican federal development bank, Banobras, and that the obligations have not been met, constituting actions tantamount to expropriation.

Desona/Azinian

U.S.-based DESONA and its individual investors, Robert Zinian et. al. filed this claim for over $14 million and costs in 1997 against the Government of Mexico. The claim related to a waste management business in Mexico. Desona claimed that a long series of unfair and conflicting decisions and actions by local authorities contributed to its losses, and culminated in the forcible removal of its managers from its waste collection and landfill business in Naucalpan, a suburb of Mexico City on four days notice.

The case was dismissed by the arbitral panel in November 1999, in a scathing decision critical of the company's actions and record of dishonesty. However, since the case turned on the finding of invalidity of the contract on which the claim was based, it does not assist governments and citizens regarding the problem of the impact of Chapter 11 claims on legislative actions.

Cemsa/Feldman

This is the first NAFTA investor-state suit involving a tax issue. U.S. investor Feldman, sole owner of the corporation CEMSA, filed a claim against the Mexican government in May 1999 for $50 million, alleging that his company was wrongly denied excise tax rebates and export rights for its cigarette exporting business. Again, allegations of numerous irregular actions by Mexican authorities are made, including that CEMSA was required to provide invoices from its vendors which stated the amount of tax included in the purchase price. However, CEMSA claims that the tax authorities did not require that manufacturers provide this information, so that CEMSA could not comply with the requirement.

Adams

This case involves a dispute over title to and use of land on which U.S. investors had built vacation homes. A group of Mexican landowners won a claim in Mexican courts that the disputed land had been illegitimately taken from them by the Mexican government, which later authorized its use by the U.S. investors. The Mexican Supreme Court ordered the land returned to the landowners, and Mexican authorities did subsequently return the land, including the vacation homes on it. The U.S. investors are seeking $75 million in compensation under Chapter 11.

-Michelle Swenarchuk