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I. Introduction

Once established as a shield that would level the playing field and protect foreign investors, the North American Free Trade Agreement's investor-state regime (Chapter 11) is increasingly referenced as a sword that attacks state sovereignty, favors foreign investors, and costs taxpayers billions of dollars.[1] Nevertheless, when President George W. Bush signed the Dominican Republic-Central American Free Trade Agreement in 2005, it too included an investment provision with an investor-state dispute resolution mechanism (Chapter 10).[2] The persistence of these sorts of investment provisions leads one to wonder: Are the critics mistaken? Is there a place for investor protection and citizen-state litigation in international law after all?

This Note argues that there is still a place for investor protection and citizen-state litigation in international law. Part II examines the layout of the North American Free Trade Agreement (NAFTA) Chapter 11, and the impetus behind its creation. Part III then outlines the most common criticisms of Chapter 11, particularly those issues recently addressed in the Dominican Republic-Central American Free Trade Agreement (CAFTA). It explores claims that Chapter 11 unfairly favors foreign investors, hinders U.S. sovereignty, and costs taxpayers exorbitant amounts of money. It also addresses the absence of an appeals mechanism and the lack of transparency under NAFTA Chapter 11. It then concludes that generally these concerns and criticisms are exaggerated and, hence, the problems posed by an investor-state mechanism are not as daunting as critics suggest.

Part IV moves into a discussion of CAFTA Chapter 10. Part V parallels Part III's criticisms, but from the perspective of CAFTA—exploring the text of CAFTA and summarizing how CAFTA addresses each of these issues. An examination of CAFTA illustrates that, even if the criticisms of NAFTA were not overblown, CAFTA effectively addresses them. The improvements adopted by CAFTA demonstrate that, to the extent that it is problematic, the

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1. *See* MARY BOTTARI & LORI WALLACH, NAFTA'S THREAT TO SOVEREIGNTY AND DEMOCRACY: THE RECORD OF NAFTA CHAPTER 11 INVESTOR-STATE CASES 1994–2005: LESSONS FOR THE CENTRAL AMERICAN FREE TRADE AGREEMENT 79 (2005) ("[I]nstead of providing investors with a shield against government seizure of property, those investor protections are being wielded by investors as a sword to attack an array of regulatory policies and everyday government functions."), *available at* http://www.citizen.org/documents/Chapter%2011%20Report%20Final.pdf.

2. The Central America-Dominican Republic-United States Free Trade Agreement, art. 10, Aug. 5, 2004, 43 I.L.M. 514 (draft text), [hereinafter CAFTA], *available at* http://www.ustr.gov/Trade_Agreements/Bilateral/CAFTA/CAFTA-DR_Final_Texts/Section_ Index.html (last visited Sept. 13, 2006) (on file with the Washington and Lee Law Review).

investor-state mechanism can adapt and become an effective method of investor protection and dispute resolution. Finally, Part VI concludes that investor protection and citizen-state litigation still have a place in international law.

Investment provisions raise a number of issues, but this Note does not attempt to address all of them. Specifically, this Note is written from the perspective of the United States Government and U.S. investors. It does not speak to the benefits or detriments of the investment provisions from the perspective of foreign governments or foreign investors.

II. Foreign Investment Under NAFTA: Chapter 11

A. NAFTA Chapter 11

NAFTA's Chapter 11 establishes rules to protect investors who wish to invest in a foreign member-State. Section A requires member-States to grant foreign investors a series of rights. If, for example, a U.S. corporation invests money in a project in Mexico, the Mexican Government must grant that corporation "most-favored-nation" status,[3] and must afford it a "minimum standard of treatment," as required by international law.[4] Further, the Government of Mexico is barred from discriminating against that corporation,[5] imposing certain "performance requirements" on the corporation,[6] limiting the corporation's hiring to a

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3. North American Free Trade Agreement, U.S.-Can.-Mex., art. 1103, Dec. 17, 1992, 32 I.L.M. 289 (1993) [hereinafter NAFTA]. The article states,

> Each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords, in like circumstances, to investments of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.
>
> Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments . . . .

Id.

4. *See id.* at art. 1105 ("Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.").

5. *See id.* at arts. 1101–02 ("Each Party shall accord to investors of another Party treatment no less favorable than that it accords in like circumstances to its own investors . . . .").

6. *See id.* at art. 1106 (outlining performance requirements). The article specifies,

> 1. No Party may impose or enforce any of the following requirements, or enforce any commitment or undertaking, in connection with the establishment, acquisition, expansion, management, conduct or operation of an investment of an investor of a

particular nationality,[7] restricting its free transfer of funds,[8] or expropriating the corporation's investment without just compensation.[9] Section A concludes by explaining that nothing in Chapter 11 "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."[10]

Section B of NAFTA Chapter 11 provides a dispute resolution mechanism that allows investors to bring suit against a Treaty Party should that Party fail to live up to any of its obligations under Section A. If, to return to the above example, the Mexican Government discriminated against a U.S. corporation, that corporation could submit a claim for damages against Mexico. In order to submit a claim, investors must meet certain conditions.[11] Section B directs investors who meet these conditions

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> Party or of a non-Party in its territory: (a) to export a given level or percentage of goods or services; (b) to achieve a given level or percentage of domestic content; (c) to purchase, use or accord a preference to goods produced or services provided in its territory, or to purchase goods or services from persons in its territory; (d) to relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment; (e) to restrict sales of goods or services in its territory that such investment produces or provides by relating such sales in any way to the volume or value of its exports or foreign exchange earnings; (f) to transfer technology, a production process or other proprietary knowledge to a person in its territory, except when the requirement is imposed or the commitment; (g) to act as the exclusive supplier of the goods it produces or services it provides to a specific region or world market . . . .

Id.

7. *See id.* at art. 1107 ("No Party may require that an enterprise of that Party that is an investment of an investor of another Party appoint to senior management positions individuals of any particular nationality . . . .").

8. *See id.* at art. 1109 ("Each Party shall permit all transfers relating to an investment of an investor of another Party in the territory of the Party to be made freely and without delay . . . .").

9. *See id.* at art. 1110. The article explains:

> 1. No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ('expropriation'), except: (a) for a public purpose; (b) on a non-discriminatory basis; (c) in accordance with due process of law and Article 1105(1); and (d) on payment of compensation in accordance with paragraphs 2 through 6.

Id.

10. *Id.* at art. 1114.

11. *See id.* at art. 1121 (listing the conditions required to submit a claim). The conditions are as follows:

to submit their claims to binding international arbitration through the International Center for Settlement of Investment Disputes (ICSID) Convention Rules,[12] the ICSID Additional Facility Rules,[13] or the United Nations Commission on International Trade Law (UNCITRAL)[14]

> 1. A disputing investor may submit a claim under Article 1116 to arbitration only if: (a) the investor consents to arbitration in accordance with the procedures set out in this Agreement; and (b) the investor and, where the claim is for loss or damage to an interest in an enterprise of another Party that is a juridical person that the investor owns or controls directly or indirectly, the enterprise, waive their right to initiate or continue before any administrative tribunal or court under the law of any Party, or other dispute settlement procedures, any proceedings with respect to the measure of the disputing Party that is alleged to be a breach referred to in Article 1116, except for proceedings for injunctive, declaratory or other extraordinary relief, not involving the payment of damages, before an administrative tribunal or court under the law of the disputing Party. 2. A disputing investor may submit a claim under Article 1117 to arbitration only if both the investor and the enterprise: (a) consent to arbitration in accordance with the procedures set out in this Agreement; and (b) waive their right to initiate or continue before any administrative tribunal or court under the law of any Party, or other dispute settlement procedures, any proceedings with respect to the measure of the disputing Party that is alleged to be a breach referred to in Article 1117, except for proceedings for injunctive, declaratory or other extraordinary relief, not involving the payment of damages, before an administrative tribunal or court under the law of the disputing Party.

Id.

12. *See* Int'l Ctr. for Settlement of Investment Disputes [ICSID], ICSID Convention Regulations and Rules (Jan. 2003), [hereinafter ICSID Convention Rules] (establishing rules for arbitrations tried through the International Center for Settlement of Investment Disputes), http://www.worldbank.org/icsid/basicdoc/basicdoc.htm (last visited Sept. 13, 2006) (on file with the Washington and Lee Law Review). ICSID is an autonomous international organization "with close links to the world bank." *See* ICSID, *About ICSID*, http://www.worldbank.org/icsid/about/about.htm (last visited Sept. 13, 2006) (on file with the Washington and Lee Law Review). The Convention on the Settlement of Investment Disputes between States and Nationals of Other States, which came into effect in 1966, created ICSID. *Id.* Currently neither Mexico nor Canada are Parties to the Convention; hence, in practice, the ICSID Convention Rules are not a true option. *Id.* If Parties elect to proceed under ICSID, they must do so under the ICSID Additional Facility Rules, which were designed for proceedings that fall outside the scope of the Convention. *Id.*

13. *See* ICSID, ICSID Additional Facility Rules, art. 53(3) (2003), [hereinafter ICSID Additional Facility Rules] (establishing Rules for arbitrations that fall outside the scope of the ICSID Convention), http:// www.worldbank.org/icsid/facility/facility.htm (last visited Sept. 13, 2006) (on file with the Washington and Lee Law Review).

14. *See* U.N. Comm'n on Int'l Trade Law [UNCITRAL], UNCITRAL Arbitration Rules (1976) [hereinafter UNCITRAL Arbitration Rules] (outlining arbitration Rules for The United Nations Commission on International Trade Law (UNCITRAL)), www.uncitral.org/pdf/english/texts/arbitration/arb-rules/arb-rules.pdf. The General Assembly of the United Nations established UNCITRAL through Resolution 2205(XXI) of 17 December 1966. *See* UNCITRAL, *Origin, Mandate and Composition of UNCITRAL*, http://www.uncitral.org/uncitral/en/about/origin.html (last visited Sept. 13, 2006) (listing facts about establishment

Arbitration Rules.[15] ICSID and UNCITRAL are existing international bodies that establish procedures for ad hoc arbitration of international commercial and investment disputes.[16] Each ad hoc tribunal "shall comprise three arbitrators, one arbitrator appointed by each of the disputing parties and the third, who shall be the presiding arbitrator, appointed by agreement of the disputing parties."[17] Unless the Parties agree otherwise, arbitrations will be held "in the territory of a Party that is a party to the New York Convention"[18] in accordance with the ICSID or UNCITRAL rules.[19] Under the ICSID Additional Facility Rules, the arbitral tribunal will determine the place of arbitration "after consultation with the parties and the Secretariat."[20] UNCITRAL provides that the arbitral tribunal will determine the place of arbitration, "having regard to the circumstances of the arbitration."[21]

Once the tribunal is set up, the arbitrators will decide the issues in dispute in accordance with NAFTA and applicable rules of international law.[22] The NAFTA Commission's interpretations likewise bind the tribunal.[23] If the tribunal determines that the defending Party violated NAFTA, it may award monetary damages and applicable interest or restitution of property to the investor.[24] Arbitral awards have no precedential value and only bind the parties in the case.[25]

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and members of UNCITRAL) (on file with the Washington and Lee Law Review). The United States, Canada, and Mexico are all members of UNCITRAL. *Id.*

15. *See* NAFTA, *supra* note 3, at art. 1120 ("[A] disputing investor may submit the claim to arbitration under: (c) the UNCITRAL Arbitration Rules.").

16. *See* ICSID Convention Rules, *supra* note 12, at Introduction ("In accordance with the provisions of the Convention, ICSID provides facilities for conciliation and arbitration of investment disputes between Contracting States and nationals of other Contracting States."); *see also* UNCITRAL Arbitration Rules, *supra* note 14, at Preface ("The General Assembly . . . recommends the use of the Arbitration Rules of the United Nations Commission on International Trade Law in the settlement of disputes arising in the context of international commercial relations.").

17. NAFTA, *supra* note 3, at art. 1123.

18. *Id.* at art. 1130 (referring to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, 21 U.S.T. 2517).

19. *See id.* at art. 1130 (requiring the place of arbitration to be chosen in accordance with ICSID and UNCITRAL).

20. ICSID Additional Facility Rules, *supra* note 13, at art. 21(1).

21. UNCITRAL Arbitration Rules, *supra* note 14, at art. 16(1).

22. *See* NAFTA, *supra* note 3, at art. 1131(1) (providing recommendations for applying international law).

23. *See id.* at arts. 1131–32 (providing guidance for interpreting annexes to NAFTA).

24. *See id.* at art. 1135 (explaining the forms of final arbitration awards).

25. *See id.* at art. 1136 (containing provisions on finality and enforcement of awards).

NAFTA does not provide an appellate body for arbitral awards; however, parties may initiate proceedings to revise, set aside, or annul the award.[26] In practice, review proceedings take place in domestic courts under the domestic law of the place of arbitration, as provided by UNCITRAL and the ICSID Additional Facility Rules.[27] If Mexico and Canada were parties to the ICSID Convention, decisions rendered under that body would be reviewed by the ad hoc committee.[28] Once the award is final, investors may seek to enforce the award under the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States,[29] the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards[30] (New York Convention), or the Inter-American Convention on International Commercial Arbitration[31] (Inter-American Convention).[32]

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26. *See* Patricia Isela Hansen, *Judicialization and Globalization in the North American Free Trade Agreement*, 38 TEX. INT'L L.J. 489, 498 (2003) (discussing parties' post judgment options).

27. *See* U.N. Comm'n on Int'l Trade Law (UNCITRAL), Model Law on Int'l Commercial Arbitration, Annex 1 art. 34, June 21, 1985, 24 I.L.M. 1302 (1985) (referring to "recourse to a court against an arbitral award made" in the territory of this State under this Law).

28. *See* Convention on the Settlement of Investment Disputes Between States and Nationals of Other States art. 52(3), Mar. 8, 1965, 17 U.S.T. 1270 [hereinafter Convention on the Settlement of Investment Disputes] ("On receipt of the request the Chairman shall forthwith appoint from the Panel of Arbitrators an ad hoc Committee of three persons."). The Convention continues:

> None of the members of the Committee shall have been a member of the Tribunal which rendered the award, shall be of the same nationality as any such member, shall be a national of the State party to the dispute or of the State whose national is a party to the dispute, shall have been designated to the Panel of Arbitrators by either of those States, or shall have acted as a conciliator in the same dispute.

Id.

29. *See id.* (explaining the administrative processes for enforcement under the Convention).

30. *See* U.N. Convention on the Recognition and Enforcement of Foreign Arbitral Awards arts. I–III, June 10, 1958, 21 U.S.T. 2517 ("This Convention shall apply to the recognition and enforcement of arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought . . . .").

31. *See* Inter-American Convention on Int'l Commercial Arbitration, arts. 1–3, Jan. 30, 1975, 1438 U.N.T.S. 249 ("An agreement in which the parties undertake to submit to arbitral decision any differences that may arise or have arisen between them with respect to a commercial transaction is valid.").

32. *See* NAFTA, *supra* note 3, at art. 1136(6) ("A disputing investor may seek enforcement of an arbitration award under . . . the Inter-American Convention . . . .").

B. The Development of Chapter 11

While many people think of NAFTA's Chapter 11 as a novel provision,[33] the investor dispute resolution mechanism was foreshadowed by a series of developments in trade law beginning in the 1950s.[34] Prior to World War II, only sovereign nations had legal personalities in international fora.[35] Private parties did not have standing to bring claims.[36] The only way for a private party to redress an injury by a foreign government was to petition his home state to file a claim on his behalf.[37]

However, as direct foreign investment multiplied in the 1950s and 1960s, the state-state dispute resolution method became increasingly unsatisfactory. Sovereign states were not always willing to pursue a claim against a foreign government, even if to do so would be in the interest of an individual citizen.[38] Even when a state did pursue a claim, the sovereign was apt to approach the dispute from its own perspective, rather than as a disinterested advocate of the investor.[39] Hence, in practice, private parties did not always have meaningful

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33. *See* Vincent L. Frakes, *NAFTA's Chapter 11 as a Judicial Vehicle for the Expansion of Investor Rights*, 1 BUS. L. BRIEF (AM. U.) 49 (2005) ("Chapter 11 of the North American Free Trade Agreement (NAFTA) established novel rules governing disputes between investors and member countries."); *see also* Robert B. Ahdieh, *Between Dialogue and Decree: International Review of National Courts*, 79 N.Y.U. L. REV. 2029, 2163 (2004) (referring to the "novel setting of Chapter 11").

34. *See* Barton Legum, *The Innovation of Investor-State Arbitration Under NAFTA*, 43 HARV. INT'L L.J. 531, 534–37 (2002) (explaining how earlier developments in international law foreshadowed the creation of NAFTA Chapter 11).

35. *See* René Lettow Lerner, *International Pressure To Harmonize: The U.S. Civil Justice System in an Era of Global Trade*, 2001 B.Y.U. L. REV. 229, 244 (2001) (providing a history of international legal personality).

36. *See id.* ("The ability of a private party to sue a foreign government directly is relatively recent in international law.").

37. *See id.* ("If a state's national were [to be] injured by the acts of a foreign government, only the state itself could bring a claim, acting on its national's behalf.").

38. *See* Glen T. Schleyer, *Power To The People: Allowing Private Parties To Raise Claims Before The WTO Dispute Resolution System*, 65 FORDHAM L. REV. 2275, 2297 (1997) (explaining why a nation might not want to raise a valid claim on behalf of one of its constituents). Schleyer lists several examples:

> [A]s one commentator notes, a nation might not want to repeat [a private party's] point if doing so could undermine the government in another . . . case or in domestic litigation. In addition, every nation has constituents with varying interests, and the government cannot possibly represent all of their interests, no matter how well-intentioned and responsive it is.

Id.

39. *See id.* ("[A] nation's responsiveness to its constituents will be balanced against its desire to maintain amicable relations with its trading partners, especially those with significant political and economic power.").

recourse against a foreign nation.[40] By the 1970s, developing countries had begun to habitually expropriate foreign investments without always compensating investors.[41]

Under these conditions, capital-exporting countries—particularly the United States—became convinced that investors needed stronger protection.[42] This protection came in the form of a series of Bilateral Investment Treaties (BITs), which granted investors a private right of action in an investor-state dispute resolution mechanism.[43] Beginning in the 1980s, the United States entered a large number of BITs with different nations.[44] Like previous investment treaties,[45] BITs established traditional investor protections by imposing national, most-favored-nation, or other specified treaty standards on a host country's regulation of foreign investment, and by granting investors rights with respect to nationalization, expropriation, payments, and financial transfers.[46] However, BITs did not rely on traditional state-state dispute

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40. *See* Ray C. Jones, Note & Comment, *NAFTA Chapter 11 Investor-to-State Dispute Resolution: A Shield to be Embraced or a Sword to be Feared?*, 2002 B.Y.U. L. REV. 527, 529 (2002) ("Unfortunately for investors, the home government was under no obligation to bring the claim, and few investors were able to obtain relief.").

41. *See* Kenneth J. Vandevelde, *Sustainable Liberalism and the International Investment Regime*, 19 MICH. J. INT'L L. 373, 385 (1998) ("[B]y the 1970s, many developing states were more skeptical about the value of foreign investment and, in the name of Marxism or nationalism or both, expropriated major foreign investments in their territories."); *see also* Alan O. Sykes, *Public Versus Private Enforcement of International Economic Law: Standing and Remedy*, 34 J. LEGAL STUD. 631, 643 (2005) ("During the middle of the twentieth century . . . various developing countries began to question whether customary law obliged them to provide 'prompt, adequate and effective compensation' for expropriation.").

42. *See* K. Scott Gudgeon, *United States Bilateral Investment Treaties: Comments on Their Origin, Purposes, and General Treatment Standards*, 4 INT'L TAX & BUS. LAW. 105, 110 (1986) (explaining that the Legal Advisor's Office of the U.S. State Department recommended broadening treaty ties in order to promote stable legal standards for U.S. investment in the Third World); *see also* Jake A. Baccari, Comment, *The* Loewen *Claim: A Creative Use of NAFTA's Chapter 11*, 34 U. MIAMI INTER-AM. L. REV. 465, 473 (2003) ("The United States has advocated these provisions in large part because of fear of foreign expropriation of U.S. investor assets abroad.").

43. *See* Gudgeon, *supra* note 42, at 109–10 (noting that BITs went "beyond [their] predecessors by also providing for the resolution of investor-host country disputes through binding arbitration").

44. *See* David A. Gantz, *The Evolution of FTA Investment Provisions: From NAFTA to The United States-Chile Free Trade Agreement*, 19 AM. U. INT'L L. REV. 679, 693 (2004) ("[M]ore than forty U.S. BITs concluded beginning in the early 1980s.").

45. *See* Gudgeon, *supra* note 42, at 107–08 (discussing FCN treaties). Prior to the development of BITs, the United States government entered into a series of "Treaties of Friendship, Commerce and Navigation" (FCNs). These treaties provided investor protections like those in the BITs, but did not grant investors a private right of action.

46. *See* Gantz, *supra* note 44, at 693 (listing traditional provisions of a BIT).

resolution to enforce these protections. Rather, they established a system based on investor-state dispute resolution.[47]

NAFTA Chapter 11 is, in essence, a BIT contained within a trade agreement. Chapter 11 mirrors the investor protections espoused in BITs and adopts the BITs' investor-state dispute resolution mechanism. Although NAFTA primarily concerns trade, the United States advocated the inclusion of an investor-state dispute resolution mechanism because of concerns about investment expropriations by the Mexican Government.[48] Because their creation was prompted by similar concerns, it makes sense that NAFTA Chapter 11 and earlier BITs contain equivalent provisions. One author went so far as to describe Chapter 11 as "a U.S. bilateral investment treaty on steroids—a dream come true for the U.S. foreign investor."[49]

III. Criticisms of NAFTA's Investment Provision

Although NAFTA Chapter 11 did not deviate much from earlier BITs, critics question the wisdom of extending the investor-state dispute resolution mechanism into NAFTA.[50] Critics are concerned about certain effects they see stemming from the inclusion of a private right of action for investors such as greater rights for foreign investors, diminished sovereignty of the member-Parties, and high costs for taxpayers. Additionally, critics have expressed concern about the manner in which suits are handled under NAFTA—specifically, the ad hoc nature of the tribunals and the lack of transparency in the proceedings. This Part examines each of these concerns in turn. It concludes that many of the concerns about NAFTA Chapter 11 are

47. *See, e.g.*, Benjamin Klafter, *International Commercial Arbitration as Appellate Review: NAFTA's Chapter 11, Exhaustion of Local Remedies and Res Judicata*, 12 U.C. DAVIS J. INT'L L. & POL'Y 409, 412 (2006) ("The greatest innovation of the BITs has been the introduction of investor-state arbitration settlement.").

48. *See* Charles H. Brower II, *Investor-State Disputes Under NAFTA: A Tale of Fear and Equilibrium*, 29 PEPP. L. REV. 43, 47 (2001) ("Their incorporation into NAFTA represented an apparent victory for U.S. negotiators, who wanted to liberalize the Mexican investment regime, protect U.S. investors from expropriation, and remove investor-state disputes from the Mexican judicial process, which was generally considered corrupt or at least compliant with the will of the state.").

49. Jose E. Alvarez, *Critical Theory and the North American Free Trade Agreement's Chapter Eleven*, 28 U. MIAMI. INTER-AM. L. REV. 303, 304 (1997).

50. *See* BOTTARI & WALLACH, *supra* note 1, at xx ("The investor-state mechanism should be kept out of future agreements. Commercial disputes arising under the terms of international agreements between nations should be dealt with by the governments themselves on a state-state basis."); *see also* Sykes, *supra* note 41, at 643 (proposing a rationale for a private right of action in investment treaties, "a rationale . . . that does not apply to trade agreements").

exaggerated, and hence, the extension of the investor-state dispute resolution mechanism into NAFTA is not as problematic as critics suggest.

A. Greater Rights for Foreign Investors

One of the most commonly voiced criticisms of NAFTA's Chapter 11 is that it provides greater rights to foreign investors than it does to domestic investors.[51] The favoritism toward foreign investors is most often discussed in terms of NAFTA's expropriation provision.[52] Article 1110 of NAFTA states that, as a general rule, "[n]o Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment."[53] This provision is meant to provide protection similar to that afforded under the Takings Clause of the Fifth Amendment of the U.S. Constitution. The Restatement (Third) of Foreign Relations Law explains that "the line in international law is similar to that drawn in United States jurisprudence for purposes of the Fifth and Fourteenth Amendments to the Constitution in determining whether there has been a taking requiring compensation."[54]

Critics assert, however, that expropriations claims adjudicated under NAFTA tend to be more investor friendly than those adjudicated under domestic takings clause analysis.[55] First, critics complain, NAFTA grants foreign investors a private right of action against the government of a member state.[56] Under the doctrine of sovereign immunity, domestic investors have no

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51. *See* BOTTARI & WALLACH, *supra* note 1, at viii ("[U]nder NAFTA, foreign investors operating within the United States must be provided with different—superior from the investor's perspective—treatment than the Constitution requires be provided to U.S. residents and businesses.").

52. *See id.* ("[T]he 'expropriations' that have been claimed using NAFTA's foreign investor protections are nothing like the 'nationalization' or government seizure of real estate that is generally conveyed by the term. Nor are they similar to the 'takings' cases that have been adjudicated in the U.S. court system.").

53. NAFTA, *supra* note 3, at art. 1116.

54. RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 712 (1987).

55. *See, e.g.*, BOTTARI & WALLACH, *supra* note 1, at ix ("Under NAFTA, the sorts of property owned by foreign investors that are provided with such protection are defined in the text and expanded upon by NAFTA tribunals in a manner that extends far beyond U.S. law.").

56. *See* Robert J. Girouard, Note, *Water Export Restrictions: A Case Study of WTO Dispute Settlements, Strategies and Outcomes*, 15 GEO. INT'L ENVTL. L. REV. 247, 251 (2003) ("NAFTA's investment provisions give private firms a right to compensation for expropriation and a private right of action against national governments . . . .").

such right.[57] Furthermore, the right of action granted to foreign investors extends to situations in which domestic investors would not have a valid claim.[58] Critics emphasize that Article 1110 goes beyond U.S. law by explicitly recognizing that an expropriation may be accomplished through indirect measures.[59] Consequently, there will be situations in which an investor would have a valid claim under NAFTA but would not under U.S. law. Because domestic investors cannot submit to arbitration in the international tribunals, the disparate treatment functions as favoritism towards foreign investors.

Critics point to *Loewen Group Inc. v. United States*[60] as an illustration of the overly investor friendly attitude of NAFTA tribunals.[61] Although the case

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57. *See id.* at viii ("[T]he sovereign immunity shield—the long-standing common law principle that governments cannot be sued for certain types of activities—does not apply in NAFTA's private tribunal system. This means that foreign investors are empowered to sue the United States for cash compensation over federal, state and local policies in instances when U.S. residents and companies would have no such right.").

58. *See id.* ("NAFTA requires signatory governments to provide to foreign investors a variety of substantive rights that go beyond those that the U.S. Supreme Court—in balancing the specific interests of property owners with the broader public interest in public health and safety—has ruled are provided by the U.S. Constitution.").

59. *See* NAFTA, *supra* note 3, at art. 1110 ("No Party may directly or *indirectly* nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment.") (emphasis added).

60. Loewen Group Inc. v. United States, 42 I.L.M. 811 (ICSID 2003). Loewen alleged that the introduction of anti-Canadian, pro-American testimony during a Mississippi State Court trial violated the anti-discrimination rules presented in Article 1102 of NAFTA, as well as the minimum standard of treatment guarantee in Article 1105. *Id.* at ¶ 39. It also alleged that the award of excessive punitive damages against it in the civil suit amounted to an indirect expropriation under NAFTA Article 1110. *Id.* In the Mississippi State Court trial, the jury awarded O'Keefe $500 million damages, including $75 million damages for emotional distress and $400 million punitive damages. *Id.* Loewen attempted to appeal the verdict, alleging that the trial judge allowed O'Keefe's attorney to make prejudicial references "(i) to Claimants' foreign nationality (which was contrasted to O'Keefe's Mississippi roots); (ii) race-based distinctions between O'Keefe and Loewen; and (iii) class-based distinctions between Loewen (which O'Keefe counsel portrayed as large wealthy corporations) and O'Keefe (who was portrayed as running family-owned businesses)." *Id.* at ¶ 4. Loewen also alleged that the trial judge refused to instruct the jury that nationality-based, racial and class-based discrimination are impermissible. *Id.* Loewen was not successful in its appeal, however, because the trial court and the Mississippi Supreme Court refused to reduce the required appeal bond. *Id.* In order to pursue its appeal, Loewen would have had to post a $625 million bond within seven days. *Id.* at ¶ 6. After the failed appeal, Loewen claims it was forced to settle "under extreme duress." *Id.* at ¶ 7. In its ruling, the ICSID discussed the merits of the case, but eventually dismissed Loewen's claim after concluding that, it did not have jurisdiction to rule because Loewen had reincorporated in the United States. *Id.* at ¶ 240.

61. *See, e.g.*, BOTTARI & WALLACH, *supra* note 1, at 26 (explaining why "the *Loewen* decision was greeted with great concern in U.S. legal circles").

was ultimately dismissed, critics were alarmed by the *Loewen* Tribunal's discussion.[62] In its Order, the *Loewen* Tribunal found that a Mississippi trial judge "failed in his duty to take control of the trial by permitting the jury to be exposed to persistent and flagrant appeals to prejudice on the part of O'Keefe's counsel and witnesses."[63] It characterized the Mississippi trial as a "disgrace,"[64] and declared that "it did not accord with the requirements of due process."[65] Finally, the Tribunal found that the U.S. government was responsible for these failures under applicable principles of international law.[66] Critics of NAFTA Chapter 11 understand this language to imply that "U.S. court cases, even cases heard by state supreme courts or the U.S. Supreme Court, are open to challenge in NAFTA's closed-door investor-state system."[67] Under the principle asserted in *Loewen*, critics contend, foreign investors can challenge adverse decisions of U.S. courts under NAFTA.[68] Because domestic investors do not have a corresponding right, critics see the decision in *Loewen* as unfairly favoring foreign investors.[69]

In general, claims of favoritism to foreign investors are overstated. Because the drafters of Chapter 11 specifically created the provision to level the playing field on behalf of U.S. investors,[70] the suggestion that Chapter 11 favors foreign investors over domestic investors seems suspect. Indeed, upon further review, NAFTA's expropriation provisions are not nearly as far off from U.S. law as critics would have one believe.[71] The expropriation clause

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62. *See, e.g.*, Lucien J. Dhooge, The Loewen Group v. United States*: Punitive Damages and the Foreign Investment Provisions of the North American Free Trade Agreement*, 19 CONN. J. INT'L L. 495, 495 (2004) (quoting Loewen Group Inc. v. United States, 42 I.L.M. 811, ¶ 53 (ICSID 2003)) ("The O'Keefe case as presented invited the jury to discriminate against Loewen as an outsider.").

63. *Id.* at 498–99.

64. Loewen Group Inc. v. United States, 42 I.L.M. 811, ¶ 119 (ICSID 2003).

65. Dhooge, *supra* note 62, at 498–99 (citing Loewen Group Inc. v. United States, 42 I.L.M. 811, 830 (ICSID 2003)).

66. *See* Loewen Group Inc. v. United States, 42 I.L.M. 811, ¶ 123 (ICSID 2003) ("[W]e take it to be the responsibility of the State under international law and, consequently, of the courts of a State, to provide a fair trial of a case to which a foreign investor is a party.").

67. BOTTARI & WALLACH, *supra* note 1, at 26.

68. *See id.* at xiv (asserting that "foreign investors will use the investor-state system to seek compensation for adverse domestic court rulings").

69. *See id.* at xiv ("In contrast, U.S. firms operating in the United States do not have this second bite at the apple outside of the domestic court system and cannot bring regulatory takings cases based upon domestic court rulings.").

70. *See supra* notes 45–49 and accompanying text (explaining that Chapter 11 and other BITs were created to protect U.S. investments from expropriation in less-developed nations).

71. *See* Gregory M. Starner, Note, *Taking A Constitutional Look: NAFTA Chapter 11 As An Extension Of Member States' Constitutional Protection Of Property*, 33 LAW & POL'Y INT'L

mirrors the Fifth Amendment's protection against takings and the Fourteenth Amendment's due process guarantee.[72] Article 1110 creates exceptions to the expropriation rule, "(a) for a public purpose; (b) on a non-discriminatory basis; (c) in accordance with due process of law and Article 1105(1); and (d) on payment of compensation in accordance with paragraphs two through six."[73] This language mimics the language of the U.S. Constitution, specifically the Fifth and Fourteenth Amendments.[74] Furthermore, NAFTA Tribunals have incorporated U.S. case law into their analysis of expropriation.[75] Given the similarities between U.S. law and article 1110 of NAFTA, any potential for disparate treatment of foreign investors will be minimal.[76]

Furthermore, many critics' assertions regarding *Loewen* are fallacious.[77] While the tribunal in *Loewen* acknowledged that U.S. courts' behavior could amount to an indirect expropriation,[78] it did not imply that foreign investors can

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BUS. 405, 427 (2002) ("NAFTA's expropriation provisions most closely mirror the constitutional protections of U.S. takings law.").

72. *See id.* at 427 (explaining the similarities between NAFTA expropriation provisions and the U.S. Constitution).

73. NAFTA, *supra* note 3, at art. 1110.

74. *See* U.S. CONST. amend. V ("[N]or shall private property be taken for *public use*, without *just compensation*.") (emphasis added); *see also* U. S. CONST. amend. XIV ("[N]or shall any State deprive any person of life, liberty, or property, without *due process of law*") (emphasis added).

75. *See* Starner, *supra* note 71, at 427–28 (discussing NAFTA tribunals' use of U.S. case law). Starner explains,

> The tribunal in *Pope* twice referred to the U.S. Restatement on Foreign Relations in defining a regulatory taking, applying the Restatement's use of "unreasonable interference" to define an expropriation under article 1110. Additionally, the language in *Metalclad* concerning the reasonable reliance on the economic use and benefit of an investment resembles the *Lucas* Court's investment-backed expectations standard for finding a taking.

Id.

76. *See id.* at 428 ("Taken all together, NAFTA's institutional language and tribunal decisions represent a consistency with U.S. constitutional principles and takings jurisprudence that make U.S. obligations to protect foreign investment under the NAFTA a minimal shift in its constitutional takings law.").

77. *Compare* Steve Louthan, Note, *A Brave New Lochner Era? The Constitutionality of NAFTA Chapter 11*, 34 VAND. J. TRANSNAT'L L. 1443, 1450 (2001) ("[T]he Loewen Group claimed that the basic structure of Mississippi's trial system 'expropriated' their investment.") *with* Loewen Group Inc. v. United States, 42 I.L.M. 811, ¶ 39 (ICSID 2003) ("Claimants argue that . . . the discriminatory conduct, the excessive verdict, the denial of Loewen's right to appeal and the coerced settlement violated Article 1110.").

78. *See* Loewen Group Inc. v. United States, 42 I.L.M. 811, ¶ 123 (ICSID 2003) ("[W]e take it to be the responsibility of the State under international law and, consequently, of the courts of a State, to provide a fair trial of a case to which a foreign investor is a party.").

bring suit under NAFTA anytime a U.S. Court issues an adverse opinion.[79] More accurately, *Loewen* suggests that a U.S. court can be held to have expropriated a corporation's investment when it imposes a discriminatory damage award based on the investor's status as a foreigner. When viewed in this light, the concern about granting greater rights to foreign citizens dissolves. By definition, a court could not discriminate against a U.S. investor on the basis of the investment's foreign character. Hence, a U.S. investor would have no reason to submit a claim to NAFTA under these circumstances and need not be concerned that it is denied the right to do so.

Finally, even if Chapter 11 does allow foreign investors to bring suit in some situations where domestic investors would not have a claim, abandoning Chapter 11 would not solve the problem. Without Chapter 11, foreign investors (including U.S. investors who invest in other countries) would often have no recourse when a foreign government violates their rights.[80] Consequently, there will be many situations in which a domestic investor could bring a claim but a foreign investor could not.[81] In other words, supposed favoritism toward foreign investors would be replaced with favoritism toward domestic investors. This Note has established that disparate treatment of foreign investors is minimal under Chapter 11. Therefore, returning to a system in which foreign investors have very few rights is an imprudent solution.

B. Hindrances to U.S. Sovereignty

Another major criticism of NAFTA's Chapter 11 is that it undermines U.S. sovereignty. According to critics, Chapter 11 is not a shield to protect investors but a sword to attack member-state governments.[82] Critics envision

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79. *See* Loewen Group Inc. v. United States, 42 I.L.M. 811, ¶ 119 (ICSID 2003) ("By any standard of measurement, the trial involving O'Keefe and Loewen was a disgrace. By any standard of review, the tactics of O'Keefe's lawyers, particularly Mr. Gary, were impermissible. By any standard of evaluation, the trial judge failed to afford Loewen the process that was due."). Although Loewen did claim that the verdict in the Mississippi trial was excessive notwithstanding any discrimination, the Tribunal's decision that the damage award could rise to the level of an expropriation was based on the outrageous conduct of the opposing counsel and the judge in the Mississippi court, not the fact that the court issued an adverse opinion.

80. *See supra* notes 38–40 and accompanying text (explaining that individual investors were often without recourse to pursue a claim before the development of investor-state dispute mechanisms).

81. *See supra* note 41 and accompanying text (noting that foreign governments are apt to expropriate foreign investments). U.S. investors can bring suit under the Fifth and Fourteenth Amendments for the expropriation of their real property. If Chapter 11 were eliminated, foreign investors would not have that ability.

82. *See* Jones, *supra* note 40, at 545 ("One of the strongest criticisms of Chapter 11 is that

investors using their ability to bring suit against the member-State governments as leverage to deter those governments from passing otherwise valid laws.[83] Because litigating NAFTA arbitrations is costly, the U.S. Government could hesitate to pass regulations that could potentially result in a NAFTA suit.[84] This trepidation could result in a chilling of the Government's ability to pass certain social or environmental regulations.

Yet again, critics inflate concerns over sovereignty. As Ian Laird, an attorney with Davis and Company LLP, a firm that frequently handles NAFTA cases, explains:

> Governments make mistakes and sometimes they intentionally create measures that hurt foreigners. That is the history of international disputes. It is misguided reasoning to think that holding governments accountable is a threat to democracy. The real risk is that rational debate about free trade and investment will be stifled under the weight of anti-free trade hysteria.[85]

Baird further explains that the image of an avalanche of investor attacks on state regulations is unrealistic.[86] Under principles of international law, an arbitral award should put the injured party in the position it would have been but for the illegal act of the state.[87] If, for example, a country issues a valid health regulation that pulls an investor's product off the market, that investor likely would fail in NAFTA arbitration.[88] If the product is, in fact,

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by allowing investors direct access to dispute resolution, the Agreement runs the risk of promoting vexatious legislation by foreign investors and creating a threat against the national sovereignty of the NAFTA countries."); *see also* BOTTARI & WALLACH, *supra* note 1, at ix (explaining that Chapter 11 has been criticized for, "undermining the basic public interest protections . . . by extending a set of rights to foreign investors operating in the United States to attack domestic policies and demand compensation for the basic environmental, land use, health and safety policies under which U.S. businesses operate and upon which citizens rely").

83. *See* Justin Byrne, Comment, *NAFTA Dispute Resolution: Implementing True Rule-Based Diplomacy Through Direct Access*, 35 TEX. INT'L L.J. 415, 434 (2000) (concluding that meritless litigation could deter governments from passing otherwise desirable legislation).

84. *See* Jones, *supra* note 40, at 543 ("[A] NAFTA country might have to think twice before instituting unpopular legislation for fear of the financial repercussions of defending expensive litigation against private foreign investors.").

85. Ian A. Laird, *NAFTA Chapter 11 Meets Chicken Little*, 2 CHI. J. INT'L L. 223, 229 (2001).

86. *See id.* at 227 ("There were many dire predictions in the early days after the signing of NAFTA that there would be an avalanche of investor-state claims. This has not come to pass.").

87. *See id.* at 228 ("[T]he seminal Permanent Court of International Justice *Chorzow Factory* case provides that the injured party be put back in the position it would have been in but for the illegal act of the state.").

88. *See id.* at 227 ("If the product or investment is genuinely a health or environmental hazard . . . it is unlikely the investor could or would bring a claim . . . .").

unhealthy, there would not be a market for it anyway.[89] To return the investor to his unmarketable position would not require much of an arbitral award.[90] Hence, it would be worthless for the investor to bring a claim.[91] Furthermore, investors are disinclined to bring suit against a foreign sovereignty, as governments "do not easily acquiesce" to a challenge.[92] Baird contends that investors will only bring suit under NAFTA in "an extreme situation in which the claimant has attempted other non-legal routes and been rebuffed."[93]

The data supports this contention. In the over a decade since NAFTA became law, tribunals have only found one case to reach the level of an expropriation.[94] In that case, the Mexican government was accused of expropriating a U.S. corporation's investment.[95] Metalclad, a U.S. company, invested considerable resources into constructing a landfill after repeated assurances by the Mexican Government that it had the government's support to proceed.[96] After the landfill construction was completed, the Mexican Government did an about-face: It did not permit Metalclad to operate the landfill and eventually denied a permit application which previously, according to the Mexican Government, had no legal

89. *See* Laird, *supra* note 85, at 228 ("If the product or investment is genuinely a health or environmental hazard . . . it is unlikely the investor could . . . collect any damages.").

90. *See id.* (discussing the requirement of making investors whole through arbitral tribunals).

91. *See id.* (explaining the difficulties in bringing these types of claims).

92. *Id.* at 229.

93. *Id.*

94. *See* Metalclad Corp. v. United Mexican States, 40 I.L.M. 36 (ICSID 2001). In *Metalclad*, the dispute arose after Metalclad Corp., a U.S. corporation, constructed a hazardous waste landfill in Mexico. *Id.* at ¶ 1. Metalclad alleged that it initially had the support of the Mexican government, and that it relied on that support in constructing the landfill. *Id.* at ¶ 33. It further contended that after the construction was completed, the Mexican government interfered with the development and operation of the landfill. *Id.* at ¶ 1. Metalclad then brought suit under NAFTA Chapter 11, alleging violations of Article 1105 (fair and equitable treatment) and 1110 (expropriation). *Id.* at ¶ 1. The tribunal held that "Metalclad's investment was not accorded fair and equitable treatment in accordance with international law, and that Mexico has violated NAFTA Article 1105(1)." *Id.* at ¶ 74. It also held that measures taken by the Mexican government "taken together with the representations [it made], on which Metalclad relied, and the absence of a timely, orderly or substantive basis for the denial by the Municipality of the local construction permit, amount to an indirect expropriation." *Id.* at ¶ 107.

95. *See id.* at ¶ 1 (detailing the dispute and claims).

96. *See id.* at ¶ 33 ("Metalclad further asserts that it was told by the President of the INE and the General Director of the Mexican Secretariat of Urban Development and Ecology that all necessary permits for the landfill had been issued . . . .").

basis for denial.[97] The situation was exactly the sort for which Chapter 11 was established.[98]

Thus far, investors have succeeded in receiving compensation for violations of NAFTA on only five occasions.[99] Tribunals awarded damages four times, and settled one case in favor of the investor.[100] All five successful NAFTA challenges came from U.S. corporations that were investing in Mexico or in Canada.[101] The United States has never lost a case.[102] This data does not suggest that the United States would feel threatened by a major influx of NAFTA challenges. There is, therefore, no reason that the United States would feel restrained in its ability to pass valid health and safety regulations.

C. Cost to Taxpayers

Another common criticism of NAFTA's investment regime is that, because the U.S. Government is susceptible to lawsuits, the regime could cost U.S. taxpayers billions of dollars. Critics point to damages that have already been awarded under NAFTA Chapter 11 as evidence that government dollars are at risk.[103] When the NAFTA tribunal awarded $15.6 million in damages in *Metalclad v. Mexico*,[104] for example, the Government of Mexico was responsible for paying the award, thus shifting the burden to Mexican taxpayers.[105] Investors have claimed billions of dollars in damages under NAFTA.[106] Should those investors succeed in their suits against the United

97. *See id.* at ¶ 88 ("The absence of a clear rule as the requirement or not of a municipal construction permit, as well as the absence of any established practice or procedure as to the manner of handling applications for a municipal construction permit, amounts to a failure on the part of Mexico to ensure the transparency required by NAFTA.").

98. *See supra* notes 40–42 and accompanying text (explaining that Chapter 11 was created to protect U.S. investment from expropriation by other governments).

99. *See* BOTTARI & WALLACH, *supra* note 1, at i–v (summarizing all NAFTA claims filed to date).

100. *See id.* (listing cases won by investors).

101. *See id.* (explaining the nature of the claims in which investors succeeded).

102. *See id.* (noting United States success rates in NAFTA tribunals).

103. *See id.* at xv ("Five times foreign investors have succeeded with at least some of their claims and $35 million has been paid in compensation to foreign investors by governments. Another $28 billion has been claimed by NAFTA investors.").

104. *See supra* note 94 (summarizing the *Metalclad* case).

105. *See* Metalclad Corp. v. United Mexican States, 40 I.L.M. 36, ¶¶ 112–26 (ICSID 2001) (stating the amount that the government of Mexico must pay).

106. *See* Press Release, Global Trade Watch, New Study by Public Citizen's Global Trade Watch Analyzes 42 NAFTA Investor-State Challenges; Illustrates How Proposed CAFTA Would Extend Threat (Feb. 22, 2005), http://www.citizen.org/publications/release.cfm?

States, U.S. taxpayers must foot the bill. These damage awards, critics allege, "could significantly impact the treasuries of national governments."[107] Critics further complain about the costs of defending against claims.[108]

Again, concerns over the cost to taxpayers seem overstated. As explained above, since NAFTA's inception, the member States' governments have only been forced to pay damages in five cases.[109] Canada has lost three cases, and paid approximately $17.9 million in damages.[110] Mexico has lost two cases, and paid approximately $17.1 million in damages.[111] The United States has yet to lose a single case, nor has the United States ever paid to settle a case.[112] Eighteen million dollars, paid over the course of eleven years, is hardly going to bankrupt countries with annual expenditures of over $150 billion each.[113]

U.S. taxpayers, in particular, have little cause for alarm. As mentioned, the United States has yet to expend a single taxpayer penny on

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ID=7366 (last visited Sept. 13, 2006) (explaining that "the growing list of NAFTA 'investor-state' cases" now "total billions in compensation demands") (on file with the Washington and Lee Law Review).

107. BOTTARI & WALLACH, *supra* note 1, at xvi.

108. *See id.* ("In addition, the costs for countries to defend against these NAFTA investor-state claims—money that could be used elsewhere in these times of pinched budgets—is significant in itself. . . . With three concluded arbitrations and seven pending against the United States, the NAFTA arbitration defense bill for U.S. taxpayers may quickly reach over $30 million.").

109. *See id.* at i–iii (charting cases and claims submitted under the NAFTA regime).

110. *See* Pope & Talbot Inc. v. Canada, 41 I.L.M. 1347, 1362 (UNCITRAL 2002) (awarding $461,566 plus interest); S.D. Myers, Inc. v. Canada, 40 I.L.M. 1408 (UNCITRAL 2001) (awarding $4.8 million); Ethyl Corp. v. Canada (Award On Jurisdiction), 38 I.L.M. 708 (UNCITRAL 1999) (awarding $13 million settlement); *see also* BOTTARI & WALLACH, *supra* note 1, at i–v (summarizing payments for NAFTA claims).

111. *See* Marvin Feldman v. Mexico, 42 I.L.M. 625, 669 (ICSID 2002) (awarding 9,464,627.50 Mexican pesos as principal, plus interest generated at the time of signature of this award, in the amount of 7,496,428.47 Mexican pesos); Metalclad Corp. v. United Mexican States, 40 I.L.M. 36, 54 (ICSID 2001) (awarding $16.6 million; later reduced to $15.6 million by a Canadian Court in United Mexican States v. Metalclad Corp., 89 B.C.L.R. (3d) 359, ¶ 135 (Sup. Ct. B.C. 2001)).

112. *See* Office of the United States Trade Representative, *CAFTA Policy Brief—May 2005: Investment Provisions in CAFTA* (May 2005) [hereinafter CAFTA Policy Brief], *available at* http://www.ustr.gov/assets/Trade_Agreements/Bilateral/CAFTA/Briefing_Book/asset_upload_file289_7750.pdf.

113. CENTRAL INTELLIGENCE AGENCY, WORLD FACTBOOK (2005) [hereinafter WORLD FACTBOOK] (noting the following country expenditures: U.S. expenditures: $2.466 trillion; Canada expenditures: $152.6 billion; Mexico expenditures: $175.4 billion), *available at* http://www.cia.gov/cia/publications/factbook/ index.html (last visited Sept. 13, 2006).

a NAFTA damage award.[114] Furthermore, the U.S. government can easily absorb the costs of a damage award should it ever lose a case. The largest single damage award under a NAFTA tribunal was $15.6 million.[115] The United States government annually spends approximately $2.5 trillion.[116] Given these figures, it is difficult to imagine a NAFTA damage award greatly affecting taxpayers in the United States.

Finally, the picture of potentially massive damage awards painted by NAFTA's critics is misleading.[117] Damage awards in the United States tend to be higher than those in other countries[118] because of its reliance on punitive damages.[119] In *Loewen*, for instance, $400 million of the $500 million damage award was punitive, and $75 million was for emotional distress.[120] Chapter 11, however, only allows awards of "(a) monetary damages and any applicable interest; [or] (b) restitution of property, in which case the award shall provide that the disputing Party may pay monetary damages and any applicable interest in lieu of restitution."[121] It explicitly excludes the use of punitive damages.[122] Hence, it is unlikely that there will be the sort of massive damage award that one might be concerned about in domestic litigation in the United States.

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114. *See supra* note 102 and accompanying text (noting U.S. success and resulting lack of expenditure).

115. *See* Metalclad Corp. v. United Mexican States, 40 I.L.M. 36, ¶ 131 (ICSID 2001) ("Respondent shall, within 45 days from the date on which this Award is rendered, pay to Metalclad the amount of $16,685,000.00.").

116. *See* WORLD FACTBOOK, *supra* note 113 (recording U.S. expenditures at $2466 trillion).

117. *See* BOTTARI & WALLACH, *supra* note 1, at 81 (explaining the high costs of NAFTA dispute resolution, under the heading "Potential Cost to the Taxpayers Could Reach the Billions").

118. *See* Lerner, *supra* note 35, at 265 ("Most countries do not recognize punitive damages at all. Those that do allow punitive damages in some circumstances are concerned about the size of awards in the United States.").

119. *See* Erik K. Moller, Nicholas M. Pace & Stephen J. Carroll, *Punitive Damages in Financial Injury Jury Verdicts,* 28 J. LEGAL STUD. 283, 304 (1999) ("Punitive damages represent a large portion of the total amount of damages awarded (this includes verdicts in which punitive damages are awarded and verdicts in which punitive damages are not awarded): from 43% of all damages in other contract verdicts to over 70% of all damages in insurance verdicts.").

120. *See* Loewen Group, Inc. v. United States, 42 I.L.M. 811, ¶ 4 (ICSID 2003) (granting damages).

121. NAFTA, *supra* note 3, at art. 1135.

122. *See* NAFTA, *supra* note 3, at art. 1135 ("A Tribunal may not order a Party to pay punitive damages.").

D. Absence of an Appeals Mechanism

Dispute resolution under Chapter 11 alarms many critics. NAFTA opponents argue that the ad hoc nature of NAFTA arbitration and the absence of an appeals mechanism lead to inconsistency and instability in arbitral rulings.[123] Under Chapter 11's dispute resolution mechanism, investors submit claims to binding international arbitration through the ICSID Convention, the ICSID Additional Facility Rules, or the UNCITRAL Arbitration Rules.[124] These international bodies conduct investment dispute arbitrations by appointing ad hoc tribunals.[125] Rulings are binding only on the parties in the case and do not have precedential value.[126] NAFTA Chapter 11 does not mention appeals, nor is there currently a standing appellate body to review NAFTA tribunal decisions.

Under these conditions, critics complain, NAFTA Chapter 11 rulings lack stability and consistency.[127] Because each NAFTA claim is heard by a different group of arbitrators who are not required to consider the interpretations of previous tribunals, there is great potential for variation in rulings.[128] The fact

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123. *See* Marc R. Poirier, *The NAFTA Chapter 11 Expropriation Debate Through the Eyes of a Property Theorist*, 33 ENVTL. L. 851, 924 (2003) ("This lack of centralized review merely amplifies the effect of 'a system of ad hoc arbitration before tribunals that issue nonprecedential awards [that create] a lack of institutional and jurisprudential continuity.'") (quoting Charles H. Brower II, *Fair and Equitable Treatment Under NAFTA's Investment Chapter*, 96 AM. SOC. INT'L L. PROC. 9 (2002)); *see also* Susan D. Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions*, 73 FORDHAM L. REV. 1521, 1613 (2005) ("Tribunals are doing their utmost to review previous decisions, avoid previous mistakes, and harmonize their decisions to create a coherent body of law; nevertheless, the stakes in investment arbitration are simply too great to sit by idly while issues of public international law are being decided inconsistently, in private.").

124. *See* NAFTA, *supra* note 3, at art. 1120 (listing the bodies to which a disputing investor may submit the claim).

125. *See* ICSID Convention Rules, *supra* note 12, at Rule 3 (establishing the arbitrator appointment procedure under ICSID); *see also* UNCITRAL Arbitration Rules, *supra* note 14, art. 6–8 (discussing the appointment of arbitrators under UNCITRAL).

126. *See* NAFTA, *supra* note 3, at art. 1136 ("An award made by a Tribunal shall have no binding force except between the disputing parties and in respect of the particular case.").

127. *See* Jessica S. Wiltse, Comment, *An Investor-State Dispute Mechanism In The Free Trade Area of The Americas: Lessons From NAFTA Chapter Eleven*, 51 BUFF. L. REV. 1145, 1190 (2003) ("[T]he creation of a body to interpret and apply NAFTA law, and hear appeals from the various dispute resolution mechanisms, including Chapter 11, would provide consistency and stability to the NAFTA dispute process."); *see also* BOTTARI & WALLACH, *supra* note 1, at xviii ("NAFTA parties are subject to ad hoc rulings by an ever-changing cast of ad hoc panelists who may or may not have had any experience with NAFTA rules or prior NAFTA cases. As a result, there have been contradictory rulings on a variety of issues.").

128. *See* Joel C. Beauvais, Note, *Regulatory Expropriations Under NAFTA: Emerging Principles & Lingering Doubts*, 10 N.Y.U. ENVTL. L.J. 245, 263 (2002) ("Moreover, precedent

that there is no standing appellate body to develop an overriding body of case law exacerbates this problem.[129] One author refers to the proceedings as a "crap-shoot,"[130] and complains,

> [W]hen rule content is (or is perceived to be) largely a subjective matter, claimants may be induced to pursue fanciful theories of recovery, or to abandon plausible ones, while correspondingly, host states may be forced to defend—perhaps unsuccessfully—claims that ought not to have been brought, while escaping rigor in cases in which they might properly have been made to account.[131]

On the other hand, critics often downplay the fact that NAFTA allows for the possibility of post-award review of tribunal decisions.[132] Although there is no standing appellate body under NAFTA, parties may initiate proceedings to revise, to set aside, or to annul an arbitral award,[133] generally in a domestic court in the place of arbitration.[134] In *Metalclad v. Mexico*, for example, the Mexican Government sought to nullify the tribunal's award by filing a set-aside action in the Supreme Court of British Columbia.[135] The Court held that

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does not bind the tribunals and there is no general mechanism for appeal. Thus, any judgment might depart from previous interpretations of the agreement and of international law, exacerbating the uncertainty associated with NAFTA's already vague substantive standards.").

129. *See* Franck, *supra* note 123, at 1606–07 ("The goal of an appellate body would be to provide a public forum for the review of public disputes and create a determinate and coherent jurisprudence.").

130. Jack J. Coe, Jr., *The State of Investor-State Arbitration—Some Reflections on Professor Brower's Plea for Sensible Principles*, 20 AM. U. INT'L L. REV. 929, 946 (2005) [hereinafter Coe, *The State of Investor Arbitration*].

131. *Id.* at 946.

132. *See* BOTTARI & WALLACH, *supra* note 1, at viii (criticizing NAFTA's ad hoc tribunal system under the heading "No Appeals in NAFTA").

133. *See supra* notes 26–28 and accompanying text (discussing procedures for review of arbitral rulings).

134. *See* Jack J. Coe, Jr., *Domestic Court Control of Investment Awards: Necessary Evil or Achilles Heel Within NAFTA and the Proposed FTAA?*, 19 J. INT'L ARB. 185, 186 (2002) [hereinafter Coe, *Domestic Court Control*] ("Though anticipated by the NAFTA text, the ratifications necessary to ICSID Convention application have not been achieved among the NAFTA states. At present, therefore, requests to nullify NAFTA awards are referred exclusively to the domestic courts of the place of arbitration rather than to ICSID's annulment apparatus.").

135. *See* United Mexican States v. Metalclad Corp., 89 B.C.L.R.3d 359 (Sup. Ct. B.C. 2001) (ruling on Mexico's claim). The Supreme Court of British Columbia explained Mexico's set-aside claim as follows:

> In order to have this Court set aside the Award in its entirety, Mexico was required to successfully establish that all three of the Tribunal's findings of breaches of Articles 1105 and 1110 of the NAFTA involved decisions beyond the scope of the submission to arbitration or that the Award should be set aside in view of Metalclad's allegedly improper acts or the Tribunal's alleged failure to answer all

Mexico succeeded in challenging some of the tribunal's findings, but failed in challenging others.[136] Accordingly, the Court reduced the tribunal award, but did not entirely set it aside.[137] *Metalclad* illustrates that meaningful review is possible under NAFTA Chapter 11. While this review may not provide the stability and consistency of a standing appellate body, it does minimize the "crap-shoot" feeling of the proceedings.[138]

In addition to overstating the absence of appeals under NAFTA, critics sometimes gloss over the benefits of NAFTA's ad hoc arbitration methods. International arbitration provides a neutral forum for expeditious and efficient resolution of investment disputes.[139] Without extensive appeals, arbitral bodies can quickly dispose of claims, saving all parties time and money.[140] Furthermore, without appeals, tribunal decisions will have more authority and finality.[141] When determining whether or not to offer an extensive appellate mechanism, NAFTA drafters were forced to weigh these interests against the desire to produce a stable body of law through appellate review. The solution they came up with is not perfect, but neither is it the catastrophe some critics make it out to be.

E. Lack of Transparency

Another perceived problem with the settlement proceedings is their lack of transparency.[142] Under Chapter 11, parties must submit to arbitration through

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questions submitted to it.

Id. at ¶ 133.

136. *See id.* ("Although Mexico succeeded in challenging the first two of the Tribunal's findings of breaches of Articles 1105 and 1110, it was not successful on the remaining points.").

137. *See id.* at ¶ 133–25 (discussing the proper damage award).

138. Coe, *The State of Investor Arbitration*, *supra* note 130, at 946.

139. *See* Franck, *supra* note 123, at 1606 ("The beauty of arbitral tribunals is their ability to conduct independent, expert decision making with 'greater autonomy, control [and] efficiency' than other available mechanisms."); *see also* Beauvais, *supra* note 128, at 261–62 ("Arbitration is considerably more flexible, confidential, and economical than domestic litigation.").

140. *See* Lauren E. Godshall, Note, *In The Cold Shadow of Metalclad: The Potential for Change to NAFTA's Chapter Eleven*, 11 N.Y.U. ENVTL. L.J. 264, 311–12 (2002) (arguing that NAFTA should eliminate all appeals options).

141. *See id.* (arguing that tribunals have more authority without the possibility of appeal); *see also* Coe, *The State of Investor Arbitration*, *supra* note 130, at 952 (2005) ("Finality is in itself an interstate value to be pursued (even at the occasional cost of allowing an arguable award to stand).").

142. *See, e.g.*, BOTTARI & WALLACH, *supra* note 1, at xvi–xxii (criticizing the private nature of NAFTA arbitrations).

either ICSID or UNCITRAL.[143] Both arbitral bodies forbid publishing awards without the consent of the parties.[144] Canada or the United States "may make an award public" when they are the disputing party in the case.[145] When Mexico is the disputing party, "applicable arbitration rules apply to the publication of an award."[146] Chapter 11 does not contain a provision for public hearings.[147]

Critics find the lack of transparency under Chapter 11 alarming because NAFTA disputes tend to involve policy issues that affect the public.[148] Often, NAFTA claims implicate regulatory laws.[149] These laws are implemented by democratic bodies and are matters of public concern.[150] Hence, when a NAFTA suit threatens such a law, proceedings should be open to public scrutiny.[151] If proceedings were open, citizens would feel less detached from

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143. *See* NAFTA, *supra* note 3, at art. 1120 (listing the bodies to which a disputing investor may submit the claim).

144. *See* ICSID Additional Facility Rules, *supra* note 13, at art. 53(3) ("[T]he Secretariat shall not publish the award without the consent of the parties."); *see also* UNCITRAL Arbitration Rules, *supra* note 14, at art. 32(5) ("The award may be made public only with the consent of both parties.").

145. NAFTA, *supra* note 3, at Annex 1137.4.

146. *Id.*

147. *See* Gantz, *supra* note 44, at 747 (explaining that public hearings are excluded under NAFTA).

148. *See* BOTTARI & WALLACH, *supra* note 1, at xvi (explaining that NAFTA arbitral bodies "are dealing with significant issues of public policy").

149. *See id.* at i–v (summarizing all NAFTA claims to date, many of which challenge regulatory actions of the member-State).

150. *See* Fulvio Fracassi, *Confidentiality and NAFTA Chapter 11 Arbitrations*, 2 CHI. J. INT'L L. 213, 220 (2001) (discussing confidentiality under NAFTA Chapter 11). Fracassi distinguishes private commercial arbitrations (where confidentiality may be a legitimate goal) from NAFTA disputes (where, he argues, it is not), as follows:

> NAFTA Chapter 11 arbitrations differ from private commercial arbitrations in three fundamental ways. First, they involve claims by a party against a state that challenge sovereign acts under international law. Second, they differ from private commercial arbitrations by virtue of the far-reaching public policy ramifications that their awards may have for all NAFTA Parties. Third, these claims may have serious implications for the public purse for which governments are accountable to the people.

Id.

151. *See* Chris Ford, Comment, *What Are 'Friends' for? In NAFTA Chapter 11 Disputes, Accepting Amici Would Help Lift the Curtain of Secrecy Surrounding Investor-State Arbitrations*, 11 SW. J. L. & TRADE AM. 207, 251 (2005) ("Toward the objective of transparency, NAFTA investors should accept that documents relating their claims against governments be made public because of the far-reaching impact on public policy and the public purse.").

the dispute resolution, and the investor-state mechanism would gain legitimacy.[152]

In the past, critics have cited *Methanex Corp. v. United States*[153] as an illustration of the opaque nature of dispute resolution.[154] In *Methanex*, a Canadian investor alleged that a California ban on the sale and use of a certain gasoline additive produced by the investor constituted a violation of the minimum standard of treatment under NAFTA and rose to the level of an expropriation.[155] Because the case threatened a law affecting the health and safety of the citizens of California, those citizens had a stake in the outcome of the litigation, and, arguably, should have been allowed to participate in the process.[156]

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152. *See id.* at 251 ("The scourge of secrecy in dispute-resolution proceedings cannot help but to undermine the public trust in these arbitrations."); *see also* Coe, The State of Investor Arbitration, *supra* note 130, at 190 ("[T]his cloaking of the process lessens the already diluted accountability that attaches to independent, temporarily-appointed arbitrators whose privately deliberated damage assessments are subject only to limited review.").

153. Methanex Corp. v. United States, 44 I.L.M. 1345 (UNCITRAL 2005). In this case, Methanex, a Canadian corporation, claimed compensation from the United States resulting from a ban on the sale and use of the gasoline additive known as "MTBE" in California. *Id.* at 1345. Methanex claimed the ban violated its rights under Articles 1102, 1105, and 1110 of NAFTA Chapter 11. *Id.* at 1346. The Tribunal held that it did not have jurisdiction to decide the claims. *Id.* at 1462. Further, if it did have jurisdiction, "[t]he Tribunal would be minded to decide these issues against Methanex and in favour of the USA, on the facts of this case." *Id.*

154. *See* BOTTARI & WALLACH, *supra* note 1, at xvii (discussing the facts of Methanex in the context of transparency concerns). When Bottari and Wallach published their article, the Methanex claim was still pending. *Id.* at i. It has since been decided in favor of the United States. Methanex Corp. v. United States, 44 I.L.M. 1345, 1462 (UNCITRAL 2005).

155. *See Methanex Corp.*, 44 I.L.M. at ¶ 1–2 ("Methanex claimed compensation from the USA in the amount of approximately US $970 million . . . resulting from losses caused by the state of California's ban on the sale and use of the gasoline additive known as 'MTBE' . . . .").

156. *See* Bottari & Wallach, *supra* note 1, at xvii (explaining the problems that stem from conducting private dispute resolution outside the view of the public). Bottari & Wallach justify their concern as follows:

> Under NAFTA these tribunals are empowered to weigh the appropriateness of public policy matters such as California's rules regarding the reclamation of open-pit mines or the California law phasing out the gasoline additive MTBE, which was found to be contaminating drinking water systems throughout that state. Yet, under the investor-state system, citizens of each state must rely on federal government agencies, such as the State Department and the USTR, to defend their laws, which the latter may not support (as in the case of the California mining regulation). The residents of California cannot be party to the cases involving the health and safety of their communities and their elected guardian of state law, the California Attorney General, has no formal role.

Id.

Transparency is a valid concern, but the problem is exaggerated in the case of NAFTA. In the past five years, the NAFTA Free Trade Commission has released a series of interpretive statements regarding NAFTA's transparency problems.[157] In response to concerns about the lack of amicus curiae submissions, the commission issued a statement outlining procedures for participation by "non-disputing" parties.[158] Another statement by the Commission emphasized the possibility of public access to documents, noting that "[n]othing in the NAFTA imposes a general duty of confidentiality on the disputing parties to a Chapter 11 arbitration."[159] In practice, most, if not all, of the arbitral awards are now available to the public.[160] Finally, in 2003, the Office of the U.S. Trade Representative released a statement affirming the United States' consent for opening hearings.[161]

To summarize, critics are persuasive in their pleas for transparency but exaggerate the extent to which it is a problem under NAFTA. On one hand, transparency in judicial proceedings is a well-founded aim. It lends legitimacy to the proceeding and allows non-disputing parties who have a stake in the outcome to participate.[162] Nevertheless, in the case of NAFTA, the

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157. *See* NAFTA, *NAFTA Claims*, http://naftaclaims.com/commission.htm (last visited Sept. 13, 2006) (linking to the recent statements made by the NAFTA Free Trade Commission) (on file with the Washington and Lee Law Review).

158. *See* NAFTA Free Trade Commission, *Statement of the Free Trade Commission on Non-disputing Party Participation*, 1–2 (detailing participation in NAFTA tribunal decisions by third parties), *available at* http://www.ustr.gov/assets/Trade_Agreements/Regional/NAFTA/asset_upload_file45_3600.pdf.

159. NAFTA Free Trade Commission, *Notes of Interpretation of Certain Chapter 11 Provisions*, § A1 (2001), http://www.dfait-maeci.gc.ca/tna-nac/NAFTA-Interpr-en.asp (last visited Sept. 13, 2006) (on file with the Washington and Lee Law Review). The document explains:

> Each Party agrees to make available to the public in a timely manner all documents submitted to, or issued by, a Chapter Eleven tribunal, subject to redaction of: i. confidential business information; ii. information which is privileged or otherwise protected from disclosure under the Party's domestic law; and iii. information which the Party must withhold pursuant to the relevant arbitral rules, as applied.

Id.

160. *See* NAFTA, *Pleadings, Orders & Awards*, http://naftaclaims.com/disputes.htm (last visited Sept. 13, 2006) (providing links to legal documents from NAFTA arbitrations) (on file with the Washington and Lee Law Review); *see also* Appleton and Associates, *NAFTA Investor-State Arbitrations*, http://www.appletonlaw.com/4acases.htm (last visited Sept. 13, 2006) (linking to documents in several key NAFTA cases) (on file with the Washington and Lee Law Review).

161. Office of U.S. Trade Representative, *Statement on Open Hearings in NAFTA Chapter Eleven Arbitrations* (Oct. 7, 2003) [hereinafter Statement on Open Hearings], *available at* http://www.ustr.gov/assets/Trade_Agreements/Regional/NAFTA/asset_upload_file143_3602.pdf.

162. *See* Naveen Gurudevan, Comment, *An Evaluation of Current Legitimacy-Based*

Commission has already implemented many of the changes critics desire. Critics' purported concern about the problem is, therefore, unwarranted.

IV. Foreign Investment Under CAFTA: Chapter 10

President George W. Bush signed The Central America-Dominican Republic-United States Free Trade Agreement (CAFTA) into law on August 2, 2005.[163] The Agreement extends free trade to Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and the Dominican Republic.[164] Like NAFTA, CAFTA contains a provision that provides for investor protections and investor-state dispute resolution.[165] CAFTA's chapter 10 repeats many of the standards adopted by NAFTA (and earlier BITs).[166] Under CAFTA, investors are granted a series of basic protections: non-discriminatory treatment relative to domestic investors and investors of non-parties, limits on "performance requirements," free transfer of funds related to an investment, protection from expropriation other than in conformity with customary international law, a "minimum standard of treatment" in conformity with customary international law, and the ability to hire key managerial personnel without regard to nationality.[167] Furthermore, the chapter makes explicit that "except in rare circumstances,"[168] nondiscriminatory regulatory actions designed and applied to meet legitimate public welfare objectives, such as public health and environmental protection, will not be considered expropriatory.[169]

Objections to NAFTA's Chapter 11 Investment Dispute Resolution Process, 6 SAN DIEGO INT'L L.J. 399, 425–26 (2005) (explaining the problems that arise when arbitrations are not open).

163. *See* Press Release, White House Office of the Press Secretary, President Signs CAFTA-DR (Aug. 2, 2005), http://www.whitehouse.gov/news/releases/20050802-2.html (last visited Sept. 13, 2006) (on file with the Washington and Lee Law Review).

164. *See* United States Office of the Trade Representative, *The Dominican Republic—Central America—United States Free Trade Agreement: Summary of the Agreement*, 1 [hereinafter *CAFTA Summary*] ("This summary briefly describes key provisions . . . that the United States has concluded with Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua and the Dominican Republic."), *available at* http://www.ustr.gov/assets/Trade_Agreements/Bilateral/ CAFTA/Briefing_Book/asset_upload_file128_7284.pdf.

165. *See* CAFTA, *supra* note 2, at art. 10 (providing all investment provisions).

166. *See generally CAFTA summary*, *supra* note 164, at 12–13.

167. *See id.* at 13 (summarizing the major provisions of the investment chapter).

168. CAFTA, *supra* note 2, at annex 10-C.

169. *See CAFTA summary*, *supra* note 164, at 13 ("[N]ondiscriminatory regulatory actions designed and applied to meet legitimate public welfare objectives, such as public health and the environment, are not expropriatory.").

Chapter 10 also provides an investor-state dispute resolution mechanism. Under the provision, Parties may submit a claim for damages against another Party to binding international arbitration. Investors may claim that the Party breached a substantive obligation under the chapter or that the Party breached an investment agreement with the investor.[170] Hearings are generally public and, with the exception of confidential business information, key documents will be publicly available.[171] Amicus submissions are now expressly allowed under the chapter.[172] The dispute resolution provision also includes a clause that resembles U.S. rules for quickly disposing of frivolous claims.[173] Finally, Chapter 10 contains an annex that calls for Parties to initiate negotiations to develop an appellate body to review awards granted under tribunals within three months of the Agreement's entry into force.[174]

V. CAFTA's Response to Specific NAFTA Criticisms

The United States Office of the Trade Representative emphasizes that "the Administration . . . substantially revised the investment text used in free trade agreements . . . [i]n response to the guidance that Congress provided in the Trade Act of 2002,"[175] and that "CAFTA is thus significantly different from NAFTA."[176] This Part examines CAFTA's response to the criticisms of NAFTA. It looks at each criticism in turn, and examines the extent to which CAFTA addresses them. This Part concludes that CAFTA effectively addresses the real or perceived problems that arise under NAFTA. The improvements adopted by CAFTA, in turn, illustrate that the investor-state mechanism can adapt and become an effective mechanism for investor protection and dispute resolution.

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170. *See id.* (summarizing investor-state disputes).

171. *See id.* ("Chapter Ten requires that hearings will generally be open to the public . . . .").

172. *See id.* ("The Chapter also authorizes tribunals to accept amicus submissions from the public.").

173. *See id.* (summarizing disposal of frivolous claims).

174. *See id.* (explaining that negotiations for the appellate body to review should begin within three months).

175. CAFTA Policy Brief, *supra* note 112.

176. *Id.*

A. Greater Rights for Foreign Investors

In response to concern that foreign investors are granted greater rights than domestic investors, the drafters of CAFTA included a series of provisions designed to bring expropriation analysis under NAFTA in line with domestic takings clause law.[177] Many of these provisions are contained in Annex 10-C.[178] The Parties' agree in Annex 10-C that "[a]rticle 10.7.1 is intended to reflect customary international law concerning the obligation of States with respect to expropriation."[179] The annex next asserts that "[a]n action or a series of actions by a Party cannot constitute an expropriation unless it interferes with a tangible or intangible property right or property interest in an investment."[180] Finally, the annex explains that, when ruling on an expropriation claim, a tribunal is to consider adverse impact, the extent to which government action impacts reasonable investment-backed expectations, and the character of the government action.[181] It adds that, "[e]xcept in rare circumstances, nondiscriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations."[182]

These provisions draw on the language of the U.S. Supreme Court in its Takings Clause analysis. In *Penn Central Transportation Co. v. New York*,[183] for example, the Court emphasized that the "economic impact of the regulation on the claimant," "the extent to which the regulation has interfered with distinct investment-backed expectations," and "the character of the governmental action" are relevant inquires in the takings clause analysis.[184] This exact language is now incorporated into CAFTA Chapter 10.[185] Because CAFTA expropriations cases now require analysis similar to that required under domestic takings clause cases, disparate treatment of foreign investors should be minimal.

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177. *See, e.g.*, CAFTA, *supra* note 2, at annex 10-C(1) (noting the changes to bring CAFTA in line with takings clause analysis).

178. *See id.* (listing these provisions).

179. *Id.*

180. *Id.* at annex 10-C(2).

181. *See id.* at annex 10-C(4) (listing the factors arbitral tribunals should consider when deciding expropriation claims).

182. *Id.*

183. Penn Cent. Transp. Co. v. New York, 438 U.S. 104 (1978).

184. *Id.* at 124.

185. *See supra* notes 179–81 and accompanying text (highlighting the language in CAFTA).

B. Hindrances to U.S. Sovereignty

CAFTA attempts to minimize concerns about lost sovereignty through a series of new provisions. First, under CAFTA, governments may review draft opinions before they are issued in final form, and litigants may comment on them.[186] CAFTA also allows respondents to request an interpretation from the Free Trade Commission on issues that fall under the scope of Annexes I and II.[187] That interpretation will bind the tribunal.[188] These provisions increase government participation in the arbitration process and reduce the chances that the arbitral award will conflict with the state's legitimate regulatory powers.

As discussed above, CAFTA also includes an annex that specifically addresses some of the concerns about regulatory takings that arose under NAFTA.[189] The annex asserts that "[a]n action or a series of actions by a Party cannot constitute an expropriation unless it interferes with a tangible or intangible property right or property interest in an investment."[190] Furthermore, it notes that "[e]xcept in rare circumstances, nondiscriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations."[191] The annex also explains that "an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred."[192] Rather, the tribunal will consider adverse impact, the extent to which government action impacts reasonable investment-backed expectations, and the character of the government action.[193] These provisions recognize that the government has a right to make certain regulations, and affirms that CAFTA should not be used as a tool to attack those regulations. They will, likewise, make it more difficult

186. *See* CAFTA Policy Brief, *supra* note 112 (providing for review and comment procedure with draft opinions).

187. *See* CAFTA, *supra* note 2, at art. 10.23 ("A decision issued by the Commission under paragraph 1 shall be binding on the tribunal, and any decision or award issued by the tribunal must be consistent with that decision.").

188. *See id.* ("Where a respondent asserts as a defense that the measure alleged to be a breach is within the scope of Annex I or Annex II, the tribunal shall, on request of the respondent, request the interpretation of the Commission on the issue.").

189. *See id.* at annex 10-C (detailing the regulatory takings procedures in CAFTA and contrasting them with those in NAFTA).

190. *Id.* at annex 10-C(2).

191. *Id.* at annex 10-C(4)(b).

192. *Id.* at annex 10-C(4)(a).

193. *See* CAFTA, *supra* note 2, at annex 10-C(4)(a) (listing the factors for the tribunal to consider in ruling on whether an expropriation has occurred).

for a tribunal to find an expropriation in a situation where the government has passed a valid regulation.

Finally, as will be discussed in more detail below, CAFTA now contains a provision that allows the tribunal to dismiss frivolous claims early in the proceedings.[194] These provisions should minimize concerns that investors will use the threat of litigation to inhibit the Government from passing legislation. If the claims can be dismissed before the Government has expended too many resources, threats of litigation will not be nearly as daunting. Combined, these new CAFTA provisions should allay fears about investor attacks on U.S. sovereignty.

C. Cost to Taxpayers

When the government introduced CAFTA, fears about costs to taxpayers resurfaced.[195] In response, the drafters of CAFTA included several new provisions—based on U.S. law—in the agreement. CAFTA now contains a provision that gives tribunals the ability to dismiss unfounded claims at an early stage in the proceedings.[196] CAFTA also expressly authorizes the award of attorney's fees and costs in the case of frivolous claims.[197]

As long as the investment provision allows for investor-state lawsuits, there will always be the potential for monetary damages, but at least under the new agreement the government will not be required to expend taxpayer

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194. *See supra* notes 184–85 and accompanying text (discussing these new provisions).

195. *See* Mary Neubecker, *CAFTA Will Cost Taxpayers*, PANTAGRAPH (Bloomington, IL), July 20, 2005, at A11 ("Taxpayers will be the ones who have to pay huge subsidies for multinational corporations and Central American governments."); *see also* Miguel Bustillo, *Some Fear CAFTA Would Undermine State's Authority*, LOS ANGELES TIMES, July 18, 2005 ("The groups say the administration might again be giving foreign corporations the power to seek payment from U.S. taxpayers when regulators pass laws that diminish a company's investments.").

196. *Compare* CAFTA, *supra* note 2, at art. 10.19 ("[A] tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favor of the claimant may be made under Article 10.26.") *with* FED. R. CIV. P. 56 ("A party seeking to recover upon a claim, counterclaim, or cross-claim or to obtain a declaratory judgment may . . . move with or without supporting affidavits for a summary judgment in the party's favor upon all or any part thereof.").

197. *Compare* CAFTA, *supra* note 2, at art. 10.20 ("[T]he tribunal may, if warranted, award to the prevailing disputing party reasonable costs and attorney's fees incurred in submitting or opposing the objection. In determining whether such an award is warranted, the tribunal shall consider whether either the claimant's claim or the respondent's objection was frivolous.") *with* FED. R. CIV. P. 11 ("If warranted, the court may award to the party prevailing on the motion the reasonable expenses and attorney's fees incurred in presenting or opposing the motion.").

dollars—or at least not as often—on frivolous lawsuits. The ability to dismiss unfounded claims early on in the proceedings will save money that would be spent defending against the claims. Meanwhile, the possibility for the award of attorney's fees creates a disincentive for filing frivolous claims. If fewer claims are filed, the government will spend less money defending against them, leading to a reduction in potential damage claims. These improvements to CAFTA should reduce taxpayer fears over the costs of NAFTA litigation.

D. Absence of an Appeals Mechanism

Although NAFTA critics tend to exaggerate the problems with the lack of appeals under Chapter 11,[198] there would be benefits to creating a standing appellate body. When crafting a dispute resolution agreement, one has to balance the desire for finality and efficiency against the desire to minimize errors and inconsistency. The NAFTA drafters erred on the side of efficiency. Congress, however, moved toward consistency and predictability.[199] When Congress passed the Bipartisan Trade Promotion Authority Act[200] in 2002, it explicitly called for future trade agreements to provide an "appellate body or similar mechanism to provide coherence to interpretations of investment provisions in trade agreements."[201]

The drafters of CAFTA were somewhat responsive to Congress's mandate. CAFTA has not yet established an appellate procedure; however, the Agreement does contain an annex that illustrates the member-States' commitment to developing such a mechanism in the near future.[202] Annex 10-F specifies that "[w]ithin three months of the date of entry into force" of the Agreement, the Commission is to develop "an appellate body or similar mechanism to review awards rendered by tribunals under this Chapter."[203] It

198. *See, e.g.*, Ari Afilalo, *Meaning, Ambiguity and Legitimacy: Judicial (Re-) Construction of NAFTA Chapter 11*, 25 NW. J. INT'L L. & BUS. 279, 280 (2005) (summarizing the arguments of critics complaining about the lack of appeals).

199. *See* Coe, *The State of Investor Arbitration*, *supra* note 130, at 951 ("It seems clear given the [Trade Promotion Authority Act] Objectives' emphasis on achieving interpretive coherence that a measure of substantive review is contemplated, leading to a de-emphasis on finality in favor of jurisprudential refinement and predictability.").

200. *See* Bipartisan Trade Promotion Authority Act of 2002, Pub. L. No. 107-210, § 2102, 116 Stat. 933 (2002) (detailing trade negotiating objectives).

201. *Id.* at 995.

202. *See* CAFTA, *supra* note 2, at annex 10-F (obliging member-States to create an appellate mechanism).

203. *Id.*

also provides a series of issues that the negotiating group should consider when developing the appeals mechanism.[204] Significantly, the annex mirrors the language of the Trade Promotion Authority. It explains that "[s]uch appellate body or similar mechanism shall be designed to provide coherence to the interpretation of investment provisions in the Agreement."[205] That CAFTA uses Congress's exact language illustrates that the drafters of CAFTA listened to Congress's concerns and altered their approach to dispute resolution accordingly.

What is unclear, however, is what sort of appellate mechanism will be inserted into CAFTA.[206] Some scholars advocate the use of a single appellate body with permanent members, like the one utilized under the World Trade Organization (WTO).[207] Like Chapter 11, ad hoc dispute settlement panels decide cases under the WTO.[208] However, unlike NAFTA, parties can appeal WTO panel decisions to a fixed appellate body.[209] This appellate body, some suggest, gives a "sense of continuity and coherence to the project of developing international norms," and thereby "confer[s] legitimacy."[210] Developing a

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204. *See id.* (listing issues to consider). The annex lists the following issues as those the Commission should direct the Negotiating Group to consider:

> (a) the nature and composition of an appellate body or similar mechanism;
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> (b) the applicable scope and standard of review;
>
> (c) transparency of proceedings of an appellate body or similar mechanism;
>
> (d) the effect of decisions by an appellate body or similar mechanism;
>
> (e) the relationship of review by an appellate body or similar mechanism to the arbitral rules that may be selected under Articles 10.16 and 10.25; and
>
> (f) the relationship of review by an appellate body or similar mechanism to existing domestic laws and international law on the enforcement of arbitral awards.

Id.

205. *Id.*

206. *See* Franck, *supra* note 123, at 1607 (explaining, in the context of NAFTA, that "[t]he precise form and mandate of an appellate body leaves room for a considerable amount of debate").

207. *See Understanding the WTO: A Unique Contribution*, http://www.wto.org/english/thewto_e/whatis_e/tif_e/displ_e.htm (last visited Sept. 13, 2006) ("WTO members have agreed that if they believe fellow-members are violating trade rules, they will use the multilateral system of settling disputes instead of taking action unilaterally.") (on file with the Washington and Lee Law Review).

208. *See id.* ("The Dispute Settlement Body has the sole authority to establish 'panels' of experts to consider the case, and to accept or reject the panels' findings or the results of an appeal.").

209. *See id.* (explaining dispute resolution under the WTO).

210. Poirier, *supra* note 123, at 924–25.

similar body to hear CAFTA and NAFTA claims would provide continuity and legitimacy to the resolution mechanisms of those Agreements as well.[211]

On the other hand, CAFTA drafters might be concerned that such a body would excessively diminish the finality and efficiency of binding arbitration. The Annex calls for the development of "an appellate body *or similar mechanism*."[212] This language suggests that Congress does not believe a standing appellate body is the only option. If Congress were convinced that a standing appellate body would best resolve the issues that arose under NAFTA, presumably they would have used such language in the Act. Under the language of the TPA, the "appellate body or similar mechanism" could take any number of forms.[213]

The debate over the appellate mechanism to be utilized in CAFTA will play out over time. What is important to note now is that the drafters of CAFTA worked to resolve the issues presented by NAFTA. Whatever appellate mechanism is adopted, it should help to promote coherence and continuity under CAFTA Chapter 10.

E. Lack of Transparency

Through its Trade Negotiating Objectives, Congress demonstrated its commitment to providing transparency in investment agreements.[214] The

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211. *See* Coe, *The State of Investor Arbitration*, *supra* note 130, at 950 (discussing the possibility of a standing supranational appellate body, and noting that "such a systemic change, properly implemented, could appreciably enhance legitimacy").

212. CAFTA, *supra* note 2, at annex 10-F.

213. *See also* Franck, *supra* note 123, at 1607 (discussing suggestions for appellate bodies). The appellate mechanism could take the form of a standing appellate body, but, as Franck explains, scholars have suggested other appellate mechanisms as well:

> One commentator suggests that a NAFTA Appellate Body could be composed of Chief Justices of the Mexican, Canadian, and United States Supreme Courts. Another commentator has suggested that ad hoc arbitral tribunals be used to provide appellate review of investment arbitration awards. Others have suggested the establishment of an appellate body affiliated with a recognized international institution to provide plenary review for investment arbitration awards.

Id.

214. *See* Bipartisan Trade Promotion Authority Act of 2002, Pub. L. No. 107-210, § 2102, 116 Stat. 933, 995 (2002) (outlining the negotiating objectives of the United States regarding foreign investment). The Act states:

> [T]he principal negotiating objectives of the United States regarding foreign investment are . . . to secure for investors important rights comparable to those that would be available under United States legal principles and practice, by . . . (H) ensuring the fullest measure of transparency in the dispute settlement mechanism, to the extent consistent with the need to protect information that is

drafters of CAFTA took this commitment seriously.[215] Under CAFTA, "(a) the notice of intent; (b) the notice of arbitration; (c) pleadings, memorials, and briefs submitted to the tribunal by a disputing party . . . ; (d) minutes or transcripts of hearings of the tribunal, where available; and (e) orders, awards, and decisions of the tribunal" are all made public.[216] The hearings themselves are to be public as well (except where a disputing party intends to use protected information).[217] Finally, CAFTA expressly authorizes the submission of amicus curiae briefs.[218]

CAFTA goes a long way in opening up proceedings by addressing all of the criticisms of NAFTA (e.g. no amicus briefs, closed hearings, documents not publicly available). Critics, however, continue to complain about transparency issues in CAFTA.[219] They assert that the public is hindered from observing the arbitration because the cases are heard in distant venues.[220] They also complain that amicus opportunities are limited and that the acceptance of amicus briefs is at the discretion of the panel.[221] Finally, they are concerned that CAFTA grants exceptions for "protected information" and "confidential business information."[222] In other words, under the Agreement, certain types of information can still be kept out of the public eye.[223]

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classified or business confidential, by—

(i) ensuring that all requests for dispute settlement are promptly made public;

(ii) ensuring that

(I) all proceedings, submissions, findings, and decisions are promptly made public; and

(II) all hearings are open to the public; and

(iii) establishing a mechanism for acceptance of amicus curiae submissions from businesses, unions, and nongovernmental organizations.

Id.

215. *See* CAFTA, *supra* note 2, at art. 10.21 (establishing rules to promote transparency in arbitral proceedings).

216. *Id.* at art. 10.21(1).

217. *See id.* at art. 10.21(2) ("The tribunal shall conduct hearings open to the public . . . .").

218. *See id.* at art. 10.20(3) ("The tribunal shall have the authority to accept and consider *amicus curiae* submissions from a person or entity that is not a disputing party.").

219. *See* BOTTARI & WALLACH, *supra* note 1, at 17 (expressing concern over the lack of transparency in CAFTA tribunal proceedings).

220. *See id.* ("For citizens who can afford to travel to sometimes distant locations, tribunal hearings will now be open to the public.").

221. *See id.* ("[T]ribunals have the explicit authority to consider whether or not to accept *amicus curiae* briefs, though it is not required that they do so.").

222. *Id.*

223. *See id.* ("It remains to be seen whether this loophole will be exploited by investors in order to keep tribunal proceedings secret.").

These arguments are exaggerated. Even the harshest critics admit that the inclusion of greater transparency in CAFTA was "a victory for all those who raised these issues with Congress."[224] While the language of the Agreement does not state that the tribunal must accept amicus submissions,[225] there is no reason to imagine that it would refuse them.[226] Furthermore, while transparency is a legitimate aim, it should not be achieved at the expense of harming businesses that seek justice through CAFTA. The "protected information"[227] and "confidential business information"[228] language represents a reasonable compromise between promoting transparency and protecting businesses from forced disclosure of confidential information.

VI. Conclusion

An examination of NAFTA Chapter 11 and CAFTA Chapter 10 demonstrates that there is still a place for investor protection and citizen-state litigation in international law. Investor-state dispute resolution has a number of benefits. It creates a safe means for citizens of a member-State to invest abroad. By protecting investors, Chapter 11 and Chapter 10 increase investor confidence, which, in turn, increases foreign investment.[229] Investment then helps to promote development and increases the prosperity of member-State economies.

Critics point to a number of issues that delegitimize the investor-state dispute resolution mechanism, including favoritism towards foreign investors, impairment of sovereignty, excessive expense to taxpayers, inconsistent rulings, and hidden arbitrations. However, as this Note demonstrates, these problems are generally overstated. Investor protections and citizen-state dispute resolution are not as problematic as critics assert.

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224. *Id.*

225. *See* CAFTA, *supra* note 2, at art. 10.20(3) ("The tribunal shall have the authority to accept and consider *amicus curiae* submissions.").

226. Since NAFTA allowed the possibility of amicus submissions, two NAFTA Tribunals have accepted amicus briefs: Methanex v. United States, Decision of the Tribunal on Petitions for Third Persons to Intervene as "Amici Curiae," Jan. 15, 2001; The United Parcel Service of America, Inc. v. Canada, Decision of the Tribunal on Petitions for Intervention and Participation as Amici Curiae, Oct. 17, 2001.

227. CAFTA, *supra* note 2, at art. 10.21.

228. *Id.* at art. 10.14.

229. *See* Beauvais, *supra* note 128, at 294 ("Clearly, the investor-state mechanism under NAFTA strongly favors investor security and thus tends to encourage foreign direct investment.").

Furthermore, even if the investor-state regime under NAFTA were problematic, CAFTA illustrates that investment mechanisms are adaptable. CAFTA's modification of investor-state dispute resolution demonstrates that the enforcement scheme can overcome growing pains to become an effective mechanism in international law. With these improvements, it is increasingly apparent that the benefits of Chapter 10 outweigh its potential liabilities. Under CAFTA, investors are still granted protections and the ability to enforce those protections but without promoting favoritism, hindering sovereignty, or bankrupting taxpayers. CAFTA resolutions are open and will eventually contain an appellate provision that will add a new level of stability and consistency to rulings. Because the effects of the investor-state mechanism are mainly beneficial, this Note concludes that the extension of investor protections and citizen-state dispute resolution into Trade Agreements was a positive development in international law.