

Myths and Omissions:

Unpacking Obama Administration Defenses of Investor-State Corporate Privileges

**Why Controversy is Growing over Inclusion of the Investor-
State Regime in a U.S.-EU Trade and Investment Pact**



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Myths and Omissions: Unpacking Obama Administration Defenses of Investor-State Corporate Privileges

Why Controversy is Growing over Inclusion of the Investor-State Regime in a U.S.-EU Trade and Investment Pact

Executive Summary

Opposition to the once arcane “investor-state dispute settlement” (ISDS) system has ballooned. ISDS empowers foreign corporations to bypass domestic courts, challenge governments’ public interest policies before extrajudicial tribunals and demand compensation. Widespread resistance to ISDS has pushed the Obama administration to become increasingly defensive about its plan to expand the regime through a proposed Trans-Atlantic Free Trade Agreement (TAFTA), also known as the Transatlantic Trade and Investment Partnership (TTIP), with the European Union (EU). The administration recently published a justification for its push for ISDS.¹ This report addresses the claims made in that document.

The administration’s attempt to quell the controversy surrounding the proposed expansion of ISDS via TAFTA was recently complicated when German government officials made clear that even EU member states do not want the deal to include a parallel legal system for corporations to privately enforce sweeping investor rights.² TAFTA must be approved by the 28 EU member states, including Germany.

One day before the Obama administration published its ISDS defense document, Germany’s Federal Minister for Economic Affairs and Energy Sigmar Gabriel warned the European Commission that Germany may oppose TAFTA if ISDS is included in the pact. On March 26, 2014 Gabriel wrote to EU Trade Commissioner Karel De Gucht, “From the perspective of the [German] federal government, the United States and Germany already have sufficient legal protection in the national courts,” and Germany “has already made clear its position that specific dispute settlement provisions are not necessary in the EU-U.S. trade deal.”³ Gabriel’s remarks echo the official anti-ISDS position of the Socialists and Democrats Group, the second largest bloc in the European Parliament, which also must approve TAFTA. The bloc explicitly opposes the inclusion of ISDS in TAFTA out of concern that it would empower foreign firms to undermine health and environmental policies.⁴

Facing mounting governmental and popular rejection of ISDS, the European Commission has sought to make clear that it is the Obama administration that is demanding its inclusion in TAFTA. One week after Gabriel first indicated Germany’s opposition to ISDS in TAFTA, De Gucht clarified that the EU had actually already formally proposed to U.S. negotiators that ISDS be excluded, but that the U.S. government continued to insist on its inclusion: “If the United States agreed to simply drop it [ISDS]...so be it...But they don’t. I’ve already submitted it [the idea] to them, and they don’t.”⁵ The new President-elect of the European Commission, Jean-Claude Juncker, has already suggested that he opposes ISDS in TAFTA, stating in the TAFTA section of his official policy agenda, “Nor will I accept that the jurisdiction of courts in the EU Member States is limited by special regimes for investor disputes.”⁶ The Obama administration, however, has shown no change in its insistence that ISDS be included in the deal.⁷

The Obama administration has also become increasingly isolated at home in pushing for ISDS, as libertarian and Tea Party groups have expressed ISDS opposition alongside the labor, environmental, consumer, health and other organizations that represent the President's base. In March the libertarian CATO Institute, for example, published an article entitled "A Compromise to Advance the Trade Agenda: Purge Negotiations of Investor-State Dispute Settlement."⁸ U.S. state and local governing bodies have also made clear that they see investor-state provisions as a threat to their autonomy and basic tenets of federalism. The National Conference of State Legislatures (NCSL), a bipartisan association representing U.S. state legislatures, many of which are GOP-controlled, has repeatedly approved a formal position plainly stating that NCSL will oppose any pact that contains ISDS.⁹

Another major complication for the administration's defense of ISDS is the crescendo of increasingly audacious investor-state cases and rulings seen in recent years. As one policy area after another has come under attack in ISDS cases, opposition to the regime has steadily grown. Take, for example, the investor-state cases that U.S. tobacco giant Philip Morris International has launched against Uruguay's tobacco regulations and Australia's cigarette plain packaging law to curb smoking. The measures have been praised by the World Health Organization as leading public health initiatives.¹⁰ They apply equally to domestic and foreign firms and products. Australia's highest court ruled against Philip Morris in the firm's domestic lawsuit against the policies.¹¹ But using ISDS, Philip Morris is demanding compensation from the two governments, claiming that the public health measures expropriate the corporation's investments in violation of investor rights established in Bilateral Investment Treaties (BITs).¹²

In another highly contentious case, Vattenfall, a Swedish energy firm that operates nuclear plants in Germany, has levied an investor-state claim for at least \$1 billion against Germany for its decision to phase out nuclear power following the 2011 Fukushima nuclear disaster.¹³ This comes after Vattenfall successfully used another investor-state case to push Germany to roll back environmental requirements for a coal-fired power plant owned by the corporation.¹⁴ Such extrajudicial attacks on *nondiscriminatory* public interest policies have made clear to the public and legislators that the standard defense of ISDS – that it is a commonsense means for foreign investors to obtain fair treatment if they are discriminated against – does not comport with the reality of the regime, fueling broader ISDS opposition.

Rising Rejection of the Extraordinary ISDS Regime as Backdoor Attacks on Public Interest Policies Have Grown

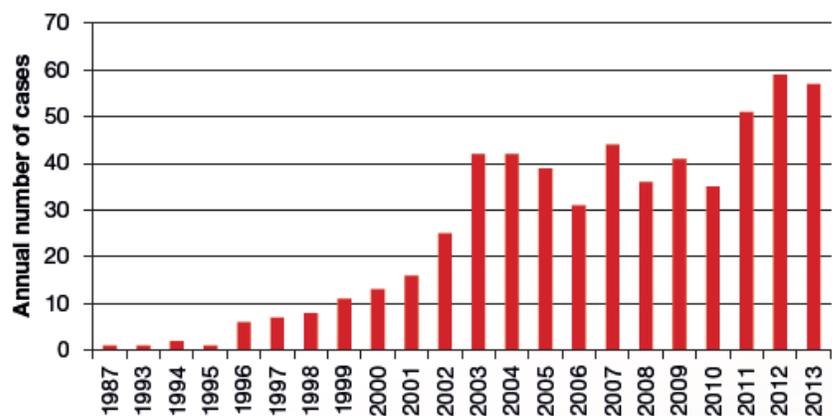
ISDS has been included in various "free trade" agreements (FTAs) and BITs signed by the United States and other countries, though it was excluded from the U.S.-Australia FTA after Australia insisted that the extrajudicial mechanism was neither in its national interest nor necessary between countries with adequate domestic legal systems.¹⁵ ISDS provisions elevate individual foreign corporations and investors to the same status as sovereign governments, empowering them to privately enforce a public treaty by skirting domestic courts and directly "suing" signatory governments for compensation over health, environmental, financial and other domestic safeguards the foreign firms believe undermine their investor rights.

The tribunals deciding these cases are comprised of three private sector attorneys, unaccountable to any electorate. Some attorneys rotate between serving as "judges" and bringing cases for corporations against governments. If a tribunal rules against a challenged policy, there is no limit to the amount of taxpayer money that the tribunal can order the government to pay the foreign corporation. Such compensation

orders are based on what an ISDS tribunal surmises that an investor would have earned in the absence of the public policy it is attacking. The cases cannot be appealed on the merits. There are narrow technical and procedural grounds for annulment. Firms that win an award can collect by seizing a government's assets if payment is not made promptly. Even when governments win cases, they are often ordered to pay for a share of the tribunal's costs. Given that the costs just for defending a challenged policy in an ISDS case total \$8 million on average, the mere filing of a case can create a chilling effect on government policymaking, even if the government expects to win.¹⁶

Claiming broad "rights" that even surpass the strong substantive property rights afforded to domestic firms in nations such as the United States, foreign corporations have used ISDS to attack an increasingly wide array of environmental, energy, consumer health, toxics, water, mining and other non-trade domestic policies. The number of such cases has been soaring. While treaties with ISDS provisions have existed since the 1960s, just 50 known ISDS cases were launched in the regime's first three decades combined (through 2000).¹⁷ In contrast, corporations have launched more than 50 ISDS claims in *each* of the last three years.¹⁸ While some ISDS defenders have argued that the surge in ISDS cases is simply due to an increase in cross-border investment, growth in investor-state cases has significantly outpaced that of foreign direct investment (FDI). The number of new ISDS cases launched each year has been growing at an annual rate of 12 percent since 2000, nearly twice the 7 percent annual growth rate of global inward FDI stocks.¹⁹

Figure 1. Known ISDS cases, annual (1987-2013)



Source: UNCTAD, "Recent Developments in Investor-State Dispute Settlement," 2014

Under U.S. FTAs alone, foreign firms have already pocketed over \$430 million in taxpayer money via investor-state cases. Tribunals have ordered more than \$3.6 billion in compensation to investors under all U.S. BITs and FTAs. More than \$38 billion remains in pending ISDS claims under these pacts.²⁰

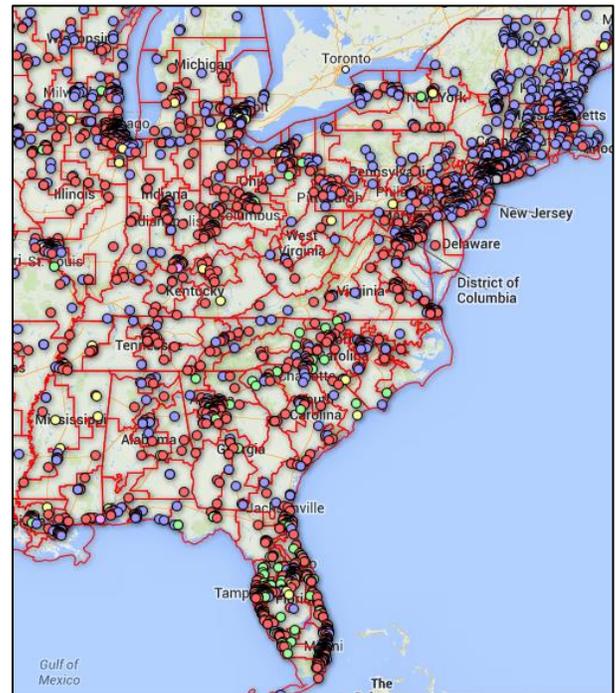
While the costs of ISDS rise for governments that have subscribed to the regime's extraordinary terms, the purported benefit of ISDS – increased FDI – remains elusive. Numerous studies have examined whether countries have seen an increase in FDI as a result of being willing to sign pacts with ISDS enforcement. Summarizing the studies' contradictory results, the United Nations Conference on Trade and Development (UNCTAD) concluded in September 2014, "[T]he current state of the research is unable to fully explain the determinants of FDI, and, in particular, the effects of BITs on FDI."²¹ UNCTAD delivered that synopsis alongside its own study finding that "results do not support the hypothesis that BITs foster bilateral FDI."²² Indeed, the findings of several earlier studies suggesting that BITs tended to boost FDI have been upended by more recent studies as not statistically robust.²³ A 2010 survey of the 200 largest U.S. corporations corroborated these results, finding that leading U.S. firms were relatively unfamiliar with BITs and considered such treaties to be relatively unimportant in their foreign investment decisions.²⁴ While countries bound by ISDS pacts have not seen significant FDI increases, countries without such pacts have not lacked for foreign investment. Brazil, for example, has consistently rebuffed BITs and U.S. FTAs with ISDS provisions,²⁵ yet remains the world's fourth most popular destination for

FDI and the leading destination of FDI in Latin America, where most other countries have signed numerous pacts with ISDS terms.²⁶

As promised benefits of ISDS have proven illusory while tangible costs to taxpayers and safeguards have grown, an increasing number of governments have begun to reject the investor-state regime. South Africa²⁷ and Indonesia²⁸ have started terminating all BITs that contain ISDS provisions. After already terminating ten BITs,²⁹ Ecuador is now conducting an audit of many of its remaining pacts to determine if they are in the national interest.³⁰ India's Ministry of Commerce and Industry has recommended that the government terminate all of India's 83 Bilateral Investment Promotion and Protection Agreements, while the Department of Economic Affairs has called for these ISDS pacts to be reviewed and renegotiated.³¹ Venezuela and Bolivia have withdrawn from the World Bank forum where most investor-state cases are tried.³² Brazil, as mentioned, has never implemented agreements with ISDS enforcement.

Developing countries that have decided to terminate their BITs have not seen FDI inflows decline. Indeed, as they have moved to exit the ISDS system, foreign investment has actually grown. Ecuador's net FDI flows with countries with which it has terminated BITs have shifted from a combined \$52 million net *outflow* in the year of BIT termination to a combined \$110 million net *inflow* in 2013.³³ And as South Africa began terminating its BITs with various EU nations in 2013, the country's FDI inflows doubled to \$10.3 billion. In fact, South Africa received more FDI than any other African country amid its announcements of BIT terminations in 2013, while FDI inflows diminished for other growing African economies such as Nigeria and Ghana (both of which have an array of BITs in force).³⁴

Developed countries have begun to join developing nations in pulling back from the investor-state system. As mentioned, Federal Minister Gabriel has stated that Germany, long a strong supporter of ISDS, is now opposing the inclusion of ISDS in TAFTA. And Australia, after a multi-year review under the past conservative government, concluded that the investor-state regime was not in its national interest. (This occurred even before Philip Morris launched its ISDS case against the nation's landmark cigarette plain packaging law). The report of the Australian government's Productivity Commission stated: "Available evidence does not suggest that ISDS provisions have a significant impact on investment flows... Experience in other countries demonstrates that there are considerable policy and financial risks arising from ISDS provisions... Against this background, the Commission considers that Australia should seek to avoid accepting ISDS provisions in trade agreements that confer additional substantive or procedural rights on foreign investors over and above those already provided by the Australian legal system."³⁵ This led Australia to lodge a "reservation" from ISDS in the ongoing Trans-Pacific Partnership (TPP) negotiations.³⁶



The dots indicate European-owned firms in the United States that would be empowered to challenge U.S. policies before extrajudicial tribunals, were TAFTA to take effect with ISDS. Source: Uniworld, *Foreign Firms Directory*, 2014

TAFTA’s Expansion of ISDS Would Empower More than 71,000 Additional Foreign Firms to Attack Domestic Policies

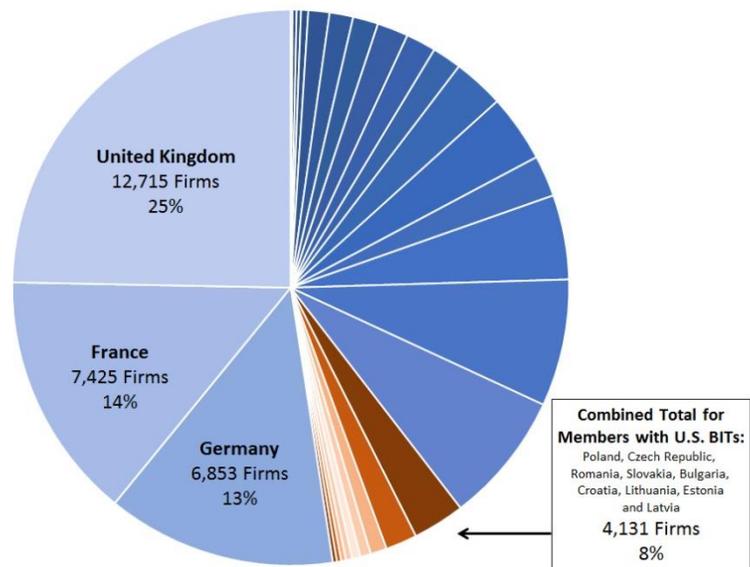
In contrast to other governments’ growing rebuke of ISDS, at the time TAFTA was launched, both the EU and U.S. governments proposed to expand the ISDS regime by including it in TAFTA. Were TAFTA to be enacted with ISDS, it would vastly increase both sides’ exposure to investor-state challenges, given the thousands of corporations doing business in both the United States and EU that would be newly empowered to attack domestic public interest policies.

More than 3,400 parent corporations in EU nations own more than 24,200 subsidiaries in the United States, any one of which could provide the basis for an investor-state claim if TAFTA were to be enacted with ISDS. This U.S. exposure to investor-state attacks far exceeds that associated with all other U.S. FTA partners. Similarly, the EU would be exposed to a potential wave of investor-state cases from any of the more than 19,900 U.S.-based corporations that own more than 51,400 subsidiaries in the EU.³⁷

Some U.S. and EU government officials have downplayed this surge in ISDS liability, arguing that the United States already has BITs with nine EU nations, and that only nine publicly known investor-state cases have been brought under those BITs.³⁸ But these nine BITs, signed exclusively with Eastern European countries that have relatively low FDI exports, cover a mere 26 of the more than 24,200 European-owned firms operating in the United States.³⁹ In other words, U.S. officials are arguing that because U.S. policies have not been challenged under existing BITs by 0.1 percent of the European firms operating here, empowering the other 99.9 percent to challenge domestic safeguards should not be cause for concern.

On the EU side, the nine existing BITs cover just 8 percent of the U.S.-owned firms operating in the EU.⁴⁰ If the number of ISDS cases is taken as proportional to the number of foreign-owned firms, the ISDS case record under the nine existing U.S.-European BITs suggests that newly exposing the other 19 EU countries to U.S. ISDS claims would invite the launch of more than 100 U.S. ISDS cases against those countries in the early years of TAFTA implementation.⁴¹ This figure does not take into account the significant growth of ISDS cases in recent years, which would suggest a higher number of expected ISDS cases under TAFTA.

TAFTA = New Investor Privileges for 92% of U.S. Firms in the EU
Existing U.S. BITs Cover Just 8% of U.S. Investors



Source: Uniworld, American Firms Directory, 2014

In sum, even after removing all firms covered by existing U.S.-European BITs, TAFTA would newly empower corporate claims against domestic policies on behalf of more than 71,600, or 95 percent, of the U.S. and EU's cross-registered firms.⁴²

Governments and Civil Society Are Mounting Increasing Opposition to ISDS in TAFTA

Such an expansion of ISDS liability is particularly senseless given that the EU and the United States have functioning, trustworthy domestic legal systems and some of the strongest property rights laws in the world. The ostensible premise for the anomalous extrajudicial enforcement of ISDS is that some domestic legal systems are too incompetent, biased or ill-equipped to hear foreign investors' claims. Given that neither the United States nor the EU is likely to assert that this description befits the other side's legal systems, what could justify the establishment of a parallel legal system for foreign corporations under the extraordinary terms of ISDS?

As the German government has reportedly joined the ISDS critics posing this question,⁴³ U.S. Trade Representative Michael Froman has resorted to arguing that the reason ISDS is needed in TAFTA is to set an example – for non-TAFTA countries. In a May 2014 speech in Germany, Froman stated, “We both have strong rule of law. We have strong legal traditions against discrimination against foreign investors. But many of the other countries don't, and for this reason, we hope that investment protection will be one of several areas in which TTIP is able to set a new global standard.”⁴⁴

The lack of a justification for TAFTA's inclusion of ISDS, combined with the prospect of a new wave of ISDS cases, also has spurred anti-ISDS outcry from a broad swath of European civil society groups. In April 2014, the European Commission initiated a formal public consultation, explaining that it “felt it was necessary to launch this particular public consultation as a response to the growing public debate and increased concerns over ISDS...”⁴⁵ Despite the highly technical nature of the consultation questions posed by European officials, the response from individuals concerned about ISDS was so overwhelming that the European Commission was forced to extend the deadline for an additional week. In the end, the Commission announced it received nearly 150,000 submissions.⁴⁶ By comparison, when another consultation earlier in 2014 generated fewer than 10,000 submissions, the Commission announced it as “one of the highest response rates ever for a Commission consultation.”⁴⁷

In response to the EU's public consultation on ISDS, dozens of the largest U.S. labor, environmental, consumer and other civil society groups have called for the Obama administration to launch a parallel public consultation with U.S. stakeholders, while halting the push for ISDS in TAFTA.⁴⁸ This follows years of U.S. civil society demands that the Obama and previous Bush administrations exclude the ISDS regime from U.S. agreements. In response to the calls for a U.S. public consultation on ISDS, the Obama administration's Office of the U.S. Trade Representative (USTR) instead issued a factsheet dismissing the concerns being raised.⁴⁹

Indeed, USTR declared that critiques of the ISDS system amounted to mere “myths.”⁵⁰ Yet, in attempt to counter the critiques, USTR's latest ISDS-defending document relies on false and misleading statements. Below we respond to 10 primary defenses of ISDS that USTR includes in its factsheet. USTR's claims attempt to paper over 10 stark realities of the investor-state system that it seeks to expand via TAFTA:

1. ISDS gives foreign corporations greater procedural and substantive rights than domestic firms by providing only foreign firms access to extrajudicial tribunals and by enabling them to obtain compensation for government policies and actions that apply equally to domestic firms and that would not be deemed to violate domestic property rights protections.
2. ISDS undermines the rule of law by empowering extrajudicial panels of private sector attorneys to contradict domestic court rulings, including those in which countries' supreme courts interpret domestic Constitutions and laws, in decisions not subject to any substantive appeal.
3. ISDS cases have led to the watering down of environmental, health and other public interest policies, and chilled the establishment of new ones, as the mere threat of an ISDS case against an existing or proposed policy raises the prospect that a government will need to spend millions in tribunal and legal costs to defend the policy, even if the government might ultimately prevail.
4. Investor-state tribunals often order governments to pay foreign corporations large sums of taxpayer funds as compensation for future profits that the tribunals surmise the firms would have earned if not for the challenged government actions or policies.
5. TAFTA would expose the U.S. government, taxpayers and domestic laws to an unprecedented surge in ISDS liability.
6. The very structure of the ISDS regime gives rise to conflicts of interest that would not be remediated by enhancement of the weak "conflict of interest" rules for tribunalists.
7. Purported safeguards and explanatory annexes added to agreements in recent years have failed to prevent ISDS tribunals from exercising enormous discretion to impose on governments obligations that they never undertook when signing agreements.
8. Transparency rules and amicus briefs are insufficient to hold accountable tribunals that remain unrestrained by precedent, States' opinions or substantive appeals.
9. State and local governments have no standing to defend the state and local policies that are often challenged in ISDS cases.
10. The Obama administration has repeatedly ignored ISDS opposition from Congress, the bipartisan National Conference of State Legislatures, diverse public interest groups and legal scholars.

By ignoring these realities and instead choosing to hawk counterfactual claims aimed at dismissing demonstrated ISDS problems, USTR threatens to expand further the damage the ISDS system has inflicted on public interest policymaking, democratic processes and public budgets in numerous countries. To avoid such an expansion via TAFTA, the legacy of existing ISDS pacts warrants honest examination.

USTR's 10 Reality-Defying Defenses of the Investor-State System

- 1. Reality: ISDS gives foreign corporations greater procedural and substantive rights than domestic firms by providing only foreign firms access to extrajudicial tribunals and by enabling them to obtain compensation for government policies and actions that apply equally to domestic firms and that would not be deemed to violate domestic property rights protections.**

USTR Claim: Investment protections are intended to prevent discrimination, repudiation of contracts, and expropriation of property without due process of law and appropriate compensation. These are the same kinds of protections that are included in U.S. law. But not all governments protect basic rights at the same level as the United States. Investment protections are intended to address that fact. Our agreements provide no new substantive rights for foreign investors.

Regardless of the intent, the ISDS provisions of existing U.S. FTAs and BITs provide foreign investors greater substantive and procedural rights than U.S. firms are afforded under U.S. law and under the jurisprudence of the U.S. Supreme Court.

The substantive privileges investors obtain under the ISDS regime include a highly elastic right to a guaranteed “minimum standard of treatment.” Investor-state tribunals have interpreted this provision to mean that investors must be compensated for nondiscriminatory changes to generally applicable regulatory policy that occur after an investment is established.⁵¹ ISDS terms also grant foreign firms a right to compensation for indirect expropriation for a wide category of property interests not subject to indirect expropriation compensation in U.S. law.⁵²

In U.S. law, there is no right for government compensation if a new policy of general application – such as the new Dodd-Frank financial rules or the new carbon emissions standards from the Environmental Protection Agency (EPA) – frustrate an investor’s “expectations.” There is no right to compensation merely because a government policy changes after the establishment of an investment in a way that may affect a business operating here. Yet, many ISDS tribunals have granted such rights to foreign firms via broad interpretations of the common FTA and BIT provision that obliges States to afford investors “fair and equitable treatment” as part of the guarantee of a “minimum standard of treatment.” Tribunals have interpreted this provision to mean that investors must be guaranteed a stable regulatory framework *that does not frustrate the expectations* they held at the time they established their investment.⁵³

In defending itself against an investor-state challenge that tried to invoke this sweeping interpretation, the U.S. government argued, “[I]f States were prohibited from regulating in any manner that frustrated expectations – or had to compensate for any diminution in profit – they would lose the power to regulate.”⁵⁴ However, under the ISDS regime, “The power to regulate operates within the limits of rights conferred upon the investor,” according to a recent pro-ISDS law review article that sought to summarize tribunals’ interpretations of the “fair and equitable treatment” standard.⁵⁵

While the United States avoided liability in the specific case cited, increasingly tribunals are using just such broad interpretations of the “fair and equitable treatment” and “minimum standard of treatment” provisions to rule against governments. The tribunal in *Occidental Exploration and Production Co. v. Ecuador*, brought under the U.S.-Ecuador BIT, argued, “Although fair and equitable treatment is not defined in the Treaty, the Preamble clearly records the agreement of the parties that such treatment ‘is desirable in order to maintain a stable framework for investment and maximum effective utilization of economic resources.’ *The stability of the legal and business framework is thus an essential element of fair and equitable treatment.*”⁵⁶ The tribunal used this curt interpretation to rule against Ecuador, in part, for enacting policy changes that frustrated the investor’s expectation of a stable policy framework, despite Ecuador’s plea “that no investor can expect that all of its expectations will be met.”⁵⁷ Violations of the “minimum standard of treatment” and “fair and equitable treatment” standards have been the basis for

tribunal rulings against governments in three out of every four investor-state cases under U.S. FTAs and BITs in which the investor has “won.”⁵⁸

Foreign corporations are also empowered under U.S. FTA and BIT terms to obtain compensation on the basis of claims that government policies or actions “indirectly expropriated” their investments. Unlike direct expropriation, claims of indirect expropriation do not require that the government take ownership or control of the investment, and often involve demands of compensation for nondiscriminatory government regulations that affect the value of an investment. Under U.S. law, the right for property holders to obtain compensation for such “regulatory takings” is extremely limited,⁵⁹ and U.S. Supreme Court jurisprudence explicitly holds that the mere diminution of the value of property does not alone create a taking.⁶⁰ U.S. organizations opposing environmental and land use regulations have sought unsuccessfully to pass federal legislation establishing broader rights to compensation for “regulatory takings.”⁶¹ In considering “regulatory takings” claims, U.S. courts must undertake detailed analyses developed in a series of Supreme Court rulings.⁶²

In contrast, ISDS tribunals’ interpretations of what constitutes an indirect expropriation are not bound by any required analyses and need not conform to any prior findings. For instance, the tribunal in another *Occidental v. Ecuador* case simply declared in a single paragraph that its finding of a “minimum standard of treatment” violation also supported a finding of indirect expropriation.⁶³

Moreover, the right to compensation for indirect expropriation, like other substantive rights granted in ISDS pacts, applies to much wider categories of property than those to which similar rights apply in U.S. law. To the limited extent that indirect expropriation compensation is permitted in U.S. law, it has generally been held that the requirement of compensation for “regulatory takings” under the Fifth Amendment of the U.S. Constitution primarily applies to regulations affecting *real* property (i.e. land).⁶⁴ For example, the Supreme Court has indicated that personal non-real-estate property is unlikely to be the basis for a successful “regulatory takings” claim given that “in the case of personal property, by reason of the State’s traditionally high degree of control over commercial dealings, [the owner] ought to be aware of the possibility that new regulation might even render his property economically worthless.”⁶⁵ However, the broad provisions of FTAs and BITs enable foreign investors to claim “indirect expropriation” if government regulations implicate their personal property, intellectual property rights, financial instruments, government permits, money, minority shareholdings or other forms of non-real-estate property.⁶⁶

In sum, contrary to USTR’s claims, the substantive rights underlying the ISDS regime are not limited to non-discrimination, due process and compensation for expropriation of property – the rights available under U.S. law. This is the case even if the expansive substantive rights that ISDS tribunals have afforded to foreign investors were not *intended* by those who drafted U.S. FTAs and BITs.

In the U.S.-Central America Free Trade Agreement (CAFTA), for example, the U.S. government and other CAFTA Parties inserted an annex that attempted to narrow the vague obligation for States to provide foreign investors a “minimum standard of treatment.” By defining the right as derived from Customary International Law that “results from a general and consistent practice of States that they follow from a sense of legal obligation,” the annex attempted to constrain the “minimum standard of treatment” obligation to the terms to which the signatory governments agreed and considered themselves bound, such as the provision of due process and police protection.⁶⁷ But in *Railroad Development Corporation (RDC) v. Guatemala* – one of the first investor-state cases brought under CAFTA – the tribunal largely ignored

the annex. The three lawyers also paid little heed to the official submissions of four sovereign governments (including the U.S. government) that the “minimum standard of treatment” obligation should be interpreted narrowly.⁶⁸ Instead, the tribunal used a more expansive interpretation of “minimum standard of treatment” – one that included protection of investors’ expectations – that had been concocted by another ISDS tribunal. On the basis of that imported interpretation, the tribunal ruled against Guatemala.⁶⁹

And the *RDC* ruling is not an isolated case. In *TECO Guatemala Holdings v. Guatemala*, another CAFTA case, an investor-state tribunal ruled in favor of TECO, a U.S.-based energy corporation, after deciding that Guatemala’s policy for setting electricity rates had violated the “minimum standard of treatment” obligation. As with the *RDC* tribunal, the *TECO* tribunal ignored the CAFTA annex that attempted to assert a narrower “minimum standard of treatment” definition and instead borrowed the broad interpretation of the obligation from the same ISDS case used by the *RDC* tribunal.⁷⁰ On that basis, the tribunal ordered Guatemala to pay TECO \$25 million, plus \$7.5 million to cover the corporation’s legal expenses.⁷¹ ISDS tribunals have thus repeatedly ignored States’ opinions and annexes intended to rein in their discretion, instead using expansive interpretations of ISDS terms that grant foreign investors sweeping new rights not available in the domestic laws of the investors’ host countries, and not agreed to by signatory governments in the ISDS pacts.

Finally, USTR’s factsheet only claims that the agreements provide no new *substantive* rights for foreign investors, avoiding the fact that the ISDS system inarguably provides greater *procedural* rights for foreign firms operating in the United States than are available to domestic firms. If a U.S. firm takes issue with a new U.S. financial or environmental regulation, for example, the corporation cannot skirt the entire U.S. domestic legal system and take its case to a private three-person international tribunal empowered to order the U.S. Treasury to compensate the firm, with extremely limited options for appeal. Nor can a U.S. firm engage in “forum shopping” – launching an ISDS claim to get a second bite at its case after a U.S. domestic court does not provide a satisfactory ruling. But those are precisely the procedural privileges granted to foreign corporations under the ISDS provisions of U.S. pacts.

2. Reality: ISDS undermines the rule of law by empowering extrajudicial panels of private sector attorneys to contradict domestic court rulings, including those in which countries’ supreme courts interpret domestic Constitutions and laws, in decisions not subject to any substantive appeal.

USTR Claim: [The Obama administration works] to ensure that our trade agenda advances our economic interests and reflects our values. One of our core values is promoting the rule of law.

How can ISDS’s empowerment of foreign corporations to circumvent an entire domestic legal system so as to challenge democratically-enacted laws before extrajudicial tribunals be said to “reflect” the value of “rule of law”? And how does it convey respect for the rule of law to authorize tribunals of three private attorneys, unaccountable to any electorate, to contradict domestic court rulings and order governments to pay large sums to the foreign firms in decisions that cannot be appealed on the merits? Time and again, foreign corporations have used ISDS under U.S. pacts to undermine the deliberations and decisions of domestic courts:

- When a Mississippi state court jury ruled against the Loewen Group, a Canadian funeral home conglomerate, in a private contract dispute, Loewen launched an ISDS claim against the U.S. government under the North American Free Trade Agreement (NAFTA).⁷² In the underlying U.S. court ruling challenged by Loewen, a Mississippi jury determined that Loewen had engaged in anti-competitive and predatory business practices that “clearly violated every contract it ever had” with a local Mississippi funeral home.⁷³ After Loewen rejected an offer to settle the case, the company was hit with a jury damages award requiring it to pay the local funeral home \$500 million.⁷⁴ Loewen sought to appeal. Under both U.S. federal and Mississippi state court procedures, a bond must be posted as part of the appeal process to ensure that a losing party does not seek to move its assets to avoid paying on the initial ruling.⁷⁵ This procedural rule, as well as the uncertainties related to jury damage awards, pertains to domestic and foreign firms alike. After a failed bid to lower the bond, Loewen reached a settlement for approximately \$85 million.⁷⁶ But then Loewen launched a NAFTA case for \$725 million, claiming that the requirement to post bond and the jury trial system violated the company’s investor rights under NAFTA.⁷⁷ The tribunal explicitly ruled that court decisions, rules and procedures were government “measures” subject to challenge and review under the ISDS regime.⁷⁸ The ruling made clear that foreign corporations that lose tort cases in the United States can ask ISDS tribunals to second-guess the domestic decisions and to shift the cost of their court damages to U.S. taxpayers. On the merits, the tribunal agreed with some of Loewen’s claims and “criticized the Mississippi proceedings in the strongest terms.”⁷⁹ Luckily for the U.S. government, Loewen’s bankruptcy lawyers filed for reincorporation as a U.S. firm under bankruptcy protection, thus destroying Loewen’s foreign investor status, and the case was dismissed.⁸⁰
- When the government of Guatemala initiated a legal process to consider revoking a disputed railroad contract with RDC, the U.S.-based firm launched a CAFTA claim against the government, even while defending itself in Guatemala’s domestic legal process. The Guatemalan government had issued a legal challenge to the company’s contract after multiple assessments concluded that it did not comply with Guatemalan law.⁸¹ This process, called *lesivo*, provided RDC the opportunity to present its case before an administrative court, and then still appeal the resulting decision to the country’s Supreme Court.⁸² But while taking advantage of this domestic due process, RDC launched its CAFTA claim. The tribunal not only allowed the ISDS claim to move forward despite the unresolved domestic process, but opined that in such instances of parallel ISDS claims, investors should be allowed to access extrajudicial investor-state proceedings *before* the conclusion of domestic legal processes.⁸³ The tribunal soon ruled against Guatemala, ordering the payment of more than \$18 million to RDC for initiating a domestic legal challenge to the company’s contract.
- When Eli Lilly and Company, a U.S. pharmaceutical corporation, failed to prove in Canada’s domestic courts that it had met the legal standard for obtaining patents for two drugs, resulting in the invalidation of its patents, the firm launched a \$481 million NAFTA claim against Canada. Canadian courts invalidated the company’s patents for Strattera and Zyprexa after ruling that Eli Lilly had failed to meet the utility standard required to obtain a patent – demonstration or sound prediction that the drugs would provide the benefits that the company promised when applying for the patents’ monopoly protection rights.⁸⁴ Eli Lilly is asking a NAFTA tribunal to second-guess not only the courts’ decisions, but Canada’s entire legal basis for determining a patent’s validity. The case is pending.⁸⁵
- When the Peruvian government denied a request from the U.S.-based Renco Group for a third extension of its deadline to comply with its contractual commitment to remediate environmental and health problems caused by its toxic metal smelting operation, Renco launched an \$800 million ISDS case against the government under the U.S.-Peru FTA.⁸⁶ After having already granted two extensions

to the company, the government ordered the plant closed, pending compliance. Even though the smelter is now shut down because of bankruptcy, the mere filing of the ISDS case assisted Renco in its efforts to evade cases brought in U.S. courts against the firm on behalf of Peruvian children allegedly injured by the smelter's emissions.⁸⁷ Renco had failed three times⁸⁸ to get the cases out of Missouri courts, where claims by foreign plaintiffs were permitted against companies located in the state.⁸⁹ The cases had a decent chance of success, since Renco's companies have also faced heavy penalties for highly publicized pollution in Missouri,⁹⁰ and the jury pool was likely to be skeptical of the company.⁹¹ In January 2011, one week after starting its investor-state case, Renco moved for a fourth time to have the Missouri state court cases removed to federal courts, this time based on its ISDS case. The same judge that had denied the previous requests now granted it, citing the ISDS case as the reason: "In removing these cases, defendants rely on the Convention on the Recognition and Enforcement of Foreign Arbitral Awards ... [U.S. law] allows removal of any action in state court in which 'the subject matter ... relates to an arbitration agreement or award falling under the Convention...' ... Accordingly, because the [FTA] arbitration panel's decision on the claims raised by Renco ... could conceivably affect the issues in this case, these actions are removable..."⁹²

In several ISDS cases brought under U.S. deals, tribunals have even obliged foreign corporations' requests to defy or reinterpret a country's Constitution. One example comes from an ISDS case that Chevron Corporation has launched against Ecuador under the U.S.-Ecuador BIT in an attempt to evade payment of a \$9.5 billion judgment that Ecuador's domestic courts have ordered the U.S. oil corporation to pay for mass contamination of the Amazonian rain forest. A three-person tribunal in 2012 ordered Ecuador's executive branch to interfere in the operations of the independent court system on behalf of Chevron to suspend enforcement of domestic rulings against the corporation.⁹³ Ecuador's government had explained to the panel that compliance with any order to interfere with the country's independent judiciary would violate the separation of powers enshrined in the country's Constitution.⁹⁴ Undeterred, the tribunal proceeded with their order.

After the government decided to heed its Constitution rather than the three lawyers, the same tribunal delivered another ruling in 2013 that cast aside 20 years of litigation and court rulings against Chevron under two sovereign legal systems. The tribunalists went beyond second-guessing this long history of domestic court proceedings – they pretended it never even happened. In entertaining Chevron's request to order the taxpayers of Ecuador rather than the oil corporation to pay the billions that Ecuador's courts had ordered the company to pay to clean up the vast Amazonian pollution, the tribunal barely made mention of the domestic rulings against Chevron.⁹⁵ Instead, the tribunal invited Chevron to make the same arguments already rejected by domestic courts as if for the first time.

In a preliminary decision, the tribunal accepted an improbable Chevron argument that had failed in Ecuador's domestic courts.⁹⁶ The three lawyers deigned to reinterpret Ecuador's Constitution and domestic law,⁹⁷ and declared that some of Ecuadorians' legal rights even to initiate a case against Chevron had been unwittingly extinguished.⁹⁸ As a final decision remains pending, it remains to be seen whether the ISDS tribunal will attempt to further trump domestic courts, impose its own interpretation of the nation's Constitution and order Ecuadorians themselves to pay for the poisoning of their ecosystem.⁹⁹

3. Reality: ISDS cases have led to the watering down of environmental, health and other public interest policies, and chilled the establishment of new ones, as the mere threat of an ISDS case against an existing or proposed policy raises the prospect that a government will need to spend

millions in tribunal and legal costs to defend the policy, even if the government might ultimately prevail.

USTR Claim: Our investment rules preserve the right to regulate to protect public health and safety, the financial sector, the environment, and any other area where governments seek to regulate. U.S. trade agreements do not require countries to lower their levels of regulation. In fact, in our trade agreements, we require our partners to effectively enforce their environmental and labor laws and to take on new commitments to increase environmental and labor protections.

This USTR claim relies on language tricks to obscure the effect of ISDS rules. Of course the standard ISDS terms of U.S. pacts do not directly “require countries to lower their levels of regulation.” That is not the concern raised by critics. The actual concern starts with the fact that the ISDS regime empowers foreign corporations to demand taxpayer compensation when a country enacts *higher* levels of regulation (i.e. stronger protections for consumers and the environment). For example:

- When Canada imposed a temporary ban on the export of a hazardous waste called polychlorinated biphenyls (PCB), considered by the U.S. EPA to be toxic to humans and the environment, U.S. waste treatment company S.D. Myers launched a case under NAFTA that resulted in an ISDS tribunal ordering Canada to pay the company almost \$6 million.¹⁰⁰
- When a Mexican municipality required Metalclad Corporation, a U.S. waste management corporation, to clean up existing problems before expanding a toxic waste facility, Metalclad launched a NAFTA case that resulted in an ISDS tribunal ordering Mexico to pay the corporation \$16 million.¹⁰¹
- When the Canadian province of Ontario enacted a program to incentivize the production of renewable energy and green jobs – hailed as one of the most advanced clean energy programs in North America – a company owned by Texas oil magnate T. Boone Pickens filed a \$746 million NAFTA case against Canada while U.S.-based Windstream Energy launched its own \$457 million NAFTA claim against the government.¹⁰²
- When the Canadian province of Quebec imposed a moratorium on fracking to conduct a study of environmental and health effects that could result from a possible leaching of chemicals and gases into the groundwater and air, the Lone Pine Resources corporation, which had plans to frack beneath the St. Lawrence Seaway, launched a \$241 million NAFTA claim against Canada.¹⁰³

The usage of ISDS to target increased consumer and environmental safeguards has two damaging effects on public interest policymaking. First, if a corporation launches an ISDS case against a given consumer or environmental protection, the government may feel compelled to roll back the challenged policy to avoid costly legal and tribunal fees, the risk of an even more costly tribunal order to compensate the firm, and the potential for other firms to launch further ISDS cases against the policy. Second, for a proposed public interest policy that has yet to be implemented, the mere threat that ISDS cases would be brought against the policy can chill its implementation. Indeed, regulatory chill and regulatory rollback have been the product of a series of ISDS cases under U.S. pacts. Here are three examples from Canada alone:

- When Canada banned the import and transport of MMT, a toxic gasoline additive that is also banned by U.S. law in reformulated gasoline,¹⁰⁴ the U.S. chemical firm Ethyl Corporation launched a NAFTA claim against Canada.¹⁰⁵ (MMT was not produced in Canada, and given Canadian provinces have significant jurisdiction over environmental matters, this import and interprovincial transport ban was a

means for the national government to effectively implement a national ban.¹⁰⁶) Less than a month after the investor-state tribunal ruled in favor of Ethyl in a jurisdictional ruling, indicating that the case would go forward to the merits, the Canadian government announced that it would settle with Ethyl. The terms of that settlement required the government to pay the firm \$13 million in damages and legal fees, to post advertising saying MMT was safe and, critically, to reverse the ban on MMT.¹⁰⁷ Today Canada depends largely on voluntary restrictions to reduce the presence of MMT in gasoline.¹⁰⁸

- When an all-party committee of the provincial government of New Brunswick, Canada recommended that the province develop its own public auto insurance program, the private insurance industry used the threat of a NAFTA investor-state case to successfully lobby against the program. In response to public outcry over skyrocketing auto insurance premiums, the New Brunswick committee recommended a public plan that would achieve average premium reductions of approximately 20 percent. The Insurance Bureau of Canada, representing Canada's largest insurers, immediately warned that the proposal could trigger NAFTA investor-state cases from foreign insurance providers in Canada as a NAFTA-prohibited "expropriation" of their market share.¹⁰⁹ The proposal was soon scuttled, due in part, according to observers, to "aggressive threats of treaty litigation."¹¹⁰
- When Canada's Parliament started to consider the enactment of plain packaging policies for cigarettes to curb smoking in 1994, the tobacco industry responded with the specter of a NAFTA investor-state case in attempt to forestall the regulation. R.J. Reynolds Tobacco Company sent a letter to the health committee of Canada's House of Commons, arguing that a plain packaging policy would constitute a NAFTA-prohibited expropriation and "would give rise to a claim under the provisions of the NAFTA for hundreds of millions of dollars in compensation."¹¹¹ The Parliament never acted on the plain packaging plan, and analysts credited the NAFTA threat for helping to bury the proposed public health measure.¹¹² Evidence suggests that the threat of ISDS cases is still chilling plain packaging proposals today in several countries. For example, in February 2013, New Zealand's Ministry of Health announced that the government planned to introduce plain packaging legislation, but indicated that it will wait until Philip Morris's investor-state case against Australia's plain packaging law is resolved, and that enactment of New Zealand's legislation could be delayed as a result.¹¹³ The legislation has since been introduced, but not enacted.¹¹⁴

The increasing pattern of investor-state retaliation for health, environmental and other public interest regulations may well lead policymakers to think twice about enacting protections that could expose the government to a costly investor-state dispute. Even when governments win cases, they are often ordered to pay for a share of the tribunal's costs plus their own legal fees – these expenses average \$8 million per case.¹¹⁵ As observed, the prospect of having to spend millions to defend a given safeguard, and potentially being ordered by a tribunal to pay millions more, can have a chilling effect on the enactment of public interest regulations. The extraordinary investor-state provisions of U.S. FTAs and BITs thus undermine public interest regulation not by directly requiring regulations to be dismantled, but by imposing new liabilities and risks on the enactment of new regulations in the public interest.

Concerned about the mounting ISDS claims against such public interest policies, countries negotiating agreements with the United States have not been convinced by USTR's claim that "[o]ur investment rules preserve the right to regulate." In both the TPP and TAFTA, negotiating partners have proposed environmental or health exceptions that would apply to investor-state cases.¹¹⁶ But the U.S. government has actually opposed the inclusion of exceptions that governments could use to defend health and environmental policies challenged in investor-state cases as indirect expropriation or "minimum standard

of treatment” violations. In the case of TPP, where most of the investment chapter’s text is agreed, this is a matter of serious contention, as many other TPP nations demand such exceptions be included.¹¹⁷

The investment chapters of past U.S. trade pacts, which inform the U.S. proposals for TAFTA, also provide no meaningful exception or defense provisions for public interest regulations challenged by foreign firms as violations of commonly-invoked foreign investor rights.¹¹⁸ Though the standard language of U.S. pacts includes an “investment and environment” section, the clause provides no meaningful safeguard against investor-state challenges to environmental policies.¹¹⁹ The relevant language in the investment chapter of existing U.S. FTAs, the leaked investment chapter of the TPP and the 2012 U.S. model BIT (a stated U.S. template for investment provisions in TAFTA)¹²⁰ is written in a manner that would likely be deemed self-canceling. It states that a signatory government may enact environmental protections, so long as doing so does not conflict with the sweeping rights that the pact gives to foreign investors. But the only instances for which a government needs an agreement to specify that its environmental regulatory rights trump its obligations to foreign investors are those in which investors’ broad rights conflict with environmental policies. For such instances, this supposed “right to regulate” provision appears to be inapplicable.¹²¹ Indeed, a tribunalist in the *S.D. Myers v. Canada* NAFTA ISDS case noted that this environmental provision, also included in NAFTA, was among those referred to by trade analysts as “‘tautologies’ or as ‘diplomatic, rather than legal’ statements.”¹²² A recent legal review from Cambridge University Press concluded that this environmental clause “falls short in failing to add more than a nebulous provision that can easily be marginalized.”¹²³

USTR also makes reference to the labor and environmental chapters typically included in U.S. FTAs. In 2007, Congress forced President George W. Bush to make some provisions of both the environment and labor chapters enforceable and subject to the same state-to-state dispute resolution system as other chapters in his pacts. But these provisions are subject to the “Gramm Clause.” Senator Phil Gramm (R-Texas) inserted in the 2002 Fast Track legislation an amendment that ensured the FTA enforcement language would be undercut.¹²⁴ The resulting Fast Track law “recognize[d] that parties to a trade agreement retain the right...to make decisions regarding the allocation of resources to enforcement with respect to other labor or environmental matters determined to have higher priorities.” Fast Track further stated, “no retaliation may be authorized based on the exercise of these rights or the right to establish domestic labor standards and levels of environmental protection.”¹²⁵ Thus, U.S. FTAs negotiated under that Fast Track included such language as: “The Parties recognize that each Party retains the right to exercise prosecutorial discretion and to make decisions regarding the allocation of environmental enforcement resources with respect to other environmental laws determined to have higher priorities.”¹²⁶

Even though the 2002 Fast Track authority expired and does not apply to the TPP, the leaked draft TPP environmental text appears to still abide by the limiting “Gramm Clause,” stating: “The Parties recognize that each Party *retains the right to exercise discretion* and to make decisions regarding: (a) investigatory, prosecutorial, regulatory, and compliance matters; and (b) the allocation of environmental enforcement resources with respect to other environmental laws determined to have higher priorities. Accordingly, the Parties understand that with respect to the enforcement of environmental laws a Party is in compliance...where a course of action *or inaction* reflects a reasonable exercise of such discretion...”¹²⁷

But even if the provisions of the labor and environment chapters of TAFTA, unlike other U.S. FTAs, were strong and fully enforceable, it would not diminish signatory governments’ broad and binding obligations to foreign investors under an investment chapter with ISDS. Nor would it prevent foreign firms from citing those expansive obligations, such as the guarantee of a “minimum standard of

treatment,” in launching investor-state cases against environmental, labor and other public interest policies. Indeed, it is precisely when governments have effectively enforced their environmental laws, as USTR claims is required by U.S. FTAs, that foreign firms have launched an array of costly ISDS cases.

4. Reality: Investor-state tribunals often order governments to pay foreign corporations large sums of taxpayer funds as compensation for future profits that the tribunals surmise the firms would have earned if not for the challenged government actions or policies.

USTR Claim: [U.S. investor-state provisions] provide no legal basis to challenge laws just because they hurt a company's profits...Our investment rules seek to promote standards of fairness, not protect profits.

While the basis of a foreign corporation's investor-state claim under U.S. pacts cannot be simply that the firm lost profits, if a corporation convinces an ISDS tribunal on the merits of its case – that a given domestic law violated one of the panoply of foreign investor rights not available to domestic firms – the firm can then calculate its demand for compensation on the “expected future profits” that the law allegedly impeded. After using sweeping interpretations of foreign firms' rights to find governments at fault, investor-state tribunals under U.S. pacts have frequently used this “expected future profits” approach to determine how much governments must pay to foreign firms. Under such logic, tribunals have ordered governments to pay more than \$3.6 billion to foreign corporations under U.S. FTAs and BITs for nondiscriminatory toxics bans, land-use rules, regulatory permits, water and timber policies and more. Meanwhile, in the 19 pending claims under U.S. FTAs alone, foreign firms are demanding \$38 billion for environmental, energy, financial regulation, public health, land-use and transportation policies.¹²⁸

Due to ISDS tribunals' increasingly wide interpretations of foreign firms' rights and increasingly investor-friendly damages calculations, the amounts that tribunals have ordered governments to pay foreign corporations have soared. While just 15 years ago tribunals typically ordered payment of millions of dollars in a given ISDS case, today it is not uncommon for a single lost case to cost a government hundreds of millions of dollars.¹²⁹

This trend was dramatically confirmed in October 2012 when the ISDS tribunal in the previously mentioned *Occidental v. Ecuador* case, brought under the U.S.-Ecuador BIT, ordered Ecuador's government to pay \$2.3 billion to the U.S. oil corporation – one of the largest-ever investor-state awards.¹³⁰ The penalty imposed by the tribunal on Ecuador's taxpayers was equivalent to the amount Ecuador spends on healthcare each year for over seven million Ecuadorians – almost half the population.¹³¹ The tribunal decided on the massive penalty after acknowledging that Occidental had broken the law,¹³² that the response of the Ecuadorian government (forfeiture of the firm's investment) was lawful, and that Occidental indeed should have expected that response.¹³³ But the tribunal then concocted a new obligation for the government (one not specified by the BIT itself) to respond proportionally to Occidental's legal breach and, upon deeming themselves the arbiters of proportionality, determined that Ecuador had violated the novel investor-state obligation.¹³⁴

To calculate damages, the tribunal majority estimated the amount of future profits that Occidental would have received from full exploitation of the oil reserves it had forfeited due to its legal breach, including profits from not-yet-discovered reserves.¹³⁵ The tribunal majority then substantially increased the penalty

imposed on Ecuador by ordering the government to pay compound interest. It has become increasingly common for investor-state tribunals to order governments to pay compound rather than simple interest, often requiring that the interest be retroactively compounded from the moment of the challenged action or policy to the date of the tribunal's decision, and prospectively until the date of payment.¹³⁶ In the *Occidental v. Ecuador* case, these interest requirements alone cost the Ecuadorian government more than \$500 million.

5. Reality: TAFTA would expose the U.S. government, taxpayers and domestic laws to an unprecedented surge in ISDS liability.

USTR Claim: ...the United States has only been sued 17 times under any U.S. investment agreement and has never once lost a case.

Citing the number of cases brought against the United States under existing FTAs and BITs says little about the investor-state liability to which the United States would be exposed under TAFTA. Of the 20 existing U.S. FTA partners, only one – Canada – is among the world's top 20 exporters of FDI.¹³⁷ Having signed deals primarily with developing countries that have few investments in the United States, the investor-state liability of existing pacts has been limited.

But were TAFTA to be enacted with ISDS, the United States would grant investor-state privileges to corporations from 12 of the world's 20 largest FDI exporters, dramatically increasing U.S. exposure to ISDS attacks.¹³⁸ EU corporations own more than 24,000 U.S.-based subsidiaries, any of which could serve as the basis for an investor-state claim against U.S. government policies or actions were TAFTA to go into effect with ISDS included.¹³⁹

Some U.S. government officials have downplayed this surge in ISDS liability, arguing that the United States already has BITs with nine EU nations, none of which have produced an investor-state case against the United States.¹⁴⁰ What they do not mention is that the nine existing U.S. BITs with EU countries are exclusively with Eastern European nations that have relatively low FDI exports: Bulgaria, Croatia, the Czech Republic, Estonia, Latvia, Lithuania, Poland, Romania and Slovakia. Indeed, there are only 26 firms operating in the United States with parent companies from these nine countries combined.¹⁴¹ In other words, U.S. officials are arguing that because U.S. policies have not been challenged under existing BITs by 0.1 percent of the more than 24,000 European firms operating here, empowering the other 99.9 percent to challenge domestic safeguards should not be cause for concern.

Number of U.S. Corporations in EU Countries & Vice Versa

Austria	900	Italy	3,939
Belgium	1,527	Latvia	122
Bulgaria	248	Lithuania	143
Croatia	190	Luxembourg	214
Cyprus	119	Malta	56
Czech Rep.	938	Netherlands	2,532
Denmark	876	Poland	1,556
Estonia	127	Portugal	930
Finland	755	Romania	491
France	7,425	Slovakia	316
Germany	6,853	Slovenia	131
Greece	707	Spain	3,801
Hungary	632	Sweden	2,019
Ireland	1,233	UK	12,715

United States 24,284

This table indicates, for example, that 900 U.S. corporate affiliates are established in Austria, while 24,284 corporate affiliates from EU countries are established in the United States.

Source: Uniworld, Foreign Firms Directory, 2014

Even assuming that the United States could somehow win all of the new cases spurred by this vast increase in investor-state liability, U.S. taxpayers would still have to pay substantially just to defend the targeted domestic policies. As mentioned, in an average investor-state case, governments spend \$8 million just on legal fees and tribunal costs – expenses that often must be paid even if the government wins the case.¹⁴² The government of the Philippines has spent at least \$58 million on tribunal and legal expenses alone in two ISDS cases brought by German firm Fraport AG Frankfurt Airport Services Worldwide.¹⁴³ As explained above, the prospect of paying millions for repeated investor-state claims against a proposed public interest policy can chill a government’s resolve to enact the policy even if it expects to win an ensuing string of ISDS cases.

But the assumption that the U.S. government will continue to dodge the ISDS bullet indefinitely is not one on which TAFTA negotiators should rely. The United States has already nearly lost ISDS cases that were dismissed on narrow procedural grounds.¹⁴⁴ The fact that these were launched by firms in Canada – the only major FDI exporter among U.S. FTA partners – should raise further concern about enacting an FTA with the EU’s array of major FDI exporters. For example, in the *Loewen v. United States* case described above, the ISDS tribunal supported several of Loewen’s arguments on the merits,¹⁴⁵ and only dismissed the case without imposing a penalty on the U.S. government thanks to a remarkable fluke: lawyers involved with the firm’s bankruptcy proceedings reincorporated Loewen as a U.S. firm, thus destroying its ability to obtain compensation as a “foreign” investor.¹⁴⁶ Such luck should not be expected to continue if foreign investor privileges are granted to thousands of European firms.

6. Reality: The very structure of the ISDS regime gives rise to conflicts of interest that would not be remediated by enhancement of the weak “conflict of interest” rules for tribunalists.

USTR Claim: Investor-state arbitration is designed to provide a fair, neutral platform to resolve disputes. The arbitration rules applied by tribunals under our agreements require that each arbitrator be independent and impartial. These rules permit either party in a dispute to request the disqualification of an arbitrator and the appointment of a new arbitrator if necessary to ensure the independence and impartiality of all tribunal members.

The actual conflict of interest rules that apply under U.S. pacts containing ISDS are notably weak. But there are more fundamental problems. The entire structure of ISDS has created a biased incentive system in which tribunalists can boost their caseload by using broad interpretations of foreign investors’ rights to rule in favor of corporations and against governments, and boost their earnings by dragging cases out for years. ISDS is neither fair nor neutral, not because of a few compromised tribunalists, but due to core design flaws.

Under ISDS rules, only foreign investors can launch cases and also select one of the three tribunalists. (By contrast, in domestic courts, judges are assigned to a case, not hired by the plaintiff.) Thus, ISDS lawyers that create novel, expansive interpretations of foreign investors’ rights while serving as a tribunalist in one case can increase the number of investors interested in launching new cases and enhance the likelihood of their selection by investors for future tribunals. (While governments can also select one of the tribunalists, these individuals do not have the same structural conflict of interest – interpreting investors’ rights narrowly may curry favor with governments, but it would diminish the number of firms interested in launching ISDS claims in the first place.) This helps explain why a few lawyers are repeatedly picked as

ISDS tribunalists – just 15 lawyers have been involved in 55 percent of all public ISDS cases.¹⁴⁷ The absence of any system of precedent for ISDS rulings, or of governments’ rights to appeal the merits of cases, further enables tribunalists to concoct ever more fanciful interpretations of ISDS-enforced agreements and order compensation for breaches of obligations to which signatory governments never agreed.

And because tribunalists are paid by the hour, unlike salaried domestic judges, the longer a case continues, the more money the tribunalist makes (and the government pays), even if the case is ultimately dismissed. Tribunalists are paid at rates ranging from \$375 to more than \$700 per hour.¹⁴⁸ Even when governments add language in ISDS-enforced agreements intended to allow for quick termination of frivolous cases, the decision to accept an argument for termination based on such terms rests with three tribunalists whose incomes rely on the case continuing.

Moreover, the ISDS system allows lawyers to rotate between roles, as supposedly impartial arbitrators and as advocates for investors, in a manner that would be unethical for judges. Many lawyers who serve on ISDS tribunals as “judges” also represent corporations in other ISDS cases against governments, or have had a business relationship with the particular corporation in their case. Thus, a lawyer can use her role as a tribunalist to push expansive interpretations of governments’ obligations that she can then take advantage of when launching an ISDS case for an investor in the future.

Specific conflicts of interest have raised alarm, such as in the *Vivendi Universal v. Argentina* case, in which the tribunal’s award in favor of Vivendi was not annulled despite one of the tribunalists serving on the board of directors of a bank that held shares in Vivendi. The tribunalist did not disclose the conflict, much less recuse herself.¹⁴⁹

Neither U.S. FTAs nor the 2012 U.S. model BIT directly stipulate requirements for investor-state tribunalists to be independent or impartial. Rather, the pacts rely on weak impartiality provisions included in the World Bank and United Nations rules under which most tribunals operate. The rules of the World Bank’s International Centre for Settlement of Investment Disputes (ICSID) – the most commonly used rules for investor-state cases – state that tribunalists need to be “relied upon to exercise independent judgment.”¹⁵⁰ However, the rules make it very difficult for a government to disqualify a tribunalist even when she or he exhibits a clear conflict of interest (e.g. serving on the Board of a firm invested in the corporation bringing the case). ICSID requires the government to convince both of the other tribunalists, or the president of the World Bank, to remove the biased tribunalist.¹⁵¹ Convincing investor-state tribunalists to remove one of their colleagues is a tall order, particularly given that, as stated, the lawyers who serve on investor-state tribunals form part of a small, tight-knit club.

That may explain why in ICSID’s 48-year history, attempts to disqualify biased tribunalists have only been successful on four occasions. In 37 other ISDS cases brought under ICSID rules, tribunalists have dodged attempts at disqualification on grounds that they exhibited bias or had conflicts of interest.¹⁵² This track record hardly inspires confidence in the impartiality of tribunalists.

The conflict of interest rules of the United Nations Commission on International Trade Law (UNCITRAL) – the second most commonly used set of rules for ISDS cases – are similarly weak. While UNCITRAL rules require arbitrators to “disclose any circumstances likely to give rise to justifiable doubts as to his or her impartiality or independence,” there are no stipulated consequences for failure to do so.¹⁵³ And while a party to the dispute can challenge an arbitrator as exhibiting a conflict of interest,

the contested tribunalist would not be removed unless the other party agrees, the arbiter removes herself, or the “appointing authority” empowered to unilaterally decide on the challenge opts for removal.¹⁵⁴ The first scenario seems unlikely – a party should not be expected to dismiss an arbiter whose conflict of interest bends in their favor. The second scenario has rarely played out – challenged arbitrators in investor-state cases have generally not proven willing to leave the arbitration on their own volition. And the third scenario – delegating the decision over challenged arbitrators to the “appointing authority” (e.g. the Secretary-General of the Permanent Court of Arbitration at The Hague) – grants wide discretion to the authority to make a unilateral decision. The rules neither stipulate criteria that shall guide the authority’s decision nor require the authority to disclose the criteria actually used.¹⁵⁵

But even if such weak rules concerning the specific conflicts of interest of individual tribunalists were strengthened, the structural conflicts of interest of the ISDS system would remain. An ISDS tribunalist who has no relationship with the particular firm bringing a case still has an incentive to use expansive interpretations of government obligations to rule in favor of the firm so as to boost the utility of ISDS and the probability of being picked for future cases.

7. Reality: Purported safeguards and explanatory annexes added to agreements in recent years have failed to prevent ISDS tribunals from exercising enormous discretion to impose on governments obligations that they never undertook when signing agreements.

USTR Claim: [U.S. pacts with ISDS provisions] include strong safeguards to deter frivolous challenges to legitimate public interest measures. The United States has proposed additional safeguards that include stricter definitions than are in most investment agreements of what is required for successful claims, as well as mechanisms for expedited review and dismissal of frivolous claims...

In fact, the “safeguards” USTR touts have already been tested, and have failed to prevent investor-state cases brought under U.S. FTAs and BITs from growing not just in number, but in the range of legitimate public interest policies being targeted. The “additional safeguards,” included in U.S. pacts since CAFTA, have not stopped investors from mounting increasingly daring challenges or prevented tribunals from handing down increasingly expansive rulings against public interest policies.

With respect to the investors’ challenges, the new “safeguards” touted by USTR were included in the Peru FTA. But that did not stop the Renco corporation from using that pact to launch its \$800 million ISDS claim against Peru for not giving the firm a *third* extension on its unfulfilled commitment to remediate against toxic pollution created by its metal smelter.¹⁵⁶ And despite the inclusion of the “safeguards” in CAFTA, a subsidiary of the Canada-based Pacific Rim Mining Corporation, named Pac Rim Cayman, used that pact to challenge El Salvador’s refusal to grant a mining permit to the company amid a major national debate about the health and environmental implications of mining and the announcements, by presidents from both the right and left parties, of a moratorium on gold mining. Pac Rim launched the ISDS case because it wanted a permit to build a controversial cyanide-leach gold mine, despite the company’s failure to complete a required feasibility study.¹⁵⁷ While the tribunal ultimately ruled that the Canada-based Pac Rim did not have standing as a U.S. firm to pursue the case under CAFTA (while giving the corporation a green light to pursue the ISDS case under a domestic investment law), this decision was not the result of the touted safeguards. Had Pac Rim simply better organized its corporate structure, the case likely could have proceeded under the U.S. pact.¹⁵⁸ And despite the tribunal’s ruling, El

Salvador still had to pay millions to defend its decision not to grant a contentious mining permit. Further, in the wake of Pac Rim's ISDS claim, implementation of proposed new mining restrictions have been delayed indefinitely.¹⁵⁹

The attempt to “include stricter definitions...of what is required for successful claims” has also failed to stop tribunals from using increasingly expansive interpretations of foreign investors' rights to side with corporations in ISDS challenges to public interest policies. In CAFTA, the Parties inserted an annex,¹⁶⁰ as described above, that attempted to narrow the vague obligation for States to guarantee foreign investors a “minimum standard of treatment,” which a litany of tribunals had interpreted as an obligation for the government to not frustrate investors' expectations, for instance by improving environmental or health laws after an investment was established. As mentioned, in both *RDC v. Guatemala* and *TECO v. Guatemala* – two of the first investor-state cases brought under CAFTA – the tribunals simply ignored the annex's narrower definition of “minimum standard of treatment.” Instead, the *RDC* and *TECO* tribunals both relied on an expansive interpretation of that standard, concocted by a previous investor-state tribunal, which included an obligation to honor investors' expectations.¹⁶¹ Both ISDS tribunals ruled that Guatemala had violated the expanded obligation, and ordered the government to pay millions.

Another provision that USTR touts as a “safeguard” is a mechanism to dispense with frivolous investor-state claims. The relevant language in the 2012 U.S. model BIT provides for expedited consideration of arguments from the government that a case should be terminated because the legal claim used by the foreign corporation to attack its policies is not permitted under the treaty's sweeping investor protections.¹⁶² One problem is that tribunalists with financial incentives to continue cases are the ones who decide whether to accept such arguments for termination. Another problem is that many investor-state claims *do* in fact fall within the wide ambit of the investor privileges found in U.S. FTAs and BITs. That is because the pacts grant broad rights to investors and give ample discretion to tribunals to interpret those rights as far-reaching restrictions on States' prerogative to regulate in the public interest. Until foreign investors' substantive rights and tribunalists' discretion are narrowed, language to prevent claims not falling under those rights will have limited impact in preventing investor-state rulings against “legitimate public interest measures.”

Indeed, initial attempts to use this mechanism against frivolous claims suggest that it may be largely ineffective, thereby adding another step in the prolonged ISDS timetable (and more billable tribunalist hours) rather than expediting the process. In the *Pac Rim v. El Salvador* case, El Salvador attempted to use the “safeguard” against frivolous cases, arguing that the company's claim was not one that could be legally argued under CAFTA.¹⁶³ But in evaluating the government's argument, the tribunal decided that for a State to successfully use the mechanism to dismiss a frivolous claim, the tribunal must determine at the outset of a case that the claim was “certain” to fail, not merely “likely” to fail.¹⁶⁴ Having decided that Pac Rim's claim did not meet this improbably high threshold, the tribunal dismissed the government's attempted usage of the “safeguard.”¹⁶⁵ As mentioned, Pac Rim's CAFTA claim did eventually fail, as the tribunal later denied Pac Rim jurisdiction under the pact. In the two intervening years, the government spent millions defending the mining decisions at issue – the very eventuality that the frivolous claims “safeguard” was supposed to prevent.

8. Reality: Transparency rules and amicus briefs are insufficient to hold accountable tribunals that remain unrestrained by precedent, States' opinions or substantive appeals.

USTR Claim: The United States is committed to ensuring the highest levels of transparency in all investor-state proceedings. Investment arbitration hearings under recent U.S. trade and investment agreements, as well as all key documents submitted to investor-state tribunals and tribunal decisions, are public. Recent U.S. trade and investment agreements also give NGOs and other non-parties to a dispute the ability to participate by filing amicus curiae or “friend of the court” submissions, similar to non-parties’ ability to make filings in U.S. courts.

Transparency is a necessary, but not sufficient, condition for reining in investor-state tribunals’ ability to fabricate new obligations for States and then rule against public interest policies as violations of the novel obligations. As investor-state documents have become more publicly available, tribunals have not indicated greater hesitance to use overreaching interpretations of investors’ rights. Documents were generally made available in the recent *Occidental v. Ecuador* case brought under the U.S.-Ecuador BIT. That includes the publicly-available 2012 award in which the tribunalists concocted a new obligation for Ecuador to respond proportionally to Occidental’s breach of the law, deemed themselves the arbiters of proportionality, and ordered the government to pay \$2.3 billion for violating the creative obligation.¹⁶⁶

And while it is important for public interest groups to be able to submit amicus briefs in investor-state cases, they will be inadequate to halt the threat that those cases pose to public interest policies, given the structural incentive and ability, described above, for ISDS tribunalists to simply ignore submissions that call for greater policy space. If these structural problems permit tribunalists to ignore the submissions of the sovereign governments whose agreements they are ostensibly interpreting, there is little reason to think they would do otherwise when facing private sector amicus submissions. As mentioned, in the *RDC v. Guatemala* CAFTA case, the governments of the United States, El Salvador and Honduras all joined Guatemala in arguing via non-disputing Party submissions that the “minimum standard of treatment” obligation should be narrowly defined according to State practice. But the tribunal paid little heed to the suggestions, skipped any examination of State practice, and instead imported an interpretation of “minimum standard of treatment” from yet another ISDS tribunal.¹⁶⁷ Why would tribunals exhibiting such gall feel bound to the suggestions of NGOs?

None of the provisions that USTR touts restrict the latitude of investor-state tribunals to levy binding decisions against domestic policies based entirely on the reasoning of three private lawyers. Tribunalists are not bound to base their decisions on precedent. They are not bound to adopt standard interpretations of international law. And they are not bound to a robust appeal system. Governments facing unfavorable investor-state rulings may only file for an “annulment” for certain specific categories of tribunal “error.” Annulment claims are not heard by domestic courts, but are decided by another tribunal comprised of private sector attorneys. U.S. FTAs have never included a substantive appeal mechanism for investor-state cases despite longstanding calls for one. The future development of such a mechanism was even included in CAFTA:

Within three months of the date of entry into force of this Agreement, the Commission shall establish a Negotiating Group to develop an appellate body or similar mechanism to review awards rendered by tribunals under this Chapter... The Commission shall direct the Negotiating Group to provide to the Commission, within one year of establishment of the Negotiating Group, a draft amendment to the Agreement that establishes an appellate body or similar mechanism.¹⁶⁸

Eight years have passed since CAFTA took effect in most signatory countries, and no such amendment has been produced.

9. Reality: State and local governments have no standing to defend the state and local policies that are often challenged in ISDS cases.

USTR Claim: [Investor-state provisions in U.S. FTAs and BITs] do not expose state or local governments to new liabilities. In any disputes arising under our trade agreements, the federal government assumes the cost of defending the United States, even if they relate to state and local issues.

An increasing range of measures taken by state, provincial and municipal governments have been challenged under the ISDS terms of U.S. pacts, including state and local land use decisions, state environmental and public health policies, adverse state court rulings, and state and municipal contracts.¹⁶⁹ If a foreign corporation challenges a state or local policy, the state or local government does not have standing to defend the policy and must rely on the federal government.

When the federal government does choose to call on a state's lawyers, given their particular expertise, to assist with the defense of a challenged state-level policy, there is no guarantee that the expenditure of state resources will be recovered, even if the corporation loses the case. Indeed, in several ISDS cases, tribunals have ordered losing corporations to pay federal government lawyers' legal fees, but the legal expenses incurred by states have not been reimbursed. For instance, in the *Methanex Corporation v. United States* NAFTA case in which a Canadian corporation challenged a California ban of the gasoline additive MTBE, the tribunal ordered that \$3 million be paid to the U.S. federal government to help cover its legal expenses. However, the tribunal did not award legal fees for the California state lawyers who worked long hours helping the federal government defend the California law.¹⁷⁰

While the federal government is technically responsible for paying any compensation ordered by an investor-state tribunal, in a successful ISDS case against a state or local measure, the federal government could hold funds for state or local projects hostage until the challenged measure was rescinded or until the locality agreed to help pay the foreign firm. While the legality of this maneuver has not been addressed by U.S. courts, attempts to foist the investor-state compensation burden onto sub-federal governments have already been tried in U.S. FTA partner countries.¹⁷¹ The federal government could also try to avoid having to pay damages in response to a tribunal's ruling against a state or local law by preempting the challenged policy with a federal law.

State and local governing bodies have expressed strong opposition to U.S. investor-state pacts due to these threats to their autonomy and the basic tenets of federalism. The National Conference of State Legislatures (NCSL), a bipartisan association representing U.S. state legislatures, many of which are GOP-controlled, has repeatedly approved a formal position of opposition to such pacts. The association's most recent position states:

NCSL will not support Bilateral Investment Treaties (BITs) or Free Trade Agreements (FTAs) with investment chapters that provide greater substantive or procedural rights to foreign companies than U.S. companies enjoy under the U.S. Constitution. Specifically, NCSL will not support any BIT or FTA that provides for investor/state dispute resolution. NCSL firmly believes that when a state adopts a non-discriminatory law or regulation intended to serve a public

*purpose, it shall not constitute a violation of an investment agreement or treaty, even if the change in the legal environment thwarts the foreign investors' previous expectations.*¹⁷²

10. Reality: The Obama administration has repeatedly ignored ISDS opposition from Congress, the bipartisan National Conference of State Legislatures, diverse public interest groups and legal scholars.

USTR Claim: As the Obama Administration promotes trade and investment agreements, we work closely with Congress, stakeholders, and the public to ensure that our trade agenda advances our economic interests and reflects our values...the Model BIT that the Obama Administration released in 2012 followed[] an extensive period of public comment and consultation.

USTR fails to mention that all public interest groups acting as advisors in the 2012 model BIT development process opposed the resulting model BIT as a rejection of their recommendations for change and an embrace of the ISDS status quo. Heeding the counsel of corporate advisors in the model BIT review process, the administration chose to perpetuate the investor-state regime's expansive corporate privileges.

Since then, ISDS opposition has only grown. Members of Congress have voiced increasing opposition to ISDS in "trade" pacts via letters and floor statements.¹⁷³ As mentioned, NCSL approved in 2012 a resolution stating in unequivocal terms that the bipartisan association of state legislatures would oppose any pact with ISDS.¹⁷⁴ Legal scholars from around the world have announced their opposition to ISDS in a letter that urges governments to "withdraw[] from or renegotiate[]" investor-state pacts.¹⁷⁵ Conservative groups have also joined the anti-ISDS chorus, as the CATO Institute made clear in its March 2014 article calling for ISDS to be excluded from TAFTA due to "legitimate concern that corporations will run roughshod over domestic laws."¹⁷⁶ Echoing that concern, 120 legal scholars from leading universities in the United States, Europe and elsewhere recently submitted a joint response to the European Commission public consultation on ISDS that strongly criticized the proposed inclusion of ISDS in TAFTA.¹⁷⁷

The largest U.S. labor, environmental, health, privacy, Internet freedom, financial, development, family farmer, faith and consumer groups have also called for the Obama administration to exclude investor-state provisions in U.S. agreements. Noting in a December 2013 letter that ISDS provisions in past U.S. pacts have undermined public interest policies and democratic decision-making, these diverse "stakeholders" have made clear they do not see the current trade agenda as "reflecting our values."¹⁷⁸ This view is held across the political spectrum. Conservative and small business stakeholders opposing TAFTA's inclusion of ISDS include the U.S. Business and Industry Council, Coalition for a Prosperous America,¹⁷⁹ the CATO Institute,¹⁸⁰ and various tea party groups.¹⁸¹ Numerous large U.S. public interest groups and small business associations indicated similar sentiments by signing a February 2014 letter urging USTR to launch a public consultation process on the inclusion of ISDS in TAFTA, to parallel the EU public consultation. Groups such as the AFL-CIO, Consumers Union, National Farmers Union, Natural Resources Defense Council, Presbyterian Church USA and U.S. Business and Industry Council argued:

*...[a] public consultation process in which American workers, families, communities, small businesses, faith institutions and civil society organizations have a real voice will be an important step toward creating more balanced investment policies that reflect the diverse needs and interests of real people and their communities, not simply large, global corporations.*¹⁸²

The Obama administration has denied this broadly-supported request, refusing thus far to initiate a public consultation on the inclusion of ISDS in TAFTA.

The current breadth of U.S. opposition to ISDS stems in part from the manner in which the Obama administration handled the “extensive period of public comment and consultation” that USTR characterizes as part of the development of the 2012 U.S. model BIT that now serves as the U.S. template for TAFTA’s investment provisions. Though the Obama administration solicited the input of several public interest groups in developing the model BIT, that input was ignored. As part of the consultation, public interest organizations represented on a special subcommittee of business, civil society and academic representatives (under the Advisory Committee on International Economic Policy) submitted a list of 17 concrete recommendations for the model BIT. But when the organizations saw the “new” model BIT, they concluded that the administration had outright rejected 15 of their 17 recommendations. The results of the remaining two recommendations “fell well short of expectations.”¹⁸³

The groups had tried to reform the old U.S. model BIT to “make[] dispute settlement consistent with the public interest,” “ensure[] that foreign investors do not have greater rights than U.S. investors,” and “protect[] health, safety, and the environment and promote[] good jobs.”¹⁸⁴ Instead, the “extensive period of public comment and consultation” touted by USTR ignored these recommendations, producing a “new” model BIT that mirrored the old model BIT and its dangers to the public interest.¹⁸⁵

Conclusion

USTR’s factsheet of counterfactual defenses of the investor-state system will not succeed in dispelling the growing criticism of the regime. As foreign corporations launch more and more investor-state attacks against a widening array of domestic safeguards, and as tribunals hand down ever-more-expansive rulings against those safeguards, ISDS opposition will continue to mount. In the wake of increasing ISDS damage to the public interest and democratic governance, USTR’s claims about the system’s benign nature sound fanciful. Rather than try to silence critical voices with far-fetched reassurances, the Obama administration should engage in genuine consultation with critics of the investor-state system, heed their warnings of its threats and reexamine its controversial and extraordinary terms. While doing so, the administration should halt the expansion of those terms by scrapping the proposed inclusion of ISDS in TAFTA. As the world rejects this extreme regime, we cannot afford to further embrace it.

Endnotes

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²² United Nations Conference on Trade and Development, *Trade and Development Report, 2014*, (New York: United Nations, 2014), at 159. Available at: http://unctad.org/en/PublicationsLibrary/tdr2014_en.pdf.

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⁵² See Vicki Been and Joel C. Beauvais, “The Global Fifth Amendment? NAFTA’s Investment Protections and the Misguided Quest for an International ‘Regulatory Takings’ Doctrine,” *New York University Law Review*, April 2003. Available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=337480. (“Although many have argued that NAFTA simply ‘exports’ the U.S. regulatory takings standard into international law, we demonstrate that, in fact, the NAFTA tribunal decisions and dicta significantly exceed U.S. takings protections (which are already among the most protective in the world) in several respects,” at 5.)

⁵³ See Lori Wallach, “‘Fair and Equitable Treatment’ and Investors’ Reasonable Expectations: Rulings in U.S. FTAs & BITs Demonstrate FET Definition Must be Narrowed,” PC memo, September 5, 2012. Available at: <http://www.citizen.org/documents/MST-Memo.pdf>.

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⁵⁵ Rudolf Dolzer, “Fair and Equitable Treatment: Today’s Contours,” *Santa Clara Journal of International Law*, 12: 1, January 17, 2014, at 21. Available at: <http://digitalcommons.law.scu.edu/cgi/viewcontent.cgi?article=1147&context=scujil>.

⁵⁶ *Occidental Exploration and Production Company v. The Republic of Ecuador*, Final Award, Ad hoc – UNCITRAL Arbitration Rules (2004), at para. 183. Italics added. Available at: <http://italaw.com/sites/default/files/case-documents/ita0571.pdf>.

⁵⁷ *Occidental Exploration and Production Company v. The Republic of Ecuador*, Final Award, Ad hoc – UNCITRAL Arbitration Rules (2004), at para. 187. Available at: <http://italaw.com/sites/default/files/case-documents/ita0571.pdf>.

⁵⁸ See Lori Wallach, “‘Fair and Equitable Treatment’ and Investors’ Reasonable Expectations: Rulings in U.S. FTAs & BITs Demonstrate FET Definition Must be Narrowed,” PC memo, September 5, 2012. Available at: <http://www.citizen.org/documents/MST-Memo.pdf>.

⁵⁹ Supreme Court rulings have indicated that compensation for claims of “regulatory takings” under the Fifth Amendment of the U.S. Constitution is only available when a government measure results in “permanent physical invasion” of a property, causes a complete and permanent destruction of a property’s value, constitutes a land-use exaction “so onerous that, outside the exactions context, they would be deemed *per se* physical takings,” or is otherwise “functionally equivalent to the classic taking in which government directly appropriates private property or ousts the owner from his domain.” *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 528, 537-540, 547-548 (2005).

⁶⁰ “[O]ur cases have long held that mere diminution in value of property, however serious, is insufficient to demonstrate a taking.” *Concrete Pipe & Products of California, Inc. v. Construction Laborers Pension Trust for Southern California.*, 508 U.S. 602, 645 (1993).

⁶¹ Harvey M. Jacobs, “New Actions or New Arguments over Regulatory Takings?” *The Yale Law Journal*, 117: 65 (September 16, 2007). Available at: <http://www.yalelawjournal.org/forum/new-actions-or-new-arguments-over-regulatory-takings>.

⁶² See Robert Meltz, “Takings Decisions of the U.S. Supreme Court: A Chronology,” Congressional Research Service report, December 9, 2013. Available at: <http://fas.org/sgp/crs/misc/97-122.pdf>.

⁶³ *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador*, ICSID Case No. ARB/06/11, Award (Oct. 5, 2012), at para. 455. Available at: <http://italaw.com/sites/default/files/case-documents/italaw1094.pdf>.

⁶⁴ See Eduardo Moisés Peñalver, “Is Land Special?” 31 *Ecology L.Q.* 227, 231 (2004) (“it is almost beyond dispute that . . . the [Supreme] Court has focused overwhelmingly on regulations affecting land and that landowners bringing regulatory takings claims stand a greater chance of prevailing in the Supreme Court than the owners of other sorts of property”); Molly S. McUsic, “The Ghost of Lochner: Modern Takings Doctrine and Its Impact on Economic Legislation,” 76 *B.U. L. Rev.* 605, 647, 655 (1996) (“Economic interests, such as personal property, trade secrets, copyright, and money, are all recognized by the Court as ‘property’ under the Fifth Amendment, but receive little protection against government regulation.”) J. Peter Byrne, “Ten Arguments for the Abolition of Regulatory Takings Doctrine,” 22 *Ecology L.Q.* 89, 127 (1995) (“the Supreme Court has shown absolutely no interest in applying the regulatory takings doctrine to assets other than land”).

⁶⁵ *Lucas v. South Carolina Coastal Comm’n*, 505 U.S. 1003, 1027-28 (1992). For further information on Supreme Court cases indicating that indirect takings compensation is generally only available for real estate claims in U.S. law, including a rebuttal to the common claim that the Supreme Court’s decision in *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986 (1984) provides an exception to the rule, see Matthew C. Porterfield, “International Expropriation Rules and Federalism,” 23 *Stanford Environmental Law Journal* 3, 11-16 (2004).

⁶⁶ 2012 U.S. Model Bilateral Investment Treaty, U.S. Department of State, 2012, at Article 1. Available at: <http://www.state.gov/documents/organization/188371.pdf>.

⁶⁷ Dominican Republic – Central America – United States Free Trade Agreement, ch. 10 (Annex 10-B), August 5, 2004, Pub. L. No. 109-53, 119 Stat. 462 (2005), at 10-27.

⁶⁸ The U.S. government attempted to make clear the narrowness of the “minimum standard of treatment” standard in its official submission in the *RDC* case, stating, “These provisions [in the CAFTA annex] demonstrate the CAFTA-DR Parties’ express intent to incorporate the minimum standard of treatment required by customary international law as the standard for treatment in CAFTA-DR Article 10.5. Furthermore, they express an intent to guide the interpretation of that Article by the Parties’ understanding of customary international law, i.e., the law that develops from the practice and *opinio juris* of States themselves, rather than by interpretations of similar but differently worded treaty provisions. The burden is on the claimant to establish the existence and applicability of a relevant obligation under customary international law that meets these requirements.” *Railroad Development Corporation v. Republic of Guatemala*, ICSID Case No. ARB/07/23, Submission of the United States of America (January 31, 2012), at para. 3. Available at: http://italaw.com/sites/default/files/case-documents/ita0709_0.pdf.

⁶⁹ *Railroad Development Corporation v. Republic of Guatemala*, ICSID Case No. ARB/07/23, Award (June 29, 2012), at para. 219. Available at: <http://italaw.com/sites/default/files/case-documents/ita1051.pdf>. For more information, see Lori Wallach and Ben Beachy, “CAFTA Investor-State Ruling: Annex on Minimum Standard of Treatment, Proposed for TPP, Proves Insufficient as Tribunal Ignores Customary International Law Standard, Applies MST Definition from Past NAFTA Award to Rule against Guatemala,” PC memo, July 19, 2012. Available at: <http://www.citizen.org/documents/RDC-vs-Guatemala-Memo.pdf>. And see Lori Wallach and Ben Beachy, “Rebutting Misleading Claims Made by Industry with Respect to *RDC v. Guatemala* Award: CAFTA Tribunal Rejected CAFTA Parties’ and CAFTA Annex 10-B’s Definition of CIL Based on State Practice, Imported Past Tribunal’s MST Standard,” PC memo, November 17, 2012. Available at: <http://www.citizen.org/documents/rdc-v-guatemala-rebuttal.pdf>.

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⁷¹ *TECO Guatemala Holdings, LLC v. Republic of Guatemala*, ICSID Case No. ARB/10/23, Award (December 19, 2013), at para. 780. Available at: <http://italaw.com/sites/default/files/case-documents/italaw3035.pdf>.

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⁷³ Communication from juror Robert Bruce to John Corlew, attorney, November 24, 1995, on file with Public Citizen.

⁷⁴ This included \$100 million in compensatory damages and \$160 million in punitive damages. However, these two stages were meant to be separate. In the punitive damages phase, the jury returned a corrected award of \$400 million, for a total of \$500 million. See *The Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Award (June 26, 2003), at paras. 96 and 101. Available at: <http://www.state.gov/documents/organization/22094.pdf>.

⁷⁵ *Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Counter-Memorial of the United States of America (March 30, 2001), at 144-152. Available at: <http://www.state.gov/documents/organization/7387.pdf>.

⁷⁶ *Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Counter-Memorial of the United States of America (March 30, 2001), at 64. Available at: <http://www.state.gov/documents/organization/7387.pdf>. “Although Loewen values the settlement at \$175 million for present purposes, that amount does not reflect the deferral of payment and tax benefits that Loewen received from the settlement. In statements to the U.S. Securities and Exchange Commission (a federal agency that regulates the securities markets) and in its press releases at the time, Loewen estimated the aftertax, net present value of the settlement to be approximately \$85 million.”

⁷⁷ *Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Notice of Claim, (October 30, 1998), at paras. 139, 162 and 187. Available at: <http://www.state.gov/documents/organization/3922.pdf>.

⁷⁸ See *Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Decision on hearing of Respondent’s objection to competence and jurisdiction (January 5, 2001), at 45, 54. Available at: <http://italaw.com/sites/default/files/case-documents/ita0469.pdf>. And see *Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Award (June 26, 2003), at 212. Available at: <http://italaw.com/sites/default/files/case-documents/ita0470.pdf>.

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- ⁸⁸ See *AAZA v. Doe Run Resources Corp.*, No. 4:07CV1874 CDP, 2008 WL 748328 (E.D.Mo. Mar. 18, 2008) (order granting plaintiff’s motion to remand to state courts). And see *A.O.A. v. Doe Run Resources Corp.*, 2011 WL 2553259 (E.D.Mo. June 22, 2011) (denial of plaintiffs’ motion to remand to state courts).
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¹¹⁷ Conversation between Public Citizen staff and TPP negotiators, December 2013.

¹¹⁸ In the Korea FTA, for example, the general exceptions provisions of Article 23.1 do not apply to the investment chapter. And exceptions related to taxation in Article 23.3 apply only narrowly to the investment chapter, not covering, for-example, claims based on the “minimum standard of treatment” obligation – the most successfully-invoked basis for investor-state claims under U.S. pacts. The investment chapter itself contains no meaningful defense or exception clause for challenged environmental or health measures – only the ineffectual clause addressed in the next paragraph. United States-Korea Free Trade Agreement, U.S.-S. Kor, Chapters 11 and 23, June 30, 2007, 46 I.L.M. 642.

¹¹⁹ “Nothing 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.” Italics added. This language is found in the 2012 U.S. model BIT, the leaked TPP investment chapter and past FTAs such as the Korea FTA. 2012 U.S. Model Bilateral Investment Treaty, U.S. Department of State, 2012, at Article 12(5). Available at: <http://www.state.gov/documents/organization/188371.pdf>.

Trans-Pacific Partnership, investment chapter leaked June 2012, at Article 12.15(1). Available at: <http://www.citizenstrade.org/ctc/wp-content/uploads/2012/06/tppinvestment.pdf>. United States-Korea Free Trade Agreement, U.S.-S. Kor, Article 11.10, June 30, 2007, 46 I.L.M. 642.

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¹²¹ See Andreas Kulick, *Global Public Interest in International Investment Law*, (Cambridge: Cambridge University Press, 2012), at 70-71.

¹²² *S.D. Myers, Inc. v. Government of Canada*, Separate Opinion by Dr. Bryan Schwartz (on the Partial Award), Ad hoc—UNCITRAL Arbitration Rules (2000), at para. 117. Available at: <http://italaw.com/sites/default/files/case-documents/ita0748.pdf>.

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- ¹²⁶ United States-Korea Free Trade Agreement, U.S.-S. Kor, Article 20.3(b)(i), June 30, 2007, 46 I.L.M. 642.
- ¹²⁷ Trans-Pacific Partnership, Environment Chapter: Consolidated Text, November 24, 2013. Available at: <https://wikileaks.org/tpp-enviro/>. Italics added.
- ¹²⁸ See Public Citizen, “Table of Foreign Investor-State Cases and Claims under NAFTA and Other U.S. ‘Trade’ Deals,” PC chart, August 2014. Available at: <http://www.citizen.org/documents/investor-state-chart.pdf>.
- ¹²⁹ Earlier ISDS cases resulting in awards of comparably small amounts, include, for example, *Metalclad v. Mexico, S.D. Myers v. Canada* and *Feldman Karpa v. Mexico*. See Public Citizen, “Table of Foreign Investor-State Cases and Claims under NAFTA and Other U.S. ‘Trade’ Deals,” PC chart, August 2014. Available at: <http://www.citizen.org/documents/investor-state-chart.pdf>. For a summary of recent ISDS awards of much larger amounts, see United Nations Conference on Trade and Development, “Recent Developments in Investor-State Dispute Settlement (ISDS),” IIA Issues Note No. 1, April 2014, at 21. Available at: http://unctad.org/en/PublicationsLibrary/webdiaepcb2014d3_en.pdf.
- ¹³⁰ See Lori Wallach and Ben Beachy, “*Occidental v. Ecuador* Award Spotlights Perils of Investor-State System: Tribunal Fabricated a Proportionality Test to Further Extend the FET Obligation and Used “Egregious” Damages Logic to Hit Ecuador with \$2.4 Billion Penalty in Largest Ever ICSID Award,” PC memo, November 21, 2012. Available at: <http://www.citizen.org/documents/oxy-v-ecuador-memo.pdf>.
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