

What To Expect On Investment Arbitration In NAFTA Reboot

By **Caroline Simson**

Law360, New York (August 23, 2017, 1:24 PM EDT) -- Despite tough talk that the U.S. is looking to do more than tweak the North American Free Trade Agreement during the ongoing renegotiations, experts say it's unlikely that the deal's investor-state dispute settlement provision will be among those targeted for substantive reform.

Ahead of the NAFTA talks that took place in Washington, D.C., last week, a trade official with the Office of the U.S. Trade Representative told reporters that the office is still considering how it will approach investment protection in the renegotiated deal. Those comments came a month after USTR released its summary of objectives for the then-upcoming talks calling for greater transparency within NAFTA's dispute settlement and a provision that NAFTA country investors in the U.S. are not accorded greater substantive rights than domestic investors — though the summary did not directly refer to the investor state arbitration provision in NAFTA, Chapter 11.

In that same list of objectives released in July, USTR made clear it intends to target a separate arbitration mechanism for trade disputes known as Chapter 19. The statement sets the stage for a showdown with Canada, which unequivocally stated earlier this month that it will not agree to nixing the controversial trade panels. But there doesn't seem to be any indication that the parties are queuing up a similar brouhaha over Chapter 11.

"If you really thought they were putting Chapter 11 in the crosshairs, you would have expected there to be a lot more commentary about it," said Nigel Blackaby, global head of the international arbitration group at Freshfields Bruckhaus Deringer LLP. "They've not been shy about attacking Chapter 19, and so the absence of any commentary or even any mention of the Chapter 11 [investor state dispute settlement provision] suggests to me that it's not really going to be a topic."

Still, it does seem likely that there will be some attempt by the NAFTA parties to modernize Chapter 11.

On Aug. 14, Canadian Foreign Affairs Minister Chrystia Freeland said that they would look to reform Chapter 11 to "ensure that governments have an unassailable right to regulate in the public interest," and to incorporate labor and environmental safeguards. It's part of their efforts to make NAFTA look more like the country's more progressive recent trade deal with Europe, the Comprehensive Economic and Trade Agreement, or CETA.

The Chapter 11 reform proposals put forward by the U.S. and Canada will be familiar to those

who've kept abreast of efforts to reform the global investor state dispute settlement, or ISDS, provisions that are in the vast majority of trade deals throughout the world. In fact, within the U.S. and Canadian statements so far on potential reform of Chapter 11 are echoes of the U.S.'s negotiating tactics for the abandoned Trans-Pacific Partnership, which included provisions recognizing nations' inherent right to regulate to protect public welfare objectives and ensuring full transparency in cases.

"Really both of those are consistent with their negotiating stances in both CETA and TPP, so these are neither new nor extraordinary," said Ian Laird, co-chair of the international dispute resolution group at Crowell & Moring LLP, referring to the U.S. and Canadian NAFTA reform proposals. "Even if you go back to NAFTA itself, Chapter 11 has ... a similar provision listing out these key regulatory and policy areas, and making it clear that the chapter won't prevent a party from fully regulating in those spaces."

And the NAFTA parties had already targeted transparency in the deal back in 2001, when the NAFTA Free Trade Commission adopted certain interpretations of Chapter 11 to clarify its meaning.

Similar provisions may now be written into the modernized agreement rather than being expressed as interpretive notes, according to Squire Patton Boggs partner Stephen Anway, who co-heads the firm's investment arbitration division of its international arbitration group. He noted there could also be room for the environmental or labor carveouts called for by the Canadians. Similar provisions were included in a 2012 model bilateral investment treaty released by the Obama administration.

"Any such moves would be entirely consistent with efforts by recent [bilateral investment treaties/free trade agreements] to give more prominence to a host state's regulatory authority and to enhance transparency," he said. "They likely would not call into question the viability generally of global ISDS, but rather fit within the recent trend of rebalancing the procedural and substantive aspects of the international legal relationship between states and investors."

The 2001 interpretive notes also clarified that the concept of "fair and equitable treatment" did not require treatment beyond that which is required by the customary international law minimum standard. The U.S.'s current proposal that NAFTA country investors not be accorded greater substantive rights than its domestic investors goes a step beyond that, but it's unclear right now how much the U.S. will emphasize this point.

The position could backfire if, for example, Canada insisted on similar provisions — meaning that U.S. investors would have rights only under Canadian law, which has a narrower definition of what can form a basis for a claim for damages as a result of an expropriation, according to Clifford Sosnow, a partner with the Canadian firm Fasken Martineau.

"If you want to do that across all three NAFTA countries, then U.S. investors, who frankly are singularly benefiting from Chapter 11, could actually have rights scaled back," he said.

With regard to ISDS reform, CETA was particularly noteworthy in that it was one of the first trade deals to incorporate the European Commission's new investor court, meant to replace the current ad hoc arbitration system incorporated in so many trade deals throughout the world that's come under scrutiny in recent years. Critics say ISDS is a secretive system where unaccountable tribunals made up of international lawyers and academics can award unlimited damages to multinational corporations at the expense of taxpayers.

But the investor court rollout has been far from smooth. It's not included in a provisional application of

CETA set to go into force next month, and the commission hasn't made any headway in convincing other trading partners, like Japan, to incorporate the court into their trade deals.

Although Freeland mentioned in her speech that Canada's efforts to make NAFTA more progressive would be "informed" by the ideas in CETA, she made no mention of the court as part of the NAFTA talks. It's unlikely the U.S. would agree to such a provision, given the American business community's resistance to including the court in the now-abandoned Transatlantic Trade and Investment Partnership deal that was to be between the U.S. and Europe.

"My sense is that it remains a European initiative, and more specifically, an EU initiative. I don't see it spreading at the moment beyond that," said Blackaby. "I think the U.S. has been well-served by investment arbitration generally, both the country itself and U.S. investors abroad."

And indeed, the business community seems rattled by the prospect of any substantive reform to NAFTA's Chapter 11. Earlier this month, more than 100 of the country's most influential business groups pleaded with the Trump administration to maintain and upgrade Chapter 11, calling it an "essential" part of NAFTA.

And from what's been said publicly thus far, it seems apparent that the three NAFTA countries are in agreement on this point.

"I don't see any impetus on behalf of any of these three governments to do away with ISDS — the fundamental idea that an investor can go to arbitration if there's a breach of treaty protections — and I don't see anything that significantly imperils rights to nondiscrimination, fair and equitable treatment, and [protection from] expropriation, which have been the cornerstones of these treaties," said Grant Hanessian, chair of Baker & McKenzie LLP's arbitration group in North America. "The demise of ISDS may have been exaggerated."

--Editing by Rebecca Flanagan and Kelly Duncan.