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Progressive Conservative Party of Canada.
Blue Ribbon Panel to Review Canada's Free Trade Agreements.
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Assessing NAFTA:

Putting Chapter 11's Investor-State Dispute Settlement System in Context

Among the many challenges we face when trying to assess the impact of the various international economic agreements that Canada has signed over the past 15 years, three stand out.

First we need to understand how transformations in the global economy are changing the previous model of government in which states managed their own economies by fine-tuning aggregate demand, put in place a basic welfare system, and thereby set the framework within which corporations produced and labor worked. For several decades, rapid changes in information technology – particularly the development of computers, satellite communications, and digitalization – have made possible transborder production and marketing systems that are regional and sometimes global in scope. As a result, corporations can avoid government taxes by manipulating transfer pricing and become autonomous of monetary policy through financing their operations on global markets.

Second, we need to distinguish the impact of domestic forces, such as the Canadian Charter of Rights and Freedoms which has been particularly significant in promoting indigenous peoples' rights, from the impact of the ideological shift among political elites, who have embraced neoconservative values since the early 1980s, when the previous paradigm of Keynesian management lost legitimacy throughout the industrialized world in the wake of Margaret Thatcher and Ronald Reagans' rise to power. In the Canadian case, the neoconservative revolution that was initiated by Brian Mulroney and Michael Wilson was completed by Jean Chrétien and Paul Martin at the federal level and introduced in the provinces of Alberta, Ontario, British Columbia, and now Québec, where cutting back government became an end in itself.

Thirdly, when trying to grasp the significance of bilateral (Canada-United States Free Trade Agreement – CUFTA, 1989), trilateral (North America Free Trade Agreement – NAFTA, 1994), and multilateral (World Trade Organization – WTO, 1995), we need to see how the process that created these treaties was driven by the United States' own international economic goals and how these differed from the Canadian government's policy objectives.

To unravel the varying impacts of these internal factors and external forces requires a careful analysis of the different sectors of the Canadian political economy. Having spent several years undertaking this labour in order to write my recent book *Uncle Sam and Us: Globalization, Neoconservatism, and the Canadian State* (University of Toronto and Woodrow Wilson Presses, 2003), I will not try to summarize this analysis. As a serious inquiry, I take it for granted that this committee's staff will consider the analysis in *Uncle Sam and Us* along with that of other analysts who have different points of view. So instead of summarizing this large and comprehensive study, I will focus on one innovation specific to NAFTA – and not included in the WTO – which could actually be changed should the Canadian government decide to take on the problem of a dramatic – and in some analysts' opinion unconstitutional – innovation known now in popular discourse as "Chapter 11."

I HISTORICAL CONTEXT

Prior to the advent of the Canada-United States Free Trade Agreement (CUFTA, 1989), Canada's international trade obligations were set out in the General Agreement on Tariffs and Trade (GATT, 1947). Initially an International Trade Organization (ITO) had been negotiated to be a strong trade-policy complement to the World Bank and the International Monetary Fund that had been set up in 1944. When the ITO fell victim to the U.S.Congress' unwillingness to have American policy fettered, GATT emerged as a weak arrangement limited to moderating government policy affecting international trade in goods. Compliance with the provisions of GATT was a matter of good will among the Parties to the Treaty.

Fast forwarding to the mid-1980s, the United States tabled an agenda for dramatically expanding the GATT framework to include areas of economic and social regulation that had never previously been the subject of international trade disciplines and which often had little, if anything**,** to do with international trade in a conventional sense. Its motivations for demanding a transformation of the world's economic rules were complex and multifaceted: enormous and growing trade deficits; the need to secure access to strategic resources such as oil and gas; and the global ambitions of its domestic sectors that had established a competitive lead in knowledge-driven technologies such as pharmaceuticals, software, biotechnology, and entertainment.

To accomplish its strategy to change the global regulatory system, the United States adopted a three-pronged strategy -- unilateral, multilateral and bilateral --- to contain what it regarded as the excessive and interventionist policies of foreign governments by requiring them to abandon export controls on energy and other strategic goods, while opening their own markets in areas where American transnational corporations (TNCs) had developed global superiority.

Unilateral Measures. Washington strengthened its already powerful unilateral measures, in the form of anti-dumping and countervailing duties laws, that were invoked either for its own protectionist purposes or to pressure other countries to abandon policies that it regarded as too restrictive to American exporters, investors, or service providers.[i]

Multilateral Measures. At the international level, Washington wanted GATT to cover:
- foreign investment so as to improve conditions for its TNCs' overseas operations;
- services, to open space for its TNCs in countries which had not established competitive or open markets in such areas as telecommunications, health care, insurance, electricity or cultural industries; and
- intellectual property protection, to globalize the patent and copyright protections granted under U.S. law.

The prospects for getting GATT members to change its rules were not promising, since resistance came from both North and South. The European Union (EU) wanted to maintain the state aids to industry and subsidies for its farmers that the U.S. was targetting. Leading Third-World countries such as Brazil and India also feared that U.S.-made economic rules would prevent their using the same kind of supportive policies to accelerate their entrepreneurs in the twenty-first century that the United States had used so successfully in the nineteenth.

Bilateral Measures. Given this political logjam at the GATT, the United States decided to pursue bilateral negotiations with more compliant trading partners with whom it hoped to set precedents that would provide prototypes for its multilateral negotiating agenda. Thus in 1986 as it tabled proposals to expand the GATT framework, Washington was also engaged in bilateral negotiations with Canada that would culminate, a scant two years later, in CUFTA's signing.

CUFTA represented a radical departure from conventional notions of where the demarcation line between domestic and international trade policy naturally belonged. For the first time a trade agreement brought the vast, but uncharted territory of business and government services under international disciplines which to that point had applied only to goods. Thus the obligation to provide "national" or non-discriminatory treatment was now to apply, not just to goods or products, but to such services as banking operations and insurance contracts, legal and architectural work, health care, and even education.

Another of CUFTA's novel features was the incorporation of rules concerning foreign investment within the framework of an international trade agreement. Pursuant to these **"**disciplines**"**, Ottawa now agreed to apply the principle of "national treatment" to investment. This meant that Canadian governments were now committed to treating U.S. investors the same way they treated domestic citizens and corporations – a concession that Canada had long resisted because of its economy's high proportion of foreign direct investment. By offering U.S. companies the same incentives that it might give domestic firms, Canada abandoned the kinds of industrial strategies aimed at promoting local enterprise, employment, and innovation that had formerly constituted much of federal and provincial economic policy.

The Canadian government further agreed in NAFTA Article 1106 to give up imposing "performance measures" whether or not these involve foreign investors. The constraint covered not just the federal but also provincial and municipal governments. British Columbia, for instance, has long attached conditions to resource extraction or forest harvesting licenses to increase domestic value-added processing. Municipalities often attach local purchase requirements to the contracts and approvals they give. Even if non-discriminatory as far as the nationality of the company involved, such performance requirements are now forbidden.

Finally, CUFTA established rules for energy trade which assured U.S. consumers virtually unfettered access to Canadian energy resources for as long as the agreement remained in place and at prices no higher than those charged to Canadian consumers. This meant Canada was prohibited from imposing export controls on oil, gas and electricity except in times of shortage. Even then, exports could not be restricted any more than domestic supplies were rationed to Canadian markets.

The second phase of North America's evolution as a trade bloc represented a simultaneous broadening and deepening of the system already established by CUFTA. The North American Free Trade Agreement broadened the free trade regime to include Mexico, and also expanded CUFTA's limits on its signatory governments by expanding its institutional structure, adding a chapter creating extensive intellectual property rights, changing CUFTA's dispute settlement mechanism, extending the coverage of its investment provisions, and adding to those investment disciplines a new dispute resolution procedure that empowered Canadian, U.S., and Mexican-based corporations to sue the governments of other NAFTA Parties.

One critical consequence of radically expanding the scope of international trade law in this manner, was to extend the threat of international economic sanctions to a host of domestic policies concerning services and investment, which previously had been entirely matters of national or local concern. Under these regimes a municipal zoning ordinance may become the subject of an international claim, as may groundwater protection legislation, cultural programs to support library services, and even the pension plan of postal workers.[ii]

The significance of these changes went well beyond simply changing economic policies. NAFTA's formal stipulations created at the continental level of North America a new legal order by which its three member states were to be bound. In other words, NAFTA had established new and comprehensive disciplines to which the policies, laws, and constitutional norms of its member states were obliged to conform.

II: THE NEW TRADE AGREEMENTS AS EXTERNAL CONSTITUTIONS

When a country signs a treaty it *internationalizes* the state's legal order to the extent that domestic laws are harmonized with the norms embodied in the accord. Before the advent of the new global trade order, literally hundreds of international treaties, conventions and other instruments had little effect on the constitutional norms of the nation state, whose legal sovereignty was barely compromised by such undertakings.[iii] Weak enforcement mechanisms allowed a state to ignore or abrogate its international commitments. Nor was a government bound to comply with an international body's ruling that it considered adverse to its interests or incompatible with its culture. Even as determinedly a team player as Canada, was on occasion willing to flout international law that challenged a constitutional norm.[iv]

The literature on the political significance of NAFTA generally discusses how, in sharp contrast with most international agreements, it created a mode of economic regulation with such broad scope and such unusual judicial authority that it transformed the political order of the three states that are parties to it.[v] Taking this argument one step further, I maintain that NAFTA so closely conforms to the conventional notions of what comprises a constitution that it can best be understood as creating an external constitution for its signatories.

As rule books that determine how political systems operate, constitutions generally contain five basic components.

(a) *Norms.* Understood as regularized constraints on behaviour, supralegislative norms are contained in constitutions to put certain values beyond the reach of legislators and officials.

(b) Institutions. Constitutions define the parameters of formal rule-making institutions, their administrative agencies, and enforcement or compliance regimes.

(c) Limits. Constitutions also set limits to the powers of the institutions that they create.

(d) *Rights.* The corollary of these limits are the rights with which the system's citizenry are endowed.

(e) Adjudication. To interpret the ambiguities inherent in these norms, limits, and rights and to resolve eventual disputes a judicial system is required.

The rest of this section applies this model to show how NAFTA effectively functions as a constitutional instrument.

(a) Norms.

Constitutions typically entrench certain inviolate principles or norms that are above the capacity of any politician to alter, and NAFTA has done this by establishing several government-inhibiting principles which apply to all policies, regulations, and actions of member states. In agreeing that CUFTA should enshrine the principle of *national treatment*, or *most favoured nation treatment,* Canada was not simply reiterating a commitment that it had made for goods in GATT, but was agreeing to apply these normative trade rules to investments and services as well.

NAFTA's Article 1110 established an absolute right to compensation, at fair market value, whenever a government measure is determined to have "directly or indirectly" expropriated a foreign investment or is "tantamount to nationalization or expropriation." Unless justified as being in the public interest, the taking of private property by governments is unlawful, quite apart from the issue of compensation. The protection of private property enshrined in these provisions concerning expropriation established another norm that is superimposed on statutory, common law, and constitutional principles concerning property.

Thus certain key international trade disciplines establish supraconstitutional norms because they are established as a superior legal order, binding broad spheres of government policy law and action. These may not be reflected in the domestic laws of the nation state, but can be enforced by international sanctions regardless of their status under, or consistency with, domestic laws or constitutional norms.

(b) Institutions.

In contrast to free trade in the European Union, NAFTA did not create continent-wide executive, legislative, or bureaucratic institutions of any substance. NAFTA's central institution, the Free Trade Commission has no permanent location or budget and amounts to little more than periodic meetings of the three Parties' ministers of trade.[vi] NAFTA's decision-making was to be by consensus, which meant that each 'party' retained a veto over common business.

Two collateral institutions were established as adjuncts to NAFTA. One, the North

American Commission for Labour Cooperation (NACLC) is overseen by an executive comprised of the three national governments' labour ministers.[vii] The other, the North American Commission on Environmental Cooperation is similarly constituted under the direction of the Parties' respective federal environmental officials. The mandate of these regimes is to ensure the effective enforcement of domestic labour and environmental laws. Neither obliges environmental or labour legislation to be raised to any specific threshold. Nor do the agreements prevent the signatory states from lowering environmental protections and labour rights. Having no meaningful enforcement regime, both commissions are condemned to being largely hortatory.

(c) Limits.

NAFTA contains two types of supraconstitutional limits on member states' domestic institutions, including governments at all levels, administrative agencies and tribunals, and state entreprises. Positive, 'thou shalt' provisions *prescribe* how members must rewrite, for example, their laws on intellectual property. Negative, 'thou shalt not' clauses *proscribe* a wide range of practices such as regulations or performance requirements of foreign direct investment.

One manifestation of NAFTA's supraconstitutional effect, can be found in the specific amendments made to domestic policies, laws, and regulations in order to bring them formally into compliance with NAFTA disciplines. Normally, changes in laws and regulations are made by governments within the institutional and legal framework established by their internal constitutions and in response to demands from below by the electorate or specific functional constituencies. Unlike these normal amendments to statutes made by sovereign legislatures, which can further amend or revoke their acts in response to changing domestic considerations, statutory amendments incorporating international trade norms can be validly amended only if the external regime changes its rules by international agreement. Otherwise, democratically legitimate government actions deemed by the appropriate arbitration procedures to violate the international agreement in question will subject that government to sanctions or penalties.

Whether or not domestic law and policy is formally amended, governments must still comply with the trade rules on pain of exposing themselves to international sanctions for non-compliance. That Canada's NAFTA obligations are binding on it, whether or not it has chosen to ensure conformity of its domestic law, underlines their supraconstitutional character.

The coercive force of Canada's commitments under NAFTA and other international trade agreements can be found in the nature of the penalties that it may suffer should it fail to comply with those commitments. It is not uncommon for example for international trade sanctions to be claimed in the billions of dollars with ruinously disruptive implications for the domestic economy, particularly one as dependent upon foreign trade as is Canada.

Moreover cross retaliation allows sanctions to be targeted strategically where they will have greatest effect. For example, when the U.S. objected to Canada's response to an adverse WTO ruling concerning certain cultural policies to protect Canada's magazine publishing industry, it proposed to target $1 billion of Canadian exports to the United States. Steel exports from Canada, much of which were produced -- not coincidentally -- in the riding of Canada's Heritage Minister, were to bear the brunt of these threatened sanctions.[viii]

Some might maintain that Canada's sovereignty remains intact because it is free to abrogate NAFTA upon giving its NAFTA partners six months notice. However, this formal right needs to be set against the political-economic dynamic in North America. Once a government has adjusted its statutes and once its economy has been restructured in accordance with the free-trade model, it becomes practically speaking impossible to abrogate the agreement that brought about this transformation. It is very difficult to imagine Canada abrogating NAFTA in the face of opposition from south of the border. And the United States would certainly attempt to hold Canadian governments to the trade rules that secure its strategic objectives, not the least of which is guaranteed access to Canadian petroleum and energy resources. The potential impact of a breakdown in trade relationships with the U.S. would devastate the Canadian economy which is so dependent upon international trade, fully 87 per cent of which is with the United States. So even if Canada has a *de jure* right to extricate itself from the obligations assumed under NAFTA, there is no practical possibility of doing so.

(d) Rights.

As the corollary to limiting government, a state constitution establishes specific rights for its citizens, whether individual or collective. But the only 'citizens' whose rights in Canada were extended by continental governance are corporations and individuals that can claim the status of foreign investors, or investments of foreign investors. These individuals and entities not only have rights and entitlements under NAFTA not available to Canadian citizens (corporate or otherwise) but have also been accorded a unilateral right to enforce those rights against the Parties to NAFTA (investor-State claims).

In 1980, when Parliament debated what should be included in the proposed new Charter of Rights and Freedoms, property rights were excluded on the grounds that they were adequately protected under the common law. In other words, the right to property was not to be absolute in Canada, but conditioned by broader societal objectives. For instance, the public interest in sound land-use planning in a municipality could have priority over the interests of entrepreneurs and developers striving to maximize the value of their property interests. But under NAFTA, private property protection is absolute. This means that an American investor could now win damages against a Canadian city on the basis that – whatever its public policy goals -- the value of its subsidiary's property had been ‘expropriated.’[ix]

(e) Judiciary.

Norms, limits on institutions, and citizens’ rights rapidly become dead letters without a judicial system to interpret and apply the constitution’s texts and authorize meaningful sanctions in cases of non-compliance. Without access to adjudication, the expansion of international trade regimes would probably not have been of any more consequence than the International Labour Organization’s many conventions, which are rhetorically powerful but practically powerless. The new generation of international economic agreements, of which NAFTA is a prototype, constrain sovereign authority much more substantially than did their predecessors not just because of their expanded breadth but because of their judicial mechanisms’ considerable strength.

Trade liberalization is typically promoted as a means for depoliticizing disputes that erupt periodically between nation states. Recent trade agreements address this challenge by establishing binding international rules to be immune from the political manipulation that so often characterized the application of U.S. domestic trade remedies. With the exception of Chapter 11's investor-State claims, NAFTA has not created a continental level of judicial governance. Under Chapter 19, for example, a Party may seek review of another’s anti-dumping determinations, but only for the purpose of ascertaining whether such measures are consistent with the domestic law of the Party imposing the measures. The effectiveness of Chapter 20 procedures for resolving state-to-state disputes is limited, because panels only make advisory rulings which ultimately return to the political arena for solutions to be negotiated by the NAFTA free trade commission.[x] Although weak in its capacity for constraining governments’ trade-remedy protectionism and for adjudicating inter-governmental trade disputes, NAFTA has established with Chapter 11 an unprecedentedly powerful mechanism through which foreign corporations may discipline governments’ regulation- and policy-making activities, particularly in the area of environmental controls.

III NAFTA’S INVESTOR-STATE DISPUTE ARBITRATION

Before NAFTA, a Mexican or American company whose Canadian subsidiary was hurt because of a Canadian government’s action had either to defend itself within Canada’s legal system or to persuade its own government to launch a trade complaint. Even if there were grounds for doing so, political leadership might have second thoughts about attacking another country’s policies in this way in case it jeopardized other mutual interests such as military collaboration. NAFTA’s innovation was to put the arbitration machinery of international commercial regimes at the direct service of foreign investors who could now enforce rights they enjoyed thanks to an international treaty to which they were not parties, but under which they had no obligations.[xi]

Article 1110 provides that no government may ‘directly or indirectly expropriate or nationalize’, or take ‘a measure tantamount to expropriation or nationalization’ except for a ‘public purpose,’ on a ‘non-discriminatory basis,’ in accordance with ‘due process of law and minimum standards of treatment’ and on ‘payment of compensation.’[xii] This provision has now been invoked to challenge a diverse array of policy and regulatory actions taken by federal, provincial, or municipal governments that have been charged with expropriating foreign investments. This ‘Chapter 11' prohibition of actions ‘tantamount to expropriation’ was itself tantamount to a new constitutional property right, but one that was only available to NAFTA Party subsidiaries of foreign-based TNCs.[xiii] This has proven the most controversial of the external constitution’s provisions, because it allows foreign corporations to invoke secretive international dispute procedures to challenge a broad spectrum of domestic policy and legal matters, from the delivery of postal services, to the regulation of gasoline fuel additives.

Chapter 11's investor-state dispute process introduces an extraordinary foreign element into the sphere of Canadian public law. In effect, this dispute mechanism withdraws an aspect of public law from governmental control by internationalizing -- though in a private tribunal format -- the domestic legal process which previously dealt with conflicts over public policy. Not only has Chapter 11 added to the Canadian constitution a new corporate property right that treats corporations unequally depending on their nationality; it has also imported an existing arbitration mechanism designed to handle international commercial disputes, turning it into a device to constrain governments’ public policy-making capacity.

Arbitral rulings made under this system may be enforced directly by foreign investors (under Part B of the chapter. They are also amenable to state-to-state enforcement under Chapter 20, in which case they would ultimately depend upon the willingness of the Parties to implement an adverse dispute ruling.

Because the investor-State dispute process is independent of political control, litigation pursued under its aegis exerts an influence over a broad sphere of domestic policy and law. This constraint of sovereign legislative action has several facets.

Arbitral Awards are Binding and Enforceable

Unlike state-to-state procedures, investor-state tribunals are empowered to make damage awards which are binding and enforceable in Canada, as they are in more than a hundred nations that provide for the recognition and enforcement of international arbitral awards.

Unpredictability in Investor-State Litigation Creates Regulatory Chill

Because of the tribunals’ independence of the political process and because NAFTA has no formal judicial structure to impart coherence, the interpretation of NAFTA’s rules under Chapter 11 procedures varies considerably from case to case. Moreover, the absence of any doctrine of judicial precedent, leaves each tribunal to decide its own approach to interpreting NAFTA disciplines.[xiv] This ad hocery combined with the broad, novel, but often ill-defined character of many NAFTA norms contributes to a new condition of regulatory uncertainty. Policy and law makers wishing to steer clear of NAFTA prohibitions have to navigate a course through a mine field where the hazards are constantly shifting. As Muthucumaraswamy Sornarajah has written,

The notoriety, cost and potential liability associated with trade challenges and investor-State claims have been described as producing a "chill" over the development of domestic policy and law by governments. Moreover the inclination to engage in this form of self-censorship is accentuated when the ambit of the constraints imposed by a particular international commitment are unknown or uncertain. Negotiators of NAFTA and officers implementing its provisions have stated that the nature of the litigation that has resulted from Chapter 11 was unforeseen.[xv]

There is considerable evidence that the threat of Chapter 11 litigation is sufficient to warn governments away from taking policy and regulatory initiatives that respond to democratic demands even if they are entirely legitimate under Canadian law. An illustrative case is Ottawa's debacle over cigarette packaging. In the mid-1990s, the federal government tabled proposals to ban differentiated cigarette packaging. This was a natural extension of its prohibition of cigarette advertising Although the tobacco industry claimed that its packaging served no other purpose than to promote competition for existing smokers, the government maintained that branding was targeted at lifestyle marketing and thus promoted increased sales and smoking.[xvi] After being threatened with a Chapter 11 claim that the proposed legislation was tantamount to expropriation, government officials abandoned their plans.

In at least two of the cases brought against Canada, Ottawa has quickly settled with the disputing investor.[xvii] In one, Ethyl Corporation of Virginia, producer of an octane-enhancing chemical, objected to the Canadian government's banning the cross-border trade of its MMT. Ethyl had been unable to persuade Washington to request a dispute panel against Canada under Chapter 20, NAFTA's regular process for resolving conflict between governments. Since the U.S. Environmental Protection Agency had banned MMT as a dangerous neurotoxin since 1977, Washington was unwilling to expend political capital on contesting Canada's right to ban trade in the same substance. Using Chapter 11's provision on investor-state disputes, Ethyl was able to bypass its government's reluctance to fight on its behalf. It put forward a claim that Ottawa's legislated ban on the fuel additive had cost it U.S. $250 million in lost business and future profits.[xviii]

Canada actually rescinded regulations effectively banning the use of the toxic fuel additive, offering Ethyl Corporation what amounted to a public apology for having regulated the substance in the first place.[xix] In addition to the $19 million paid to Ethyl as part of the settlement, and the costs of unsuccessfully defending the measure, the political embarrassment of having to beat a hasty and public retreat also exerted a constraint on government enthusiasm for pursuing future environmental and public health initiatives that might aggrieve foreign investors.

The MMT case revealed how Canadian environmental policy, once thought to be the purview of the sovereign legislature, has been taken hostage by continental governance. Under the supraconstitutional aegis of Chapter 11, the issue is no longer the classic Canadian question of *which* level of government -- federal or provincial -- can initiate an environmental regulation. The issue now became *whether any* level of government could initiate such legislation if it jeopardizes the interests of a Mexican or American company.[xx] Far from the polluter's paying to rectify the externalities that it caused, Chapter 11's expropriation clause leads to the polluters being paid to keep on polluting.[xxi]

The constraining influence of these international trade agreements has already been institutionalized in domestic policy formation. The federal government has established a process for vetting policy proposals for their potential to generate damaging suits mounted by foreign governments or corporations.

Adding further to the chilling effect of these international disciplines, the range of government "measures" that may be subject to foreign investor claims extends beyond that for which legal sanctions would be available under the common law. Even a minister speaking to a piece of legislation or regulation in a debate in the House of Commons about the need for an environmental regulation could attract litigation by the manufacturer of the impugned substance on the grounds that the public criticism of its product has damaged its good will and so is tantamount to expropriation.

The Internationalization of Legal Norms

Since American corporate law tends to dominate international commercial law cases, conflicts between U.S. corporations and the Canadian state will inexorably cause U.S. legal definitions to infiltrate Canadian legal standards and force Canadian governments to operate as if American law on 'regulatory takings' applied to them. While some observers expected that Canadian, American, and Mexican jurisprudence would interpret 'expropriation' differently in each country,[xxii] it is generally acknowledged that panel findings will impose the U.S. interpretation instead of the other two signatories' legal notions.[xxiii]

Chapter 11 dispute settlement violates many values held dear in the common law tradition.

Judicial Sovereignty

Through the privatization of legal disputes concerning state actions, judicial sovereignty has become another casualty of this extraordinary addition to the Canadian legal order.

When the place of arbitration is chosen to be someplace outside the jurisdiction whose measure is being challenged, no judicial supervision may be exercised by that country's courts.

Chapter 11 tribunal rulings are subject to judicial review (which can only deal with matters of jurisdiction) but not to appeal (which can rehear the merits of a case). When the U.S. waste-disposal company Metalclad used Chapter 11 to attack the environmental order made by a Mexican village that had shut down its landfill site, the arbitrators, who met in Washington, ruled in the firm's favour. Because the tribunal had named Vancouver as its nominal address, the Mexican government's only recourse was to the Supreme Court of British Columbia which considered the review under B.C.'s provincial legislation providing for the review of foreign arbitral awards arising from commercial disputes.

For Canadian governments, the lack of an appeal process subverts the notion that the decision of a tribunal will ultimately adhere to the most fundamental notions of justice that have been woven into the fabric of its constitutional democracy. Because arbitral awards may be set aside for being incompatible with the public policy of the state chosen as the place of arbitration, this may have the absurd result of having the courts of a nation with no connection to the dispute, assessing whether the award is consonant with its public policy – not that of the state defending its measure, or even the host-state of the disputing investor. Yet this is precisely what occurred in the Metalclad case.

Transparency
T. Transparency is a victim in the secret world of investor-State justice, commercial arbitration whose proceedings, following the norms of commercial arbitration, are held in camera. The pleadings, evidence, and argument may be kept secret if either party objects to their publication. The same is true for the Aaward itself, and, while NAFTA accords the Parties the explicit right to release tribunal ruling, nothing requires them actually to do so.

Fairness
The notion of fairness to the interests of non-parties is entirely absent from the arbitral model. No consideration for the participation of third parties is offered by either NAFTA's own clauses or the arbitration rules which they invoke. While tribunals may yet accord a third- party an opportunity to make submissions on public interest grounds - this is certain to be permitted only on the most restrictive terms.[xxiv]

Objectivity and independence
The sociology of the panellists' selection for international arbitral tribunals makes it highly likely that they will respond to the legal arguments privileging the norms of international commercial law at the expense of domestic values. As the investor and the state each have the right to appoint one arbiter, and since the panel's chair is chosen by

these two appointees, it is likely that there will be just one Canadian adjudicating suits launched against Canadian governments. This suggests that, when a norm of international corporate law comes into conflict with a Canadian legal standard, the latter is likely to be overridden.

Moreover, Chapter 11 cases are good business for the private international commercial judicial community that, as Dezalay and Garth have shown, has a vested interest in promoting the development of a largely autonomouUs but privatized global domain of corporate law.[xxv] This situation raises questions about the self- interest of adjudicators influencing the outcome of disputes. In the Desona case for example, the tribunal found the disputing investors guilty of fraudulent conduct and their claim entirely lacking in merit but it ordered no costs against them. Whatever the reasons for this ruling, it clearly sent a message to would-be disputing investors that they would not be penalized for launching even the most frivolous and unmeritorious of fishing expeditions.

The Lack of Reciprocity Increases Exposure to Investor-State Claims
Rights without Restraints
Unlike state-to-state procedures, NAFTA's Chapter 11 gives foreign investors substantial new rights without imposing on them any corresponding restraints or obligations. For instance, Chapter 11's new corporate rights were not balanced with a requirement to promote the public interest by protecting the environment or public health. rRecourse to investorstateinvestor-state litigation is untempered by many of the considerations -- such as the fact that NAFTA disciplines also bind the complaining state -- that intervene to limit state-to-state claims. -- the fact that NAFTA disciplines also bind the complaining state .
The new system is also skewed because foreign corporations and their investors were given weapons to attack governmental regulations that neither citizens nor domestic corporations enjoy. Moreover, no balancing obligations have been imposed on them by continental-level institutions such as those developed in the European Union, which have the clout to regulate their behaviour, redistribute some of their winnings through taxation, or to monitor and adjust the workings of the emerging continental market. [xxvi] Chapter 11's new corporate rights balanced a requirement to promote the public interest by protecting the environment or public health.

Taken together, the factors described here cast a broad shadow over the landscape of domestic policy and law. Governments must now chart a course through the uncertain terrain of international trade disciplines, which may be invoked with few constraints by foreign corporations. The impact is to constrain the authority of Canadian governments at all levels as definitively but more arbitrarily than do the norms and limitations imposed by Canada's constitution and its common law.

Recommendation

Bearing in mind NAFTA’s extra-constitutional weight, I recommend that the PC Party’s Blue Panel take a stance against Chapter 11's egregious, arbitrary, and anti-democratic nature.

i Sylvia Ostry, *Getting to First: The Post-Cold War Trading System* (Chicago: University of Chicago Press, 1999).

ii All of these examples are taken from investor-State claims initiated pursuant to Chapter 11 procedures see United Parcel Services of America Inc. v. Canada; Metalclad Corp. v. Mexico; and Methanex Inc. v. the United States. These cases are summarized in *Private Rights, Public Problems,* published by the International Institute for Sustainable Development and the World Wildlife Fund, (Winnipeg, 2001).

iii John H. Jackson, *The World Trading System: Law and Policy of International Economic Relations* 2nd ed. (Cambridge, MA.: MIT Press, 1997), 32.

ivWhen a UN committee censured the government of Ontario for not extending to all religiouUs schools the state funding that it gives Catholic public schools, it was challenging a key element of the 1867 confederal bargain that guaranteed Roman Catholics in the provinces the preservation of their educational system.

v The same assessment applies to the World Trade Organization and the international agreements that are organized under its administration. Indeed the WTO's state-to-state enforcement mechanisms, are significantly stronger than their corollary in NAFTA.

vi The North American Free Trade Commission consists of the three countries' trade ministers who retain final authority to supervise NAFTA's institutional mechanisms, resolve disputes over interpreting its text, and take whatever steps might be necessary for its future development.

vii Rafael Fernández de Castro and Claudia Ibargüen, "Las instituciones del TLCAN: una evaluación a los cinco años," in Beatriz Leycegui y Rafael Fernández de Castro, eds., *Socios naturales? Cinco años del Tratado de Libre Comercio de América del Norte* (Mexico: ITAM, 2000), 515-32.

viii 'Pitch for Bill C-55: Canadian Magazine Publishers Argue in Washington That Bill Does Not Violate Free Trade,' *Maclean's* (March 8, 1999), 42.

ix Of course, Canadian firms operating in the United States and Mexico would benefit from this right to attack American or Mexican regulations that they allege have 'expropriated' their property.

x For example, it took Mexico from 1995 to 2001 to have a Chapter 20 process rule that the United States should honour its NAFTA obligation to allow Mexican truckers to ply their trade in the American market – a ruling that is still being stalled by challenges in American courts.

xi Richard C. Levin and Susan Erickson Martin, 'NAFTA Chapter 11: Investment and Investment Disputes,' *NAFTA: Law and Business Review of the Americas* 83:2 (summer 1996), 90.

xii NAFTA, Article 1110.

xiii Schneiderman, supra note 14.

xiv See the following articles by two of Canada's most experienced international trade practitioners. Jon R. Johnson, *Essential Disciplines of the National Treatment Obligation under NAFTA Chapter Eleven*, J.C. Thomas, NAFTA *Chapter 11 to date: The Progress of a Work in Progress*, Discussant's Comments, in "Whose Rights?" ed. [] Dawson, Centre for Trade Policy and Law, 2002.

xvMuthucumaraswamy Sornarajah, [], 70.

xvi Susan Goodeve, "Canada Commits to Trade Liberalization," Section 2194 in Peter Haydan and Jeffrey Burns, eds., *Foreign Investment in Canada* (Scarborough: Carswell, 1996).

xvii See the Trammel Crowe Company v. Canada which can be found at http://www.dfait-maeci.gc.ca/tna-nac/gov-en.asp.

xviii Elizabeth May, 'Fighting the MAI,' in Andrew Jackson and Matthew Sanger, eds., *Dismantling Democracy: The Multilateral Agreement on Investment and Its Impact* (Toronto: CCPA and Lorimer, 1998), 32-47.

xix While the evidence of harm associated with the use of the particular substance MMT is equivocal, most other member nations of the OECD relying upon the precautionary principle, have banned the use of this fuel additive.

xx David Schneiderman, 'NAFTA's Takings Rule: American Constitutionalism Comes to Canada,' *University of Toronto Law Journal* 46 (1996), 535.

xxi See discussion of the terms upon which this case was settled at paragraph 49.

xxii Richard Dearden, 'Arbitration of Expropriation Disputes between an Investor and the State under the North American Free Trade Agreement,' *Journal of World Trade* 29, no. 1 (Feb. 1995), 127.

xxiii 'The term "expropriation" includes, but is not limited to, any abrogation, repudiation, or impairment by a foreign government of its own contract with an investor with respect to a project, where such abrogation, repudiation or impairment is not caused by the investor's own fault or misconduct, but materially and adversely affects the continued operation of the project.' United States Foreign Assistance Act of 1969, section 238, cited in Levin and Marin, 'NAFTA Chapter 11: Investment and Investment Disputes,' 97. See also Schneiderman, "NAFTA's Takings Rule."

xxiv UPS v. Canada, note 3.

xxv Dezalay and Garth, Dealing in Virtue: *International Commercial Arbitration and the Construction of a Transnational Legal Order*, University of Chicago Press, 1996.

xxvi Stephen Blank and Stephen Krajewski, "U.S. Firms in North America: Redefining Structure and Strategy," *North American Outlook* 5:2 (February 1995).