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INTERNATIONAL ARBITRATION TO RESOLVE DISPUTES UNDER NAFTA CHAPTER 11: INVESTMENT

S. Benton Cantey[†]

I. INTRODUCTION

Chapter 11 of The North American Free Trade Agreement (NAFTA) provides rules for foreign investment and investment disputes between the United States, Canada and Mexico.¹ This chapter “has three objectives: establish a secure investment environment through the elaboration of clear rules of fair treatment of foreign investing and investors; remove barriers to investment by eliminating or liberalizing existing restrictions; and provide an effective means for the resolution of disputes between an investor and the host government.”² The dispute resolution framework provides NAFTA investors the ability to request pecuniary damages through international arbitration instead of seeking alternative remedies through the host government’s courts or tribunals.³ Chapter 11 is laid out according to those objectives.⁴ Chapter 11 is divided into two primary sections, section A and section B.

Section A “provides four basic protections to ‘investors of other parties’: non discriminatory treatment; freedom from ‘performance

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1. North American Free Trade Agreement, Dec. 8, 1992, art. 11, 38 I.L.M. 88 [hereinafter NAFTA].

2. Daniel M. Price, *An Overview of the NAFTA Investment Chapter: Substantive Rules and Investor-State Dispute Settlement*, 27 INT’L LAW. 727 (1993).

3. Richard C. Levin & Susan Erickson Marin, *NAFTA Chapter 11: Investment and Investment Disputes*, 2 NAFTA: L. & BUS. REV. AM. 82 (1996).

4. Price, *supra* note 2, at 727.

requirements;’ free transfer of funds related to an investment; and expropriation only in conformity with international law.”⁵ Further, Section A includes provisions where the host government may not control senior management, may deny NAFTA benefits, may maintain environmental protections, and may provide exceptions to the general rules. “Section B of Chapter 11 provides a mechanism for an investor to pursue a claim against a host government that it has breached its obligations under Section A.”⁶

This comment is intended to provide investors with a clear understanding of the core provisions of Chapter 11. Additionally, the comment will convey the rules of international arbitration under NAFTA, as well as provide the investor with insight as to the practical workings of this procedure from the relatively few cases that have been arbitrated under Chapter 11. Part II will discuss and provide investors with an outline of the significant parts of Chapter 11 of NAFTA. Part III will furnish the reader with a clear understanding of the International Centre for Settlement of Investment Disputes (ICSID). In Part IV, the handful of cases that have been decided or are pending under the Centre will be discussed, as well as the potential ramifications of those decisions. Next, Part V will provide a look at the results of expropriation for compensation. This portion of the comment will focus on possible alternatives and arguments for narrowing the scope of the expropriation provision under NAFTA Chapter 11. Finally, Part VI concludes with an overview of the pertinent NAFTA provisions for future potential international investors and some crucial factors for investors to consider before investing under NAFTA.

II. CHAPTER 11

A. Section A

It is first necessary to define the terms “investor” and “investment.”⁷ An “investor of a party” is defined to encompass both firms (including branches) established in a NAFTA country, without distinction as to the nationality of ownership, and NAFTA-country nationals.”⁸ The term investment is defined very broadly in Article 1139, which includes both future and existing investments.⁹ Moreover, “investment” includes

5. *The North American Free Trade Agreement Implementation Act: Chapter Eleven: Investment*, 1993 WL 561159, at 1 [hereinafter NAFTA Implementation Act].

6. NAFTA Implementation Act, *supra* note 5, at 5.

7. Price, *supra* note 2, at 728.

8. NAFTA Implementation Act, *supra* note 5, at 1.

9. *Id.*

“ownership and other interests in an enterprise, such as equity or debt securities of an enterprise as well as certain loans to an enterprise.”¹⁰ Other interests such as “interests that entitle an owner to share in the income or profits of an enterprise; real estate; and all forms of tangible and intangible property, including intellectual property” are all included under the investment definition.¹¹ The investment definition “also extends to interests arising from the commitment of capital or other resources such as under concession agreements; turnkey or construction contracts; or contracts where the remuneration depends on the production, revenues, or profits of an enterprise such as may occur under license or franchise agreements.”¹²

1. Non-Discriminatory Treatment

NAFTA governments are required to treat NAFTA investors and their investments “no less favorably than its own investors and their investments, and no less favorably than investors of other countries and their investments.”¹³ This treatment applies “to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.”¹⁴ A host government may not impose local equity requirements or require an investor from another NAFTA country, by reason of its nationality, to sell an investment according to Article 1102.¹⁵ Further, Article 1102(3) calls for an investor to receive “treatment no less favorable than the most favorable treatment accorded, in like circumstances, by that state or province to investors . . . of the Party of which it forms a part.”¹⁶ Thus, a major reason this provision was incorporated was to encourage international investing. In addition, this provision was intended to increase the confidence of international investors, allowing them not to worry about losing their investment capital under international uncertainty.

2. Performance Requirements

According to Article 1106, a government may not require a firm to “export a certain percentage of output; give preferences for domestic sourcing; achieve a certain level of domestic content; transfer technology;

10. Price, *supra* note 2, at 728.

11. *Id.*

12. *Id.*

13. NAFTA Implementation Act, *supra* note 5, at 1.

14. NAFTA, *supra* note 1, art. 1102(1).

15. NAFTA Implementation Act, *supra* note 5, at 1.

16. NAFTA, *supra* note 1, art. 1102(3).

or achieve a certain trade balance by restricting domestic sales to some proportion of exports or foreign exchange earnings.”¹⁷ All NAFTA host governments are required to abide by the rules that prohibit performance requirements “whether by non-NAFTA investors, domestic investors, or investors from another NAFTA country.”¹⁸

Preventing performance requirements serves two goals.¹⁹ First, “trade distortions that arise from the imposition of performance requirements” are eliminated.²⁰ Consequently, a host country is prevented from placing a performance requirement on its own investors.²¹ Second, investors’ decisions are based solely on their own judgment rather than being clouded by interests of the host government.²² Yet, it is important to note that “performance requirements do not affect a government’s ability to apply nondiscriminatory environmental measures.”²³

3. Managerial Regulation

NAFTA governments shall not require that senior management positions be filled with local nationals.²⁴ In spite of this, the host government may require the majority of the board of directors to consist of local nationals as long as this does not “materially impair the ability of the investor to exercise control over its investment.”²⁵ Based on the face of this provision, it seems that host government interference has been eliminated. Nevertheless, skepticism remains that political persuasion has been removed because of host governments’ ability to put local nationals on the board of directors.

4. Transfers

Each NAFTA government must permit transfers relating to an investment to be made “freely and without delay.”²⁶ “This includes transfers to the investor such as the remittance of profits and dividends, the payment of interest and principal under a loan agreement, royalty payments, management fees, and proceeds from sale or liquidation of an

17. Price, *supra* note 2, at 729.

18. NAFTA Implementation Act, *supra* note 5, at 2.

19. Price, *supra* note 2, at 729.

20. *Id.*

21. *Id.*

22. *Id.*

23. NAFTA Implementation Act, *supra* note 5, at 2.

24. *Id.* art. 1107(1).

25. *Id.* art. 1107(2).

26. *Id.* art. 1109(1).

investment.”²⁷ Still, there are exceptions under Article 1109, and a government is also protected because the government “may prevent a transfer through the equitable, non-discriminatory and good faith application of its laws” regarding such issues as bankruptcy and criminal offenses.²⁸ Once again, on its face this appears to be a favorable provision for international investors. However, one must be aware that with the ability to prevent a transfer, foreign host governments have the opportunity to construe some actions as criminal, which might not be criminal otherwise, in order to prevent a transfer of money.

5. Expropriation and Compensation

A NAFTA government “may not expropriate an investment made by an investor from other NAFTA countries other than for a public purpose, on a non-discriminatory basis and in accordance with due process of law.”²⁹ Article 1110 “covers direct, indirect and so-called ‘creeping’ expropriation.”³⁰ “Compensation must be paid without delay, be equal to the fair market value of the investment, include interest from the date of expropriation, and be fully realizable and freely transferable as provided in the transfers article.”³¹ According to Article 1110 (2), “[v]aluation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.”³² Article 1110 “does not attempt to articulate the line between a legitimate regulation and a compensation taking.”³³ The “[a]greement between Mexico and the United States on the expropriation article effectively ends a difference that has persisted for decades on what compensation is due in the event of an expropriation.”³⁴ Foreign governments should be weary of this provision.³⁵ The language in the expropriation provision is broad.³⁶ Formerly impervious to lawsuits from foreign investors, this provision creates an avenue for foreign investors to file a lawsuit against a host government over any regulation they might make that impairs investor’s property interests.³⁷ Accordingly, a

27. Price, *supra* note 2, at 729.

28. NAFTA, *supra* note 1, art. 1109(4).

29. NAFTA Implementation Act, *supra* note 5, at 4.

30. Price, *supra* note 2, at 730.

31. *Id.*

32. NAFTA, *supra* note 1, art. 1110(2).

33. Price, *supra* note 2, at 730.

34. *Id.*

35. *Id.*

36. NAFTA, *supra* note 1, art. 1110(2).

37. Price, *supra* note 2, at 730.

government should be worried about being sued for expropriation every time it promulgates a regulation which curtails a foreign investor's business.³⁸ Moreover, rather than being worried just about the lawsuit, the compensation remedy for expropriation is extremely significant.³⁹

6. Denial of Benefits

"Article 1113 describes those circumstances under which a NAFTA government may refuse to apply the protection of Chapter 11 to firms, or their investments, that otherwise qualify for coverage under the chapter, where firms are owned or controlled by investors from a non-NAFTA country."⁴⁰ Further, each government may deny benefits to a firm owned or controlled by investors to which it is applying economic sanctions.⁴¹ Shell companies could be denied benefits if they have no substantial business activities in the NAFTA country where they are established.⁴² On the other hand, these shell companies cannot be denied benefits if they "maintain their central administration or principal place of business in the territory of, or have a real and continuous link with, the country where they are established."⁴³ However, "this provision requires the denying government to give prior notification, and to consult, in accordance with Articles 1803 and 2006."⁴⁴

7. Environmental Protections

Article 1114 provides two main environmental protections for NAFTA host countries.⁴⁵ The article indicates that "[n]othing in this Chapter shall be construed to prevent a party from adopting, maintaining or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns."⁴⁶ Further, paragraph two states, "[t]he parties recognize that it is inappropriate to encourage investment by relaxing domestic health, safety or environmental measures."⁴⁷ "Derogations from this provision are subject to compulsory consultations if requested by a NAFTA government but are not subject to

38. *Id.*

39. *Id.*

40. NAFTA Implementation Act, *supra* note 5, at 5.

41. *Id.*

42. *Id.*

43. *Id.*

44. *Id.*

45. NAFTA, *supra* note 1, art. 1114(1)(2).

46. *Id.*

47. NAFTA, *supra* note 1, art. 1114(2).

formal dispute settlement under Chapter 20.”⁴⁸ Although this provision is included in NAFTA, it has not delayed investors from suing over environmental regulations that have affected their businesses.

B. Section B

Section B sets out rules of settlement disputes between a host government and an investor of another party. It “establishes a mechanism for the settlement of investment disputes that assures both equal treatment among investors of the parties in accordance with the principal of international reciprocity and due process before an impartial tribunal.”⁴⁹ “This mechanism is patterned after the investor-State dispute settlement mechanism of the standard U.S. bilateral investment treaty and permits an investor to submit its claim to binding arbitration under internationally-accepted rules.”⁵⁰

1. Statute of Limitations

“An investor may not make a claim if more than three years have elapsed from the date on which the investor first acquired, or should have first acquired, knowledge of the alleged breach and knowledge that the investor has incurred loss or damage.”⁵¹ Similar to statutes of limitations in the United States, this provision creates the propensity for significant argument about when an investor should have first acquired knowledge of the breach.⁵² Moreover, since the inherent nature of a NAFTA investment is a “foreign” investment, the likelihood that an investor maintains a hands-off approach to foreign investment creates even more uncertainty about the ability of a defendant government in proving when the hands-off investor, if such is the case, acquired or should have acquired knowledge of the breach.⁵³ Thus, a hands-off investor seems to have a bit of an advantage in surviving the statute of limitations here, whereas a host government is at a bit of a disadvantage.⁵⁴

2. Types of Claims Allowed to be Submitted to Arbitration

There are two main categories of injury that may be submitted to arbitration: “allegations of direct injury to an investor, and allegations of

48. NAFTA Implementation Act, *supra* note 5, at 5.

49. NAFTA, *supra* note 1, art. 1115.

50. NAFTA Implementation Act, *supra* note 5, at 5.

51. NAFTA, *supra* note 1, art. 1116(b)(2).

52. *Id.*

53. *Id.*

54. *Id.*

indirect injury to an investor caused by injury to a firm in the host country that is owned or controlled by the investor.”⁵⁵ In both instances, “investors may bring claims where the injury results from an alleged breach of Section A or of certain provisions governing the behavior of government monopolies in Chapter Fifteen.”⁵⁶ “The investor-state arbitration provisions extend, subject to explicit reservations set out in NAFTA, to (1) actions taken by federal, state and provincial governments; (2) certain actions taken by state enterprises; and (3) actions taken by certain state-chartered monopolies when the actions are inconsistent with the NAFTA.”⁵⁷

Arbitration is viewed in the United States as a form of alternative dispute resolution, but under NAFTA Chapter 11, arbitration is the adjudication of a claim.⁵⁸ Nevertheless, Chapter 11 would be unclothed without a provision recommending alternative dispute resolution before commencing a binding arbitration.⁵⁹ Hence, Article 1118 provides “[t]he disputing parties should first attempt to settle a claim through consultation or negotiation.”⁶⁰

3. Arbitration Process

Pursuant to Article 1119, a “disputing investor shall deliver to the disputing Party written notice of its intention to submit a claim to arbitration at least 90 days before the claim is submitted.”⁶¹ Similarly, for a complaint filed in the United States, the written notice must specify such items as the disputant’s address, where the claim is being made, issues and factual basis of the claim, and relief sought.⁶² Then again, a claim may not be submitted to arbitration until six months have passed since the events that gave rise to the claim.⁶³

Once all of these conditions are met, an investor may submit a claim to the International Centre for the Settlement of Investment Disputes if the investor and host country are parties to the ICSID Convention.⁶⁴ If only the investor or the government is a party to the Convention but not both, the claim may be brought under the Additional Facility Rules of the

55. NAFTA Implementation Act, *supra* note 5, at 1.

56. *Id.*

57. Price, *supra* note 2, at 732.

58. NAFTA, *supra* note 1, art. 1115.

59. *Id.* art. 1118.

60. *Id.*

61. *Id.* art. 1119.

62. *Id.* art. 1119 (a)-(d).

63. *Id.* art. 1120(1).

64. NAFTA Implementation Act, *supra* note 5, at 6.

ICSID⁶⁵ or the United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules.⁶⁶ “At present, only the United States is party to the ICSID Convention. Therefore, only U.S. investors, or claims against the United States, may be heard under the Additional Facility Rules.”⁶⁷ Article 1121, however, “requires the investor . . . to consent in writing to arbitration, and to waive the right to initiate or continue any actions in local courts or other fora relating to the disputed measure, except actions for injunctive or other extraordinary relief.”⁶⁸

Although waiving a right to initiate actions in other forums may sound rather insignificant, it can cause a claim to be dismissed for lack of jurisdiction with the Arbitral panel.⁶⁹ This was indeed the case in *Waste Management Inc. v. United Mexican States*.⁷⁰ In *Waste Management*, Waste Management, Inc. filed a notice of intent to arbitrate with the ICSID on an action against the government of the United Mexican States.⁷¹ Waste Management, Inc. sought

compensation by way of damages for an alleged breach on the part of the state-owned entities, BANCO NACIONAL DE OBRAS Y SERVICIOS PUBLICOS, S.N.C. (hereinafter referred to as BANOBRAS), the MEXICAN STATE OF GUERRERO (hereinafter referred to as GUERRERO), AND THE CITY COUNCIL OF ACAPULCO DE JUAREZ (hereinafter referred to as ACAPULCO) of obligations laid down by Articles 1105 and 1110 of the North American Free Trade Agreement (NAFTA).⁷²

Pursuant to Article 1121, the claimant must waive their right to pursue the same action in any other forum.⁷³ Waste Management filed the following waiver:

Additionally, Claimants hereby waive their right to initiate or continue before any administrative tribunal or court under the law of any

65. NAFTA, *supra* note 1, art. 1120(1)(b).

66. *Id.* art. 1120(1)(c).

67. Price, *supra* note 2, at 732. See discussion *infra* Part III.

68. NAFTA Implementation Act, *supra* note 5, at 6.

69. *Waste Management, Inc. v. United Mexican States ARB(AF)/98/2*, ICSID (June 2, 2000), available at http://www.worldbank.org/icsid/cases/waste_award.pdf.

70. *Id.* § 1.

71. *Id.*

72. *Id.*

73. NAFTA, *supra* note 1, art. 1121(2)(b).

NAFTA Party, or other dispute settlement procedures, any proceedings with respect to the measures taken by Respondent that are alleged to be a breach of NAFTA Chapter Eleven and applicable rules of international law, except for proceedings for injunctive, declaratory, or other extraordinary relief, not involving the payment of damages. **This waiver does not apply, however, to any dispute settlement proceedings involving allegations that Respondent has violated duties imposed by other sources of law, including the municipal law of Mexico.**⁷⁴

Disenchanted with this waiver, specifically the highlighted exclusion, counsel for the United Mexican States requested Waste Management confirm that the waiver did not deviate from the waiver required by Article 1121.⁷⁵ In response, Waste Management sent the same waiver clause mentioned above except for the addition of the following language:

Without derogating from the waiver required by NAFTA Article 1121, Claimants here set forth their understanding that the above waiver does not apply to any dispute settlement proceedings involving allegations that Respondent has violated duties imposed by sources of law other than Chapter Eleven of NAFTA, including the municipal law of Mexico.⁷⁶

Still concerned with this waiver provision, the legal advisor for the ICSID sent a letter to Waste Management seeking confirmation that the waiver

tendered was applicable to any such dispute settlement proceedings in Mexico as might involve allegations of breaches of any obligations, imposed by other sources of law, which in substance were not different from those of the Party State under NAFTA Chapter XI, except for proceedings for injunctive, declaratory or other extraordinary relief, not involving the payment of damages.⁷⁷

Waste Management responded with the following answer to the ICSID's inquiry:

74. *Waste Management Inc.*, *supra* note 69, § 4.

75. *Id.*

76. *Id.* § 5.

77. *Id.*

With respect to the inclusion in the Notice of Institution, of the waiver required by NAFTA Article 1121 and USA Waste's understanding of the scope of that required waiver, USA Waste hereby **confirms that the waiver contained in the Notice of Institution applies to dispute settlement proceedings in Mexico involving allegations of breaches of any obligations, imposed by other sources of law, that are not different in substance from the obligations of a NAFTA State Party under Chapter Eleven of the NAFTA**, except for proceedings for injunctive, declaratory, or other extraordinary relief, not involving the payment of damages. **With respect to USA Waste's efforts to resolve its dispute with Mexico outside of the remedies offered by NAFTA, there are no pending legal proceedings related to that dispute in which the Government of the United Mexican States is a named party.**⁷⁸

The Government of Mexico vehemently disagreed that this waiver and confirmation was within the terms laid out in Article 1121.⁷⁹ The Government of Mexico evidenced this assertion with proof that there were current proceedings being brought against BANOBRAS and ACAPULCO.⁸⁰ Finally, in November of 1996, the Government of Mexico submitted a question of jurisdiction to ICSID alleging that Waste Management had not given the proper waiver in accordance with Article 1121.⁸¹

Most noteworthy for international investors, the Arbitral Tribunal held that a waiver was a unilateral act under NAFTA Article 1121.⁸² The tribunal stated that the waiver "implies a voluntary abdication of rights, inasmuch as this act generally leads to substantial modification of the pre-existing legal situation, namely, the forfeiting or extinguishment of the right."⁸³ The panel went on to state that "[w]hatever the case, any waiver must be clear, explicit and categorical, it being improper to deduce same from expressions the meaning of which is at all dubious."⁸⁴ Further, the panel indicated that the conduct of the party asserting the waiver must be reviewed to see if there is a difference between sentiments manifested and

78. *Id.*

79. *Id.* § 6.

80. *Waste Management Inc.*, *supra* note 69, § 6.

81. *Id.*

82. *Id.* § 18.

83. *Id.*

84. *Id.*

the actual conduct.⁸⁵ This means that the panel investigated the separate actions being brought against BANOBRAS and ACAPULCO to decide if they were different from the allegations brought under Chapter 11.⁸⁶ The tribunal recognized that in the other two suits brought under Mexican law rather than NAFTA, those actions could be held separate from NAFTA.⁸⁷ Nevertheless, those actions could also be derived from the same measures as the NAFTA lawsuit.⁸⁸ When this is the case, a NAFTA cause of action and a separate but derivative claim may not co-exist.⁸⁹ If this were not the case, the claimant would be entitled to double benefits in its claim for damages.⁹⁰

In deeming the waiver submitted by Waste Management invalid, the panel stated that Waste Management “did not limit itself to a full transcription of the content of this Article.”⁹¹ Instead, the tribunal found that Waste Management “introduced a series of statements that reflected its own understanding of the waiver submitted, as is evident from the findings of fact outlined in this arbitral award now issued hereunder.”⁹² The panel went on to state that Waste Management “systematically failed to comply with the actual agreement that the waiver of Article 1121 requires.”⁹³ Further, Waste Management did not intend to present “the waiver within the terms prescribed in NAFTA Article 1121, rather, it had the intention to present it in accordance with its own interests.”⁹⁴

Since the Arbitral Tribunal found the waiver submitted by Waste Management was invalid,⁹⁵ and the waiver was a condition precedent of arbitration under the ICSID, the ICSID was without jurisdiction to decide the claims brought by Waste Management.⁹⁶ The tribunal found no bad faith on the part of Waste Management so both parties were responsible for their own legal fees.⁹⁷ However, Waste Management had to bear the expense of this arbitral proceeding.⁹⁸

85. *Waste Management Inc.*, *supra* note 69, § 24.

86. *Id.* § 27(b).

87. *Id.*

88. *Id.*

89. *Id.*

90. *Id.*

91. *Waste Management Inc.*, *supra* note 69, § 31.

92. *Id.*

93. *Id.*

94. *Id.*

95. *Id.*

96. *Id.*

97. *Waste Management Inc.*, *supra* note 69, § 31.

98. *Id.*

This was an expensive lesson learned by Waste Management. However, this case serves as a caution for future foreign investors and states who wish to try to circumvent the waiver required by NAFTA Article 1121.

III. WHO IS THE ICSID?

The ICSID is a product of the World Bank. "On a number of occasions in the past, the World Bank as an institution and the President of the Bank in his personal capacity have assisted in mediation or conciliation of investment disputes between governments and private foreign investors."⁹⁹ The rise of the ICSID in 1966 was partly meant to alleviate the World Bank President and his staff of the aggravation of becoming involved in these disputes.¹⁰⁰ "But the Bank's overriding consideration in creating ICSID was the belief that an institution specially designed to facilitate the settlement of investment disputes between governments and foreign investors could help to promote increased flows of international investment."¹⁰¹

"Established under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States in 1966, the ICSID has an Administrative Council and a Secretariat."¹⁰² Headed by the World Bank's President, the Administrative Council has one representative of each state that has ratified the convention.¹⁰³ "Annual meetings of the council are held in conjunction with the joint Bank/Fund annual meetings."¹⁰⁴

Even though the ICSID is a self-governing international organization, it has close connections with the World Bank.¹⁰⁵ "All of the ICSID's members are also members of the Bank."¹⁰⁶ "Unless a government makes a contrary designation, its Governor for the Bank sits *ex officio* on ICSID's Administrative Council."¹⁰⁷ "The expenses of the ICSID Secretariat are

99. The World Bank Group, *About ICSID*, at <http://www.worldbank.org/icsid/about/about.htm> (last visited Sept. 10, 2001) [hereinafter The World Bank Group].

100. *Id.*

101. *Id.*

102. *Id.*

103. *Id.*

104. *Id.*

105. The World Bank Group, *supra* note 99.

106. *Id.*

107. *Id.*

financed out of the Bank's budget, although the costs of individual proceedings are borne by the parties involved."¹⁰⁸

"Pursuant to the Convention, ICSID provides facilities for the conciliation and arbitration of disputes between member countries and investors who qualify as nationals of other member countries."¹⁰⁹ ICSID conciliation and arbitration are completely voluntary.¹¹⁰ Once parties have agreed to arbitrate under the ICSID Convention, neither party may withdraw its consent without the consent of the other.¹¹¹ In addition, all countries that are members of the ICSID, regardless if they are parties to the dispute, must validate and require compliance with ICSID arbitral awards.¹¹²

Other than supplying facilities for conciliation and arbitration, since 1978 the Centre has had a set of Additional Facility Rules empowering the ICSID Secretariat to manage specific types of proceedings between foreign nationals and states that fall outside the realm of the Convention.¹¹³ "These include conciliation and arbitration proceedings where either the State party or the home State of the foreign national is not a member of the ICSID."¹¹⁴ "Additional facility conciliation and arbitration are also available for cases where the dispute is not an investment dispute provided it relates to a transaction which has 'features that distinguishes it from an ordinary commercial transaction.'"¹¹⁵ Moreover, the Additional Facility Rules allow the ICSID to conduct certain proceedings not covered in the convention, "namely fact-finding proceedings to which any State and foreign national may have recourse if they wish to institute an inquiry 'to examine and report on facts.'"¹¹⁶

The ICSID also performs another activity. "A third activity of the ICSID in the field of settlement of disputes has consisted in the Secretary-General of the ICSID accepting to act as the appointing authority of arbitrators for ad hoc (i.e., non-institutional) arbitration proceedings."¹¹⁷ "This is most commonly done in the context of arrangements for

108. *Id.*

109. *Id.*

110. *Id.*

111. The World Bank Group, *supra* note 99.

112. *Id.*

113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.*

117. The World Bank Group, *supra* note 99.

arbitration under the Arbitration Rules of UNCITRAL, which are specially designed for ad hoc proceedings.”¹¹⁸

Certain areas on ICSID arbitration are prevalently seen in “investment contracts between governments of member countries and investors from other member countries.”¹¹⁹ Prior approval by governments to settle investment disputes by ICSID arbitration is commonly seen in “about twenty investment laws and in over 900 bilateral investment treaties.”¹²⁰ “Arbitration under the auspices of ICSID is one of the main mechanisms for the settlement of investment disputes under four recent multilateral trade and investment treaties including, NAFTA, the Energy Charter Treaty, the Cartagena Free Trade Agreement and the Colonia Investment Protocol of Mercosur.”¹²¹

ICSID proceedings do not have to be held in Washington D.C., the Centre’s headquarters, pursuant to the ICSID Convention.¹²² Any other venue that is acceptable to both parties is acceptable to the ICSID.¹²³ “The ICSID Convention contains provisions that facilitate advance stipulations for such other venues when the place chosen is the seat of an institution with which the Centre has an arrangement for this purpose.”¹²⁴ Up to the present time, the ICSID has used other venues such as the “Permanent Court of Arbitration at the Hague, the Regional Arbitration Centre of the Asian-African Legal Consultative Committee . . . the Australian Centre for International Commercial Arbitration at Melbourne, the Australian Commercial Disputes Centre at Sydney, the Singapore International Arbitration Centre and the GCC Commercial Arbitration Centre at Bahrain.”¹²⁵ Several of these arrangements have validated their usefulness in many instances. Not only have they settled disputes, but they have also “helped to promote cooperation between ICSID and these institutions in several other respects.”¹²⁶

The ICSID has experienced a significant augmentation in the amount of cases submitted to the Centre in recent years.¹²⁷ “These include cases brought under the ICSID Convention and cases brought under the ICSID

118. *Id.*

119. *Id.*

120. *Id.*

121. *Id.*

122. *Id.*

123. The World Bank Group, *supra* note 99.

124. *Id.*

125. *Id.*

126. *Id.*

127. *Id.*

Additional Facility Rules.”¹²⁸ “The ICSID also carries out advisory and research activities relevant to its objectives and has a number of publications.”¹²⁹ The Centre works with other World Bank group units in filling “requests by governments for advice on investment and arbitration law.”¹³⁰ “The publications of the Centre include multi-volume collections of Investment Laws of the World and of Investment Treaties, which are periodically updated by the ICSID staff.”¹³¹ “Since April 1986, the Centre has published a semi-annual law journal entitled ICSID Review-Foreign Investment Law Journal.”¹³² Recently, the journal was rated as one of the top twenty international and comparative law journals in the United States.¹³³ “Since 1983, the Centre has also co-sponsored, with the American Arbitration Association (AAA) and the International Chamber of Commerce (ICC) International Court of Arbitration, colloquia on topics of current interest in the area of international arbitration.”¹³⁴

IV. CASES

A. *Metalclad Corporation v. United Mexican States*

Metalclad is a Newport Beach, California waste disposal company, which adds insulation to pipes, ducts, furnaces, boilers, and other industrial equipment and includes maintenance, repair and removal.¹³⁵ The company, primarily a West Coast operation, also provides asbestos abatement services.¹³⁶ Metalclad filed a complaint with the ICSID in January of 1997 alleging that the Mexican State of San Luis Potosi transgressed several NAFTA provisions when the state prevented a Metalclad subsidiary, Quimica Omega de Mexico, from commencing the operation of its waste disposal plant.¹³⁷ The facility was taken over by Metalclad on the condition

128. *Id.*

129. The World Bank Group, *supra* note 99.

130. *Id.*

131. *Id.*

132. *Id.*

133. *Id.*

134. *Id.*

135. Hoover's Online, *Metalclad Corporation Company Capsule*, at <http://www.hoovers.com/co/capsule/2/0%2C2163%2C45952%2C00.html> (last visited Sep. 4, 2000).

136. *Id.*

137. Public Citizen Global Trade Watch, *Our Future Under the Multilateral Agreement on Investment* at <http://www.citizen.org/pctrade/nafta/cases/metalcla.htm> (last visited Aug. 9, 2000) [hereinafter *Our Future Under the Multilateral Agreement*].

that it would cleanup preexisting contaminants.¹³⁸ The plant had a history of contaminating local ground water.¹³⁹

NAFTA only allows Metalclad to file suit against Mexico's federal government.¹⁴⁰ Regardless, the federal Environmental Ministry claims that it was not involved "in designating the ecological zone because such activities fall under state government jurisdiction."¹⁴¹ "According to Clyde Pearce, a lawyer for Metalclad, the defense is 'claiming that it followed some normal procedures' in canceling the project."¹⁴² He also stated that "even if it did, that doesn't matter because those procedures violate the guarantees of NAFTA."¹⁴³

Metalclad chief executive officer Grant Kesler feels that Mexico could suffer, if Metalclad should lose the case. Kesler stated, "[i]f we get screwed, who else is going to take the risk of going down there?" Kesler is confident that Metalclad would be able to collect on any award by the tribunal because "we have the right to attach Mexican assets in the United States, which would include their account at the World Bank. There is no way to avoid paying a NAFTA award." This whole dispute could have been avoided, according to Mr. Kesler, except for the actions of "a single Mexican governor."¹⁴⁴

There are only two other hazardous waste facilities in Mexico for a country that generates more than eight million tons of hazardous waste a year.¹⁴⁵

An environmental impact assessment was conducted and revealed that the plant "[laid] atop an ecological sensitive underground alluvial

138. *Id.*

139. *Id.*

140. *Mexico: Metalclad Sues Mexico under NAFTA*, 8 WORLD ARB. & MEDIATION REP. 288 (1997).

141. *Id.*

142. David R. Adair, Comment, *Investors Rights: The Evolutionary Process of Investment Treaties*, 6 TULSA J. COMP. & INT'L L. 195, 207 (1999) (citing Mark Thompson, O.C. *Firm Applies for Investment Protection*, L.A. DAILY J., Jan. 29, 1998, at A1). Metalclad operates facilities in eight Mexican states. Metalclad waited to file its NAFTA dispute until the last day of a three-year statute of limitations that would have barred some of the company's claims. Company officials met with Mexican trade officials, ambassadors, and cabinet ministers, trying every political and diplomatic avenue possible. *Id.*

143. *Id.*

144. *Id.*

145. *Mexico: Metalclad Sues Mexico under NAFTA*, *supra* note 140.

stream.”¹⁴⁶ From that assessment, the governor declared the site part of a 600,000-acre ecological zone and refused to allow Metalclad to reopen the facility.¹⁴⁷ Metalclad alleged that this action “effectively expropriated its future expected profits and seeks \$90 million in damages.”¹⁴⁸ Metalclad alleged that this taking of the company’s property, commonly known as environmental zoning, under the property rights provided by NAFTA requires that the “offending government compensate the company.”¹⁴⁹

Without NAFTA’s forceful provision on expropriation, Metalclad by itself would be compelled to assume the risks of investment. Metalclad learned a valuable lesson for all investors: conduct proper environmental assessments before committing significant capital to an investment.¹⁵⁰ This case is demonstrative of how “certain non-market related risks of investment could be shifted from companies to governments.”¹⁵¹

There are other questions raised by this case. Metalclad alleged “the Mexican Federal government is (unofficially) encouraging the company’s NAFTA lawsuit so that it can deflect the political fall-out of forcing the state to open the facility.”¹⁵² The local community was “never consulted about the possibility of reopening the facility by either the federal or state governments or Metalclad, and vehemently opposes locating a toxic dump in its area.”¹⁵³ The local community is still suffering from the water contamination exuded by the previous owners who indulged in illegal storage procedures.¹⁵⁴

The case raises yet another troublesome possibility.¹⁵⁵ “If Metalclad’s claim that the Mexican federal government supports the suit is indeed accurate, this case raises the disturbing possibility that investors can use their rights to collude with governments to force unwanted, or even dangerous investments on unwilling populations.”¹⁵⁶

On August 30, 2000, the Arbitral Panel found “Mexico must be held to have taken a measure tantamount to expropriation in violation of

146. *Our Future Under the Multilateral Agreement*, *supra* note 137.

147. *Id.*

148. *Id.*

149. *Id.*

150. *Id.*

151. *Id.*

152. *Our Future Under the Multilateral Agreement*, *supra* note 137.

153. *Id.*

154. *Id.*

155. *Id.*

156. *Id.*

NAFTA Article 1110(1).”¹⁵⁷ As a result of this finding, Metalclad was awarded \$16,685,000.00 in damages.¹⁵⁸ The result in this case helps to establish the scope and power of expropriation provision.¹⁵⁹

B. Ethyl Corporation v. Government of Canada

Ethyl Corporation (Ethyl) of Richmond, Virginia brought a lawsuit against the Government of Canada in April of 1997.¹⁶⁰ The Canadian Parliament decided to place the interests of its citizens before Ethyl’s right to sell products in Canada through NAFTA.¹⁶¹ Unable to ban the use of the well-known and dangerous gasoline additive MMT under the Canadian Environmental Protection Act, the Parliament banned the import and interprovincial transport of MMT produced by Ethyl.¹⁶² Ethyl retaliated by bringing this lawsuit against the Government of Canada under the NAFTA Chapter 11 expropriation provision.¹⁶³ Ethyl sought restitution of \$251 million and alleged that the ban on importing MMT into Canada was expropriation of its MMT production plant and excellent reputation.¹⁶⁴

MMT, produced only by Ethyl, has usually been known as a dangerous and toxic product.¹⁶⁵ It is a toxic manganese-based compound that is added to gasoline to strengthen octane and lower engine knocking.¹⁶⁶ Legislators in Canada were concerned that the MMT emissions created a consequential public health risk.¹⁶⁷ “Automobile manufacturers have long argued that MMT damages emissions diagnostics and control equipment in cars,” therefore increasing general emissions.¹⁶⁸ The use of MMT is tracked by the Environmental Defense Fund (EDF), and the EDF indicated that MMT is only used in Canada.¹⁶⁹ The U.S.

157. *Metalclad v. United Mexican States*, ARB(AF)/97/1 (Aug. 30, 2000), available at <http://www.worldbank.org/icsid/cases/awards.htm>.

158. *Id.*

159. *Our Future Under the Multilateral Agreement*, *supra* note 137.

160. *Adair*, *supra* note 142, at 208.

161. Public Citizen Global Trade Watch, *Ethyl Corporation vs. Government of Canada: Now Investors Can Use NAFTA to Challenge Environmental Safeguards*, at <http://www.citizen.org/pctrade/harmonizationalert/NAFTA/ethyl.htm> (last visited Aug. 24, 2000) [hereinafter *Ethyl Corporation vs. Government of Canada*].

162. *Id.*

163. *Id.*

164. *Id.*

165. *Id.*

166. *Id.*

167. *Ethyl Corporation vs. Government of Canada*, *supra* note 161.

168. *Id.*

169. *Id.*

Environmental Protection Agency has banned the use of MMT in reformulated gasoline in the United States.¹⁷⁰ Reformulated gasoline makes up around one third of the U.S. gasoline market.¹⁷¹ However, it should be noted, the State of California has implemented a total ban on MMT.¹⁷²

Known as the third and largest lawsuit brought under Chapter 11, this suit settled recently when Canada agreed to pay Ethyl \$13 million and repeal its ban on MMT.¹⁷³ This settlement creates a plethora of issues that should concern policy-makers.¹⁷⁴ Most importantly, this is the latest indication that “international investment and trade agreements are leading to the elimination of important environmental, consumer, health and human rights laws.”¹⁷⁵

First, this case seems to indicate that a government must compensate investors when it wants “to regulate them or their products for public health or environmental reasons.”¹⁷⁶ “Under NAFTA, the presumed ‘right’ of corporations to be compensated when public health regulations affect a company’s bottom line is treated as the moral equivalent of the public’s right not to be harmed by industrial toxins.”¹⁷⁷ This case could be construed by investors to mean that demanding compensation from host governments for the burdens of complying with the government’s environmental concerns creates a competent and fruitful business strategy.¹⁷⁸ For this reason, “the effect on environmental regulation could be chilling.”¹⁷⁹

Second, the result of this case could increase the number of frivolous lawsuits brought against host governments.¹⁸⁰ Usually, governments are the only entities to have “standing to bring a case against a regulation” under international agreements.¹⁸¹ Therefore, the political and diplomatic

170. *Id.*

171. *Id.*

172. *Id.*

173. Public Citizen Global Trade Watch, *Another Broken NAFTA Promise: Challenge by U.S. Corporation Leads Canada to Repeal Public Health Law* at <http://www.citizen.org/pctrade/t/NAFTA/cases/ethyl.htm> (last visited Aug. 24, 2000) [hereinafter *Another Broken NAFTA Promise*].

174. *Ethyl Corporation vs. Government of Canada*, *supra* note 161.

175. *Another Broken NAFTA Promise*, *supra* note 173.

176. *Ethyl Corporation vs. Government of Canada*, *supra* note 161.

177. *Id.*

178. *Id.*

179. *Id.*

180. *Id.*

181. *Id.*

pressure placed on governments helps to ensure a lack of frivolous lawsuits.¹⁸² However, Chapter 11 provides the investor with the ability to bring the suit himself, and the settlement value of this case could persuade the previously weary investor to file suit.¹⁸³

In considering new regulations, lawmakers may now be intimidated by private investors with the threat of a lawsuit.¹⁸⁴ In this case, Ethyl filed suit six months prior to the passing of the MMT ban by the Canadian legislature.¹⁸⁵ Ethyl's purpose was to threaten the lawmakers with a multimillion-dollar suit in hope that it would deter them from passing the MMT ban.¹⁸⁶ Obviously, Ethyl was unsuccessful in its threat.¹⁸⁷ In the future, investors now armed with the ability to file suit against a host government may very well be successful with their threats.¹⁸⁸ This could have tantamount ramifications, as the legislative process as a whole could be considerably undermined.¹⁸⁹

Corporations can seek an unlimited amount of damages under Chapter 11.¹⁹⁰ Corporations may request damages for actual and future earnings as well as compensation to repair its loss of goodwill.¹⁹¹ Consequently, there is a possibility that these suits could drain state treasuries.¹⁹² The \$251 million that Ethyl sought and the \$13 million that it settled for could be the genesis of investor complaints seeking astronomical figures in compensation.¹⁹³ Moreover, any number of corporations have the ability to consolidate their suits, which could have the effect of multiplying a government's potential payout.¹⁹⁴

Several critics of NAFTA had voiced their concerns that the agreement would hinder the ability of governments to legislate on significant matters such as environmental protection and public health.¹⁹⁵ NAFTA supporters easily dismissed these concerns; however, the Ethyl

182. *Ethyl Corporation vs. Government of Canada*, *supra* note 161.

183. *Id.*

184. *Id.*

185. *Id.*

186. *Id.*

187. *Id.*

188. *Ethyl Corporation vs. Government of Canada*, *supra* note 161.

189. *Id.*

190. *Id.*

191. *Id.*

192. *Id.*

193. *Id.*

194. *Ethyl Corporation vs. Government of Canada*, *supra* note 161.

195. *Id.*

case has proven that those concerns were legitimate.¹⁹⁶ This is of particular significance because Chapter 11 “could be used by more than 350 million individuals and corporations” within the NAFTA countries.¹⁹⁷

C. *Azinian v. United Mexican States*

In this case, Robert Azinian and others are citizens of the United States and shareholders of Desechos Solidos De Naucalpan S.A. de C.V. (Desona), a Mexican corporate entity.¹⁹⁸ In 1992, at the invitation of Azinian the Mayor of Naucalpan, Mexico and members of its City Council, or “Ayuntamiento,” visited Los Angeles to observe operations of Global Waste Industries, Inc., controlled by Azinian.¹⁹⁹

The Mayor and the Ayuntamiento were looking for a solution to their city’s solid waste problem.²⁰⁰ Naucalpan is a large and important suburb of Mexico City.²⁰¹ At the time, the waste collection of the city was in disarray and much of the city’s equipment was inadequate and obsolete.²⁰² The city of Naucalpan entered into a \$20 million, fifteen-year concession contract with Desona.²⁰³

Desona did not provide the five rear load vehicles as required by the concession contract.²⁰⁴ In fact, of the seventy state-of-the-art vehicles required by the contract only two front loaders were provided.²⁰⁵ The Ayuntamiento became concerned and canceled the contract.²⁰⁶ Azinian brought suit under Chapter 11 “seeking recovery for the loss of the value of the concession contract as an ongoing enterprise.”²⁰⁷ The total claim for damages was \$19.2 million.²⁰⁸

The arbitral panel found that Azinian and others “had presented themselves as principals in Global Waste, with approximately forty years of experience in the industry.”²⁰⁹ Subsequently, it was revealed that Global

196. *Id.*

197. *Id.*

198. *Azinian v. United Mexican States*, ARB(AF)/97/2 (1999), ICSID (W. Bank).

199. *Id.*

200. *Id.*

201. *Id.*

202. *Id.*

203. *Id.*

204. *Azinian v. United Mexican States*, ARB(AF)/97/2 (1999), ICSID (W. Bank).

205. *Id.*

206. *Id.*

207. *Id.*

208. *Id.*

209. *Id.*

Waste was incorporated in 1991 and filed for bankruptcy in 1992.²¹⁰ The panel also found that Azinian did not have forty years of experience in the waste management industry; rather, he had a long record of unsuccessful commercial litigation.²¹¹ Hence, the arbitral panel held that Azinian's claim failed entirely.²¹²

The importance of this case does not lie within its substantive ruling. Rather, contrary to the Ethyl decision comments, the case is a prime example that claimants will not be able to threaten and use Chapter 11 as a sword.²¹³ This decision indicates to host governments that a threat of a law suit under Chapter 11, much like any other lawsuit, requires some legitimate claim to effectuate settlement.²¹⁴ Although Chapter 11 gives the individual investor the power to sue the host government, it also provides the host government a shield to protect itself from frivolous suits.²¹⁵

D. Lowen Group v. United States

In 1995, Jeremiah O'Keefe a Biloxi, Mississippi businessman, brought suit against The Lowen Group, Inc. (Lowen).²¹⁶ The suit alleges that Lowen, a Canadian corporation, was strategizing to control the local funeral market and that the group committed various other predatory and anti-competitive acts "designed to drive O'Keefe's local funeral and insurance companies out of business."²¹⁷ O'Keefe alleged that Lowen refused to honor a contract that gave O'Keefe exclusive rights to funeral and insurance services in the area.²¹⁸

A Mississippi jury assessed compensatory damages of \$100 million and punitive damages of \$400 million against Lowen.²¹⁹ Mississippi state law requires that a losing defendant, who wishes to appeal without beginning to pay damages, post a bond worth 125% of the damages owed.²²⁰ The case was eventually settled for \$150 million.²²¹

210. *Azinian v. United Mexican States*, ARB(AF)/97/2 (1999), ICSID (W. Bank).

211. *Id.*

212. *Id.*

213. *Id.*

214. *Id.*

215. *Id.*

216. Public Citizen Global Trade Watch, *Canadian Corporation Found Liable in Mississippi Courts Uses NAFTA to Claim Legal System Violated its Right*, at <http://www.citizen.org/pctrade/nafta/cases/Lowen.htm> (last visited Aug. 24, 2000) [hereinafter *Canadian Corporation Found Liable*].

217. *Id.*

218. *Id.*

219. *Id.*

220. *Id.*

From this case, Lowen derived a Chapter 11 cause of action against the United States.²²² Lowen claimed that the Mississippi bond requirement of 125% of the damages assessed expropriated its assets without providing compensation.²²³ Further, it argued that “the Mississippi Supreme Court denied it justice in violation of NAFTA by not exempting it from the state law bond requirement.”²²⁴ “Lowen is in effect arguing that the very civil justice system allowing jury trials violated the company’s NAFTA-guaranteed rights to fair and equal treatment and non-discrimination.”²²⁵ It is seeking compensation from the U.S. government in taxpayer dollars for the settlement value of the O’Keefe case, \$150 million, and the later plunge in the value of the its stock, which it claims was a direct result of the lawsuit.²²⁶

The consequences of Lowen’s NAFTA lawsuit could be severe. The lawsuit threatens the core of our nation’s civil justice system.²²⁷ If Lowen is successful, legal precedent would be created that would allow other corporations to exploit it and escape liability for its wrongful acts.²²⁸ If successful, the floodgates would open to allow any type of civil action or court rule, on a foreign NAFTA corporation to be challenged as illegal under NAFTA.²²⁹ Jury verdicts, especially for products liability, could readily be overturned.²³⁰

Punitive damages could disappear if Lowen’s attack on them is successful under NAFTA.²³¹ For many years, corporations have tried to no avail to lobby Congress to cap or eliminate punitive damages.²³² If punitive damages disappear as a result of being deemed illegal under NAFTA, once again the legislative process would be undermined.²³³ Even more important, “U.S. taxpayers not corporate defendants could end up footing the bill when a corporation is found liable by a jury for injury to others,

221. *Id.*

222. *Canadian Corporation Found Liable, supra* note 216.

223. *Id.*

224. *Id.*

225. *Id.*

226. *Id.*

227. *Id.*

228. *Canadian Corporation Found Liable, supra* note 216.

229. *Id.*

230. *Id.*

231. *Id.*

232. *Id.*

233. *Id.*

wiping out both the concept of fairness and the deterrent effect of our liability system.”²³⁴

Many U.S. corporations, however, have already done something very similar against the governments of Canada and Mexico.²³⁵ The U.S. corporations have successfully challenged environmental and public health regulations in Canada and Mexico.²³⁶ With the United States involved in talks to expand NAFTA to the entire Western Hemisphere, the pool of investors and corporations which could sue the United States is immeasurable.²³⁷

E. *S.D. Myers Case*

Similar to the Ethyl case, in July of 1998, another U.S. corporation filed suit against the Canadian government under Chapter 11.²³⁸ “S.D. Myers, an Ohio company specializing in the cleaning of hazardous waste,” brought an action against the Canadian government for the ban of polychlorinated biphenyls (PCBs), an extremely hazardous coolant used in electricity transformers.²³⁹ The Canadian government had banned the export of PCBs for a period of fifteen months in 1995.²⁴⁰ S.D. Myers alleges that this ban cost the company \$15 million and was an expropriation of its business.²⁴¹

The Canadian government had concerns that the PCBs might not be properly disposed of in the United States and might return to contaminate the Canadian environment.²⁴² The Canadian government alleges that the ban was instituted to comply with the international obligations under the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal.²⁴³ After fifteen months, the ban was

234. *Canadian Corporation Found Liable*, *supra* note 216.

235. Public Citizen Global Trade Watch, *The Importance and Implication of Lowen's NAFTA Suit*, at <http://www.citizen.org/pctrade/nafta/cases/importance.htm> (last visited Aug. 24, 2000).

236. *Id.*

237. *Id.*

238. Public Citizen Global Trade Watch, *NAFTA Investor-State Provision, Polychlorinated Biphenyls (PCBs)*, at <http://www.harmonizationalert.org/Sept98/naftapcb.htm> (last visited Aug. 28, 2000) [hereinafter *NAFTA Investor-State Provision*].

239. *Id.*

240. *Id.*

241. *Id.*

242. Kevin Banks, *NAFTA'S Article 1110-Can Regulation Be Expropriation?*, 5 *NAFTA: L. & BUS. REV. AM.* 499 (1999).

243. *Id.*

finally rescinded.²⁴⁴ However, the ban was only rescinded for treatment and destruction of hazardous waste and did not include landfills.²⁴⁵ Therefore, S.D. Myers alleged that during those fifteen months, the ban had prevented the company from completing its existing contracts that involved the exportation of PCBs.²⁴⁶ S.D. Myers is praying for \$6.3 million in damages.²⁴⁷

Similar to the Ethyl case, the S.D. Myers case has environmentalists worried about the safety of the environment and the health of the citizens.²⁴⁸ If S.D. Myers is able to recover or settle like Ethyl, there is a sincere threat that governments will no longer ban toxic substances.²⁴⁹ It seems clear that if governments are subject to multi-million dollar lawsuits for banning toxic substances, they will no longer be able to afford the luxury of protecting their environment and citizens with environmental protection laws.²⁵⁰ The question then becomes where to draw the line. Many will argue that Chapter 11 gives investors and companies a power that will inevitably be detrimental to citizens and the environment.²⁵¹ Conversely, investors must have the ability to hold host governments accountable for their actions.²⁵² It appears that there might be a way to compromise.²⁵³ It might be possible to restrict the ability to file a law suit, and perhaps hold out certain environmental issues that would not include the power to sue.²⁵⁴

V. RESULTS

In essence, the question to be resolved by most of the cases brought under NAFTA Chapter 11 thus far is: When is regulation really expropriation?²⁵⁵ It is readily apparent that the current NAFTA provision defining investment, Article 1139, is extremely broad.²⁵⁶ In that provision, "investment" is a term that encompasses several different property

244. *Id.*

245. *Id.*

246. *NAFTA Investor-State Provision, supra* note 238.

247. *Id.*

248. *Id.*

249. *Id.*

250. *Id.*

251. *Id.*

252. *NAFTA Investor-State Provision, supra* note 238.

253. *Id.*

254. *Id.*

255. *Banks, supra* note 242, at 499.

256. *Id.*

interests including equity and debt securities, real estate, interests from commitment of capital and various contracts.²⁵⁷

It has been argued that the scope of Article 1139 could be limited to provide a better definition of what is really protected from expropriation with compensation.²⁵⁸ Further, it has been argued that compensation should only be awarded in cases where the property value is totally destroyed or almost totally destroyed.²⁵⁹ Conversely, the broad language of Article 1139 mitigates these arguments. Thus, if the drafters did not want to include such a broad provision in NAFTA, they would not have included such a broad array of property interests protected from expropriation with the ability to seek compensation if expropriated. “Moreover, [Article 1139] is unlikely to be read narrowly given that international law has traditionally recognized that expropriation compensation claims may be made in respect of a wide range of property interests.”²⁶⁰

One of the stronger arguments in limiting the expropriation provision includes dividing or redefining property rights.²⁶¹ The nature of the argument is to isolate the property interests that are more likely to be affected by regulation and only allow those certain interests the ability to seek compensation.²⁶² Nevertheless, this argument also has its opposition.²⁶³ Defining which property interests are more likely to be affected by a regulation could be a magnanimous task.²⁶⁴ Although ascertaining which large groups of property interests might be affected by a government regulation would be uncomplicated, it is the smaller groups of property interests, which are intertwined or ancillary to the larger interest that will create a laborious task.²⁶⁵ It has been said however, that “[a]n astute producer, anticipating the possibility of regulation of its products, might even arrange its investments so as to receive some compensation in the event of regulation.”²⁶⁶

For many years it has been recognized by legal scholars and international tribunals that a government should not be liable for

257. *Id.* at 508.

258. *Id.*

259. *Id.*

260. *Id.*

261. Banks, *supra* note 242, at 499.

262. *Id.*

263. *Id.*

264. *Id.*

265. *Id.* at 508-509.

266. *Id.* at 509.

economic injury caused by a legitimate state regulation.²⁶⁷ It is unfortunate that the description of economic injury and legitimate state regulation is extremely vague.²⁶⁸ Only regulations regarding public health, safety, and the environment have been recognized as regulations which may be regarded as non-compensable takings.²⁶⁹

In contravention to this long-recognized police power of the governments, "at least one review of international tribunal decisions has concluded that the public purpose of the measure is not by itself sufficient to establish the exercise of a police power."²⁷⁰ The language in Article 1110 is analogous to this perception.²⁷¹ Therefore, the conclusion appears to be that "since deference can be expected from international tribunals in the face of a state's assertion of a public purpose, the key to understanding the police power exception to international compensation rules lies in the distinction between bona fide regulation and compensable measures."²⁷²

In deciding expropriation claims, current arbitration tribunals have relied on judicial and arbitral precedent.²⁷³ However, the term "expropriation" per se has rarely been defined by international jurisprudence.²⁷⁴ It seems that international arbitration panels and scholars are far more concerned with developing the rules that govern expropriation rather than defining the term itself.²⁷⁵ In almost all international cases regarding whether or not an expropriation has occurred, it was decided that an expropriation occurred.²⁷⁶ "Indeed, as late as 1986, a careful reviewer of international tribunal decisions, international investment treaties, and state practice concluded that the boundary line between regulation and expropriation remained essentially undefined in international law."²⁷⁷

The Iran-United States Claims Tribunal (Tribunal) is the leading source of decisions on international law of expropriation.²⁷⁸ The Tribunal holds the most extensive set of state arbitrations ever undertaken.²⁷⁹ When

267. Banks, *supra* note 242, at 510.

268. *Id.*

269. *Id.*

270. *Id.*

271. *Id.*

272. *Id.*

273. Banks, *supra* note 242, at 514.

274. *Id.*

275. *Id.*

276. *Id.*

277. *Id.*

278. *Id.*

279. Banks, *supra* note 242, at 514.

the Shah of Iran was overthrown in 1979, there were thousands of claims made by Iranian property owners in the United States and American property owners in Iran.²⁸⁰ “The Tribunal has rendered approximately fifty awards addressing claims for the taking of property arising out of those events.”²⁸¹

Analogous to Chapter 11, the Iran-United States Claim Tribunal contains language that is extremely broad.²⁸² The Tribunal calls for authority to resolve disputes that arise out of expropriations and other measures affecting property rights.²⁸³ This is similar language to NAFTA Article 1110, which includes “measures tantamount,” arguably even broader than the Tribunal’s language.²⁸⁴ “Moreover, as one member of the Tribunal has noted, the breadth of its jurisdiction may have led to a certain degree of laxity on the part of the Tribunal in maintaining definitional distinctions between terms such as ‘expropriation,’ ‘appropriation,’ ‘deprivation,’ ‘taking,’ and ‘other measures affecting property rights.’”²⁸⁵

The Tribunal, no matter how broad its language, still provides several useful points of reference.²⁸⁶ The cases in which the Tribunal has decided what expropriation means have established a ceiling for the expropriation definition.²⁸⁷ As a result, the Tribunal has been hesitant to distinguish between expropriation and other measures affecting property rights.²⁸⁸ Further, when the Tribunal makes a decision that a certain regulation does not give rise to compensation, it can be taken as a reliable indicator that the same regulation should not give rise to compensation under NAFTA Chapter 11.²⁸⁹

VI. CONCLUSION

This comment on Chapter 11 provides the individual foreign investor with insight into its provisions, as well as the relatively few cases that have been brought under this investment section of NAFTA. Investors should now be well aware of the ICSID and its basic functions. Investors, as well

280. *Id.*

281. *Id.*

282. *Id.* at 515.

283. *Id.*, quoted in Claims Settlement Declaration, Jan. 20, 1981, U.S.-Iran, art. II, 20 I.C.M. 230, 231.

284. *Id.*

285. Banks, *supra* note 242, at 515.

286. *Id.*

287. *Id.*

288. *Id.*

289. *Id.*

as citizens of NAFTA countries, could be affected by the expropriation provision of NAFTA. Finally, it is apparent that this provision may be too broad and needs to be addressed because the environmental and public health ramifications could be tantamount.

A. Chapter 11 Provisions

1. Section A

Section A of NAFTA Chapter 11 provides the definition of investor and investment.²⁹⁰ It is obvious that the terms are defined very broadly to include an overabundance of property interests.²⁹¹ Section A provides for nondiscriminatory treatment, performance requirements, managerial regulation, transfers, expropriation and compensation, denial of benefits and environmental protections.²⁹²

Non-discriminatory treatment means that NAFTA governments are required to treat investors and their investments no less favorably than their own domestic investors or investments.²⁹³ A host government may not impose equity requirements of a foreign investor or require that investor to sell his investment.²⁹⁴

A host government may not impose any performance requirements on international investors.²⁹⁵ They may neither require a firm to export a certain percentage of output nor may they require a firm to achieve a certain trade balance.²⁹⁶ The implementation of performance requirements causes trade distortions to be eliminated, and host countries are further prevented from placing performance requirements on their own investors.²⁹⁷

A host government may not require senior management positions of a foreign NAFTA firm to be filled with local nationals.²⁹⁸ However, the host government may force firms to have a majority of the board of directors filled by local nationals.²⁹⁹ Although this provision was intended to prevent local persuasion, it is evident that having the board of directors filled with local nationals hinders its purpose.

290. Price, *supra* note 2, at 728.

291. *Id.*

292. *Id.*

293. *Id.* at 729.

294. *Id.*

295. *Id.*

296. Price, *supra* note 2, at 729.

297. *Id.*

298. *Id.*

299. *Id.*

Each NAFTA government must permit monetary transfers relating to an investment to be made freely and without delay.³⁰⁰ A government, however, may prevent a transfer of funds if the firm is in bankruptcy or has committed any criminal offenses.³⁰¹ Thus, the blocking of a transfer must be made in a good faith application of the government's laws.³⁰²

Arguably, the most important provision so far is the expropriation and compensation provision. A NAFTA government may not expropriate any investment made by an investor of another NAFTA country other than for a public purpose, on a non-discriminatory basis, and in accordance with due process of law.³⁰³ Should a government expropriate a NAFTA investor's investment, it is required to pay compensation without delay equal to the fair market value of the investment.³⁰⁴ As noted earlier, this provision has been the subject of a majority of the few cases brought under NAFTA Chapter 11. The expropriation provision is overly broad and is subject to abuse by NAFTA investors. Consequently, this abuse could cause detrimental effects to the environment or public health.

A government may deny the benefits of Chapter 11.³⁰⁵ A government may deny benefits if the government is currently applying economic sanctions to the home country of the investor or if the investor has no substantial business activity in the NAFTA country where they are established.³⁰⁶ This provision is mainly directed at shell companies.³⁰⁷ However, even a shell company may be provided benefits if it is the company's principal place of business.³⁰⁸

Finally, Section A does provide host governments some environmental protections.³⁰⁹ It provides that Chapter 11 should not be construed to prevent a party from adopting regulations to make sure investments are undertaken in an environmentally sensitive manner.³¹⁰ However, this protection has not been universally enforced. As seen in the *Ethyl* case, investors are able to escape this provision by claiming expropriation regardless of the environmental issues. Therefore, this

300. *Id.*

301. NAFTA Implementation Act, *supra* note 5, at 4.

302. *Id.*

303. *Id.*

304. *Id.*

305. *Id.*

306. *Id.*

307. NAFTA Implementation Act, *supra* note 5, at 5.

308. *Id.*

309. *Id.*

310. *Id.*

provision, at least so far, has not been used to defend an expropriation suit over environmental regulations.

2. Section B

All of the rules of settlement dispute resolution are set out in Section B.³¹¹ This section provides a mechanism to settle investment disputes that assures equal treatment and due process before an impartial tribunal.³¹² Section B describes the statute of limitations, the types of claims allowed to be submitted to arbitration, and the arbitration process.³¹³ All investment disputes, if not negotiated, will be settled before the ICSID.³¹⁴

a. *The ICSID*

The ICSID provides facilities for the conciliation and arbitration of disputes between member countries and investors who qualify as nationals of other member countries.³¹⁵ ICSID conciliation and arbitration is entirely voluntary, but once parties have agreed to arbitrate, neither party may withdraw its consent.³¹⁶ Also, all countries that are members of the ICSID, whether or not they are parties to the dispute, must recognize the arbitration award.³¹⁷ The ICSID also provides Additional Facility Rules, which enables the ICSID to provide a venue for arbitration or conciliation where either the state party or home state of the foreign national is not a member of the ICSID.³¹⁸ A final activity the ICSID performs is the ad hoc arbitration. This usually surfaces in the performance of arbitration proceedings under UNCITRAL.³¹⁹

b. *Cases*

Most of the cases discussed throughout this comment have dealt with the issue of whether or not host government promulgation of environmental regulations is expropriation. The most noteworthy seem to be the *Ethyl* and *Metalclad* cases. Although the *Ethyl* case settled, the Canadian government ended up paying a high price for the suit.³²⁰ Canada relinquished a ban on MMT, which they believed was dangerous to its

311. NAFTA, *supra* note 1, art. 1115.

312. *Id.*

313. *Id.* art. 1116-1117.

314. *Id.* art. 120.

315. The World Bank Group, *supra* note 99.

316. *Id.*

317. *Id.*

318. *Id.*

319. *Id.*

320. *Another Broken NAFTA Promise*, *supra* note 173.

environment and public health, and paid \$13 million to settle.³²¹ Moreover, *Metalclad*, provides clear precedent for exactly what the expropriation provision means for governments and investors.

c. Results

The expropriation provision of NAFTA has several fallacies. The provision is too broad and investors have already begun to exploit its breadth. This expropriation provision needs to be narrowed so the environmental protection and public health of any country is never compromised. Moreover, the United States, Mexico, and Canada should create an ad hoc committee to review the expropriation provision of Chapter 11. The purpose of this committee should be to create ideas for narrowing this provision so that all countries maintain the ability to protect its public health and environment as it deems necessary. However, it seems that this will not happen until one country, likely the United States, suffers serious financial discomfort from defending and/or losing a Chapter 11 expropriation lawsuit.

321. *Id.*

