Law and Business Review of the Americas

Volume 8 | Number 1 Article 12

2002

An Examination of Investor-State Dispute Resolution under the MERCOSUR and NAFTA Regimes

Michael Cornell Dypski

An Examination of Investor-State Dispute Resolution under the MERCOSUR and NAFTA Regimes

*Michael Cornell Dypski**

Table of Contents

I. Introduction

Since the late 1980s and the end of the Cold War, the negotiation of regional trade agreements (RTAs) has become one of the favorite pastimes of economists, policymakers, and international lawyers throughout the Western Hemisphere.[1] The rationale behind such organizations is understandable. Founded on the theory of comparative advantage, which pervades arguments in favor of RTAs, "if each country sticks to what it does best... and imports everything else it needs, everyone will be better off."[2] In general, governments acceding to RTAs reduce or eliminate tariffs and quotas among the

* The author, a member of the Maryland and District of Columbia Bars, holds a B.A. in political science from Saint Mary's College of Maryland, an M.A. in International Affairs from The Elliott School of International Affairs at The George Washington University, and a J.D. from The University of Baltimore School of Law. He currently is pursuing an LL.M. in International and Comparative Law at The Georgetown University Law Center.

1. Duncan Green, Silent Revolution: The Rise Of Market Economics In Latin America 141 (1995). Mr. Green asserts: "Everybody's doing it." *Id.* As Mr. Green points out, by the mid-1990s, Latin American states were involved with at least twenty-two bilateral accords and sub-regional pacts. *Id.* These regional agreements take the form of either preferential arrangements (e.g., the Andean Trade Preference Act, the Caribbean Basin Initiative), reciprocal arrangements (e.g., Latin American Integration Association), free trade agreements (e.g., NAFTA), or common markets (e.g., Andean Pact, Caribbean Community, MERCOSUR). *See* Nora Lustig & C.A. Primo Braga, *The Future of Trade Policy in Latin America, in* Integrating The Americas: Shaping Future Trade Policy 31–38 (Sidney Weintraub ed., 1994).
2. Green, *supra* note 1, at 141.

signatories, and may eventually lead to a customs union and free trade area. In the former, tariffs and quotas among the member states are reduced or eliminated; a common external tariff is charged to parties outside of the agreement region, labor and capital move about more freely, and, in some instances, as in the European Union, a common currency is utilized.[3] A free trade area is a system in which, as in a customs union, members reduce or abolish quantitative restrictions and tariffs on imports between the party states. Individually, however, the party states may maintain such protective measures against nonassociated countries (i.e., no common external tariff).[4]

Beyond these lofty, liberal notions of freer trade, harmonization, and commonality, economic realism appears to have become the true driving force behind RTAs in the

3. *Id.* Of course, regional trade agreements in the Americas did not emerge only at the dawn of the 1990s. "The integration or union of several countries is not a new concept in Latin America. After the various countries achieved independence, attempts were made in this direction, although mainly politically motivated." VICTOR L. URQUIDI, FREE TRADE AND ECONOMIC INTEGRATION IN LATIN AMERICA 20 (Marjory M. Urquidi trans., 1964). Before, during, and after World War II, blocs were considered throughout the Americas either on a regional or pan-American basis. *Id.* at 20–21.

While not of direct concern to this paper, the author would be remiss to neglect the dynamic between the development of RTAs and member state obligations under the World Trade Organization (WTO). On their face, most RTAs violate the nondiscrimination principles of the General Agreement on Tariffs and Trade (GATT), because these arrangements allow members of an RTA to afford better treatment to each other than to non-member states. An exception to this rule has been carved out in GATT Article XXIV. *See* JOHN H. JACKSON ET AL., DOCUMENTS SUPPLEMENT TO LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS 47–50 (3rd ed. 1995). Under Article XXIV, states are permitted to depart from the nondiscrimination principle through the formation of either a customs union (CU) or free trade area (FTA). Under Article XXIV(5)(a) and 5(b), respectively, members of a CU or FTA may not raise trade barriers to non-parties higher than those existing at the creation of the RTA. *See* Robert Hudec & James D. Southwick, *Regionalism and WTO Rules: Problems in the Fine Art of Discriminating Fairly*, *in* TRADE RULES IN THE MAKING: CHALLENGES IN REGIONAL AND MULTILATERAL NEGOTIATIONS 50 (Miguel Rodriguez Mendoza et al. eds., 1999).

However, NAFTA, MERCOSUR, and most RTAs in force currently remain in a "legally ambiguous situation." Sergio Lopez-Ayllon, *Beyond the Summit of the Americas II: Prospects for FTAA and Future Western Hemisphere Integration*, NAFTA: L. & BUS. REV. AM. 241, 246 (1999). Although NAFTA Articles 101 and 103 affirm its consistency with, and obligations to, the GATT, ambiguity remains, in part, because of variations in sectoral breadth and treatment relations between the GATT and NAFTA members.

In contrast, MERCOSUR documents "do not mention the GATT, or how the regional economic arrangement relates to it." Cherie O'Neal Taylor, *Dispute Resolution as a Catalyst for Economic Integration and an Agent for Deepening Integration: NAFTA and MERCOSUR?* 17 NW. J. INT'L L. & BUS. 850, 889 (1996–1997). In 1992, the states of MERCOSUR presented the Treaty of Asunción before the GATT, to affirm its existence and compliance with GATT rules. The Committee on Trade and Development affirmed MERCOSUR's status as an RTA under the GATT rules of Article XXIV and section 2(c) of the "enabling clause," permitting special treatment for developing countries. *See* Adrian Makuc, *Multilateral Trading System and Regional Integration*, 13 FLA. J. INTL L. 59, 61 (2000); *Regionalism: the Enabling Clause*, *available at* www.wto.org/english/tratop_e/region_e/regenb_e.htm

4. José Manuel Salazar-Xirinachs et al., *Customs Unions*, *in* TOWARD FREE TRADE IN THE AMERICAS 45 (José Manuel Salazar-Xirinachs & Maryse Robert eds., 2001).

Western Hemisphere after the demise of the Soviet Union, communism, and the bipolar dynamic. Greater input of investment, whether regional, extra-regional, or national, came to the fore as a fundamental concern for leaders, particularly in Latin America. The "greatest concern that the end of the Cold War generated in Latin America was fundamentally economic. . . . The larger countries feared that private credit and investment flows would be diverted. . . to the new capitalism of Eastern Europe."[5] Therefore, investment flow, and the disputes that can arise from this input were, and continue to be, of great effect both to the nations of the Western Hemisphere on individual bases, as well as to the overall survival of the various RTAs in existence. Two such RTAs, while nascent during the Cold War, but solidified by the early and mid-1990s, are the Common Market of the South (MERCOSUR) and the North American Free Trade Agreement (NAFTA).[6]

The purpose of this paper is to examine the investor-state dispute settlement mechanisms of the MERCOSUR and NAFTA systems.

First, this paper will provide brief, cursory histories of the creation and aspirations of MERCOSUR and NAFTA. Part 2 will discuss and analyze the treaty provisions relevant to investor-state dispute resolutions under these regimes. Finally, this paper will conclude with the author's central argument that from the treaty provisions of MERCOSUR and NAFTA, while both imperfect, the latter promotes a paradigm the former should attempt to emulate. While the leaders of Argentina, Brazil, Paraguay, and Uruguay seek investment, internal political and financial strife may, at least to this author, provide a catalyst for further withdrawal. A return to nationalism, greater attention to import-substitution industrialization, and movement away from extra-regional trade will further dissuade investment and promote further economic deterioration.

II. Historical Background

A. Common Market of the South

While efforts at regional economic integration are not a new phenomenon in Latin America, early "incarnations were largely dysfunctional," as was the case with the Latin

5. Jorge G. Castañeda, *Latin America and the End of the Cold War: An Essay in Frustration, in* Latin America In A New World 40 (Abraham F. Lowental & Gregory F. Treverton eds., 1994). As one Argentine student is quoted as saying: "What role can Latin America play on the global stage as the bipolar world comes to an end, and the Eastern bloc emerges as a fabulous opportunity for investment, as the United States looks East and Europe looks East?" *Id.* In the early and mid-1990s, President Salinas de Gortari of Mexico, and President Collor de Mello of Brazil were strongly motivated by this fear of investment transfer from the South to the former Warsaw Pact. *Id.* "Salinas, for example, justified his changed stance on a free trade agreement with the United States, and his efforts to seek such an agreement precisely because funding from Europe was no longer available as a result of the transformation of the Eastern European economies." *Id.*

6. Interestingly, while the conclusion of a Multilateral Agreement on Investment (MAI) "remains elusive. . . bilateral and regional agreements. . . have proliferated in all regions of the world, not only between developed and developing countries [e.g., NAFTA]. . . but now also between developing countries [e.g. MERCOSUR]." Riyaz Dattu, *A Journey from Havana to Paris: The Fifty-Year Quest for the Elusive Multilateral Agreement on Investment*, 24 Fordham Int'l L.J. 275, 275 & 277 (2000).

American Free Trade Association (LAFTA).[7] By the mid-1980s, however, the Southern Cone[8] experienced a sea change towards cooperation in a region beleaguered by military dictatorship, protectionism, hyperinflation, and border disputes.[9] In 1986, Argentina and Brazil signed the Program for Integration and Economic Cooperation (PICE), an agreement comprising of twenty-four sectors covering trade, most notably in capital goods, automobiles, and wheat.[10] Two years after PICE was enacted, the two giants signed a new treaty aimed at creating a common market.[11] "This agreement between the two most important countries in Latin America was the real catalyst which lead to the creation of MERCOSUR."[12]

Hence, on 26 March 1991, the leaders of Argentina, Brazil, Paraguay, and Uruguay signed the Treaty of Asunción, thereby setting forth a process to establish a "common market in the Southern Cone" by the last day of December 1994.[13] By 1 January 1995, "the fundamental elements of a common market were achieved" by MERCOSUR, in that a common external tariff and reductions of internal tariffs were implemented.[14] The Treaty of Asunción and the inchoate MERCOSUR regime promulgated a system of "flexibility and simplicity."[15] Initially, the Member States of MERCOSUR "refrained from

---

7. SIDNEY WEINTRAUB, DEVELOPMENT AND DEMOCRACY IN THE SOUTHERN CONE: IMPERATIVES FOR U.S. POLICY IN SOUTH AMERICA 2 (2000).
8. *See* G. POPE ATKINS, LATIN AMERICA IN THE INTERNATIONAL POLITICAL SYSTEM 32–34 (3rd ed. 1995). Mr. Atkins provides an interesting survey of the political international subsystems present in South America, contrasting that of the Caribbean states (i.e., Colombia, Guyana, Suriname, and Venezuela) and the Southern Cone (i.e., Argentina, Bolivia, Brazil, Chile, Ecuador, Paraguay, Peru, and Uruguay).
9. Peter Coffey, *The Historical Background to Integration in Latin America, in* LATIN AMERICA—MERCOSUR 4–6 (Peter Coffey ed., 1998).
10. *Id.* at 6.
11. *Id.*
12. *Id.* Mr. Coffey asserts that it was "both logical and simple" for Argentina and Brazil to promote the common market integration scheme further by including Paraguay and Uruguay.
13. Treaty of Asunción, Mar. 26, 1991, art. 1, 30 I.L.M. 1041, 1044 (). Chile and Bolivia hold associate member status in MERCOSUR. The former joined in 1996, the latter in 1997. Salazar-Xirinachs et al., *supra* note 4, at 77.

    The central goal of the MERCOSUR regime, member state integration, is to be achieved through: (1) the free movement of goods, services, and factors of production by the elimination of customs duties, non-tariff barriers, and other restrictive measures; (2) the establishment of a common external tariff, adoption of common policies in relationship to third party states, and overall economic and commercial coordination; (3) macroeconomic and sectoral policy coordination in areas such as foreign trade, agriculture, industry, fiscal and monetary matters; foreign exchange and capital, services, customs, transport, and communications; and (4) overall legislative harmonization to further the integration process. *See* Treaty of Asunción, *supra* note 13, at 1045; Jorge Lucángeli, *Argentina and the Challenge of Mercosur, in* LATIN AMERICA—MERCOSUR, *supra* note 9, at 22–23. Article 15 of the Treaty of Asunción states that MERCOSUR headquarters is to be located in Montevideo, Uruguay. Treaty of Asunción, *supra* note 13, at 1048.
14. Malcolm Rowat et al., *Competition Policy and MERCOSUR*, xviii World Bank Technical Paper No. 385 (1997).
15. Miguel Rodriguez Mendoza, *Dealing with Latin America's New Regionalism, in* TRADE RULES IN THE MAKING, *supra* note 3, at 84.

creating supranational institutions to guide the process."[16] Hence, at the institutional level, the Treaty of Asunción itself is fairly shallow. The treaty established the Council of the Common Market, the supreme organ of the common market, responsible for the political leadership and the compliance decision-making of the organization,[17] as well as the Common Market Group, the executive organ of MERCOSUR, which has the "powers of initiative"[18] and "oversees the implementation of the agreement."[19]

The MERCOSUR regime required much needed depth, both institutionally and structurally. This was accomplished through the Protocol of Ouro Preto, signed on 17 December 1994.[20] Under this Protocol, MERCOSUR achieved a further adjustment aimed at greater integration into the world economy.[21] MERCOSUR became endowed with a legal status, empowering it to negotiate on an international level.[22] Ouro Preto, in addition to reaffirming the role of the Common Market Group and the Council, created bodies including the MERCOSUR Trade Commission, the Joint Parliamentary Commission, the Economic-Social Consultative Forum, and the MERCOSUR Administrative

16. *Id.*
17. The Treaty of Asunción, *supra* note 13, at arts. 9 & 10. The Council of the Common Market is to consist of the Ministers of Foreign Affairs and the Ministers of Economy of the member states. *Id.* art. 11.
18. *Id.* art. 13. The CMG is to monitor compliance with the Treaty of Asunción, enforce the decision of the Council of the Common Market, and further ensure the liberalization and overall functioning of MERCOSUR. *Id.* The CMG is to consist of four members and four alternates for each member state representing the Ministry of Foreign Affairs, the Ministry of Economy or its equivalent, and the Central Bank. *Id.* art. 14.
19. Salazar-Xirinachs, *supra* note 4, at 79. The Treaty of Asunción also contains five annexes. Treaty of Asunción, *supra* note 13, at 1050–1061. In order, these annexes deal with trade liberalization/tariff reduction, rules of origin, dispute settlement, safeguards, and working groups. *Id.* Of specific concern to this paper is Annex III, dealing with dispute settlement. The Treaty of Asunción calls for the settlement of disputes by direct negotiations, with CMG and Council consultation if necessary. The members of MERCOSUR were to establish a permanent system of dispute resolution by 31 December 1994, the birth of the common market. *Id.* at 1059. This was accomplished to an extent on 17 December 1991 with the Protocol of Brasilia for the Settlement of Disputes. Protocol of Brasilia for the Settlement of Disputes, Dec. 17, 1991, 36 I.L.M. 691 [hereinafter Protocol of Brasilia]. The Protocol of Brasilia, which went into effect in April 1993, deals only with disputes between MERCOSUR states (government-to-government) and private parties and a MERCOSUR state (private-to-government). Nadia de Araujo, *Dispute Resolution in Mercosul: The Protocol of Las Leñas and the Case Law of the Brazilian Supreme Court*, 32 U. MIAMI INTER-AM. L. REV. 25, 36 (2001). As will be mentioned further in Part II of this paper, the Protocol of Brasilia plays an integral role in certain aspects of the MERCOSUR investment instruments, the Protocol of Colonia and the Protocol of Buenos Aires.

    As one writer points out: "The MERCOSUR has not yet established a permanent dispute settlement system... The Brasilia Protocol... established a dispute settlement system that was to remain in force until the permanent dispute system for the common market was set up." Taylor, *supra* note 3, at 859–860; *see* Protocol of Ouro Preto, Dec. 17, 1994, art. 44, 34 I.L.M. 1244, 1257 [hereinafter Protocol of Ouro Preto].
20. Protocol of Ouro Preto, *supra* note 19, at 1258.
21. WEINTRAUB, *supra* note 7, at 9.
22. Coffey, *supra* note 9, at 11; Protocol of Ouro Preto, *supra* note 19, at art. 8(III–IV).

Secretariat.[23] The Council, the Common Market Group, and the MERCOSUR Trade Commission are the three intergovernmental organs with decision-making authority.[24]

Therefore by the end of 1994, at the dawn of the official genesis of MERCOSUR, the governments of Argentina, Brazil, Paraguay, and Uruguay, had established the foundation for a viable, functioning organization through the "key MERCOSUR agreements" of the Treaty of Asunción and the Protocol of Ouro Preto.[25] While a "complete customs union" was not achieved by 1995, a common external tariff was implemented, while most other tariffs had been eliminated by the end of 1994.[26]

In recent years, MERCOSUR, "gradually moving towards becoming completely operational as a full free trade area,"[27] has been successful, despite recent economic and

23. Protocol of Ouro Preto, *supra* note 19, art. 1.

24. Salazar-Xirinachs, *supra* note 4, at 79; Protocol of Ouro Preto, *supra* note 19, art. 2. The Protocol of Ouro Preto further defined the roles of the Council and the CMG. Article 8 of the Protocol details the duties and functions of the Council. Its main purpose is to promote the development of the common market and to act of behalf of MERCOSUR in international settings. As the supreme body of MERCOSUR, decisions of the Council are binding on all member states, under Article 9 of the Protocol. *Id.* art. 9.

    The CMG acts on behalf of the Council's mandate. Its purpose is threefold: (1) to ensure that the Treaty of Asunción and all its ancillary protocols and agreements are respected by the member states; (2) to ensure progress towards a common market through the creation of work programs; and (3) to negotiate, at the Council's direction, with member countries, third countries, and international institutions. Protocol of Ouro Preto, *supra* note 19, art. 14. The decisions of the CMG called Resolutions are binding on all member states. *Id.* art 15. *See also* Salazar-Xirinachs, *supra* note 4, at 80.

    The newly created MERCOSUR Trade Commission is to monitor the application of the common trade policy instruments of MERCOSUR in the overall operation and functioning of the common market. Protocol of Ouro Preto, *supra* note 19, arts. 16 & 19. Directives of the MTC are binding on all the member states. *Id.* art. 20.

    It must be pointed out that the "binding" decisions of the Council, CMG, and MTC must be ratified and incorporated into the domestic legal system of each state. *Id.* arts. 38–40. "None of the MERCOSUR countries are monist states—states which allow international law to be incorporated without the need for domestic legislative action." Taylor, *supra* note 3, at n.98.

    December 1994 saw not only the strengthening and reaffirmation of the MERCOSUR system through the Protocol, multiple decisions were approved by the member states at Ouro Preto. These decisions included principles of global banking supervision, standardization of information for the stock market, transportation of hazardous materials, agreement on transportation system between the MERCOSUR states, application of customs norms, intellectual property agreements, sugar sector rules, anti-competition distortion policies, a common external tariff, harmonization of tariff criteria, and a common automotive regimen. MASAAKI KOTABE, MERCOSUR AND BEYOND: THE IMMINENT EMERGENCE OF THE SOUTH AMERICAN MARKETS 40–41 (1996).

25. WEINTRAUB, *supra* note 7, at 9.

26. Salazar-Xirinachs, *supra* note 4, at 82.

27. *Latin America and the Caribbean in the World Economy*, U.N. Economic Commission for Latin America and the Caribbean 122 (1999). MERCOSUR "made significant progress toward a free trade area in a brief period of time, and intraregional trade flows experienced a significant rise." Roberto Bouzas, *Regional Trade Arrangements: Lessons from Past Experiences*, *in* TRADE RULES IN THE MAKING, *supra* note 3, at 192.

political crises.[28] Evidence of this is the phenomenal increase in intra-regional trade and input of foreign investment in the MERCOSUR states following its creation.[29] While the economic performance of MERCOSUR has slumped in recent years, the overall achievements of this "integration scheme in the areas of trade, investment, and interaction between the production structures of member countries have been substantial."[30]

B. North American Free Trade Agreement

"The Parties to this Agreement... hereby establish a free trade area."[31] With these words, the North American Free Trade Agreement between Canada, Mexico, and the

28. This has been most notable in the executive and monetary crises gripping Argentina. *See* The Economist, 12 Jan. 2002, at 13 & 34; Manuel Pastor & Carol Wise, *From Poster Child to Basket Case*, Foreign Affairs, Nov. 1, 2001, at 60.

    By 2000, MERCOSUR had established itself as "the third wealthiest regional trading organization in the world", surpassed only by the European Union and NAFTA. Jorge Guira, *MERCOSUR: The Emergence of a Working System of Dispute Resolution*, 6 NAFTA: L. & Bus. Rev. Am. 255, 255 (2000).

29. Total exports by Argentina, Brazil, Paraguay, and Uruguay grew from $34.8 billion in 1985 to almost $75 billion in 1999. Karsten Steinfatt & Patricio Contreras, *Trade and Investment Flows in the Americas*, *in* Toward Free Trade In The Americas, *supra* note 4, at 22. Import data also indicate "the high degree of interdependence among MERCOSUR member countries." *Id.* at 25. In 1999, 20 percent of total imports were intra-regional (intra-MERCOSUR), double the amount from 1985. *Id.* This data reflects MERCOSUR's commitment to the promotion of "economics of complementarity... based on their respective comparative advantage." Kotabe, *supra* note 24, at 27.

    From 1990 to 1995, foreign direct investment from the European Union, Japan, and the United States to MERCOSUR increased from $2.3 billion to $10.88 billion. Foreign Direct Investment In Latin America: Perspectives Of The Major Investors 271 (The Inter-American Development Bank & The Institute for European-Latin American Relations, 1998). However, overall inability to compete internationally, increased flows to Mexico, burgeoning global economic malaise, as well as domestic woes, reflect a, hopefully, reversible drop in *overall* FDI to MERCOSUR from 1999 to 2000. Argentina saw a drop of FDI from $23.5 billion to $11.9 billion; FDI to Brazil fell from $32.65 billion to $30.25 billion; FDI to Paraguay interestingly increased from $95 million in 1999 to $100 million in 2000. This was a decrease, however, from $196 million in 1998. Uruguay experienced a decrease from $229 million in 1999 to $180 million in 2000. *Foreign Investment in Latin America and the Caribbean*, U.N. Economic Commission for Latin America and the Caribbean 39 (2001).

30. *Latin America and the Caribbean in the World Economy*, *supra* note 27, at 121. The U.N. points out further that under the MERCOSUR system, there has been an increase by civil society in participation in the sub-regional integration process, and expanded links between municipal and provincial leaders, professional, and labor organizations, and employers' associations. *Id.*

31. The North American Free Trade Agreement, Dec. 17, 1992, art. 101; 32 I.L.M. 289, 297 [hereinafter NAFTA]. NAFTA is the culmination of nearly a decade's progress towards the "establishment of the first [preferential trade arrangement] between developed and developing countries." Roberto Bouzas, *supra* note 27, at 187.

    In 1985, Canada began to seek freer trade with her larger southern neighbor. Maryse Robert, *Free Trade Agreement*, *in* Toward Free Trade In The Americas, *supra* note 4, at 88. Eventually, on 1 January 1989, the Canada-U.S. Free Trade Agreement entered into force and eliminated trade barriers between the two countries, as well as loosening restrictions

United States was born on 1 January 1994.[32] Basically, the goal of NAFTA is to provide for the "progressive elimination of all tariffs and other barriers to trade on goods qualifying as North American."[33] By 1 July 1997, Canada, Mexico, and the United States implemented the first round of accelerated tariff elimination,[34] followed on 1 August 1998, with the implementation of a second round of further tariff reductions, covering around $1 billion in trade.[35] Tariff elimination on a number of goods continued and took effect on 1 January 2001.[36] These eliminations will continue to occur for more sensitive items, such as agricultural products and textiles, throughout the first decade of this century.[37]

---

in services and investment. *Id.* In 1986, Mexico joined GATT, and by 1990 approached the United States in regards to free trade area negotiations. *Id.* at 89.

Both Canada and Mexico entered into negotiations for a free trade area with the United States for varied reasons. Roberto Bouzas, *supra* note 27, at 188. For Canada, the dominant objective was to guarantee more stable access to the U.S. market by limiting U.S. discretion in the implementation of trade remedy laws, and by protecting Canadian exports from future increases in U.S. protection. [As discussed earlier in this paper], Mexico was also interested in increasing its attractiveness to foreign investors, as well as in buying credibility for, and locking in, domestic reform policies." *Id.*

32. NAFTA, *supra* note 31, art. 2203. The actual NAFTA text "is a massive document of thousands of pages. . . . Consequently, the agreement is not an easy read. NAFTA is sure to keep many lawyers. . . gainfully occupied for years making interpretations that will have modest social welfare benefits." Sidney Weintraub, *The North American Free Trade Agreement as Negotiated: A U.S. Perspective, in* ASSESSING NAFTA: A TRINATIONAL ANALYSIS 1 (Steven Globerman & Michael Walker, eds., 1993).

NAFTA is a dramatically more complex, integrated, and structured regime than MERCOSUR. To delve into NAFTA beyond a cursory fashion, would be venturing into an amount of detail well beyond the scope of this paper. The aim of this paper is far more modest.

33. Robert, *supra* note 31, at 89. Under Article 102 of NAFTA:

> The objectives of this Agreement, as elaborated more specifically through its principles and rules, including national treatment, most-favored nation treatment, and transparency, are to: (a) eliminate barriers to trade in, and facilitate the cross border movement of, goods and services between the territories of the Parties; (b) promote conditions of fair competition in the free trade area; (c) increase substantially investment opportunities in the territories of the Parties; (d) provide adequate and effective protection and enforcement of intellectual property rights in each Party's territory; (e) create effective procedures for the implementation and application of this Agreement, for its joint administration and for the resolution of disputes; and (f) establish a framework for further trilateral, regional, and multilateral cooperation to expand and enhance the benefits of this Agreement.

NAFTA, *supra* note 31, art. 102.

34. Robert, *supra* note 31, at 89.
35. *Id.*
36. *Id.*
37. *See* Eric Barry & Elizabeth Siwicki, *NAFTA: The Textile and Apparel Sector, in* ASSESSING NAFTA: A TRINATIONAL ANALYSIS, *supra* note 32, at 145; Thomas Grennes, *Toward a More Open Agriculture in North America, in* ASSESSING NAFTA: A TRINATIONAL ANALYSIS, *supra* note 32, at 150.

The "central institution"[38] of NAFTA is the Free Trade Commission (FTC), which supervises the implementation of the agreement, attempts to resolve disputes, oversees the operation of all relevant committees and working groups, and aims to ensure the overall functioning of the NAFTA system.[39] Ancillary to the FTC is the Secretariat, which maintains an office in each member state[40] and administers the dispute settlement provisions under the chapters dealing with financial services, anti-dumping/countervailing duties, and certain investment provisions.[41] Additionally, each national section of the Secretariat maintains a "'court-like' registry" relating to NAFTA proceedings and assists the FTC when called upon to do so.[42]

Currently, NAFTA is one of the most "closely integrated areas in the world, as evidenced by the high level of trade among its three members."[43] In 1999, intra-NAFTA exports accounted for over 50 percent of total exports within the troika, up from 42 percent in 1986.[44] Imports from Canada and Mexico accounted for about 30 percent of imports to the United States.[45] In contrast, NAFTA imports accounted for 70 percent of total imports to Canada and 75 percent of total imports to Mexico.[46]

Concerning investment, NAFTA has produced a significant impact on its members, most dramatically in Mexico and its maquila manufacturing centers.[47] In fact, between 1995 and 2000, more than 60 percent of overall foreign direct investment was aimed at the Mexican manufacturing sectors,[48] with investment from the United States accounting for over 65 percent of that total.[49]

38. Robert, *supra* note 31, at 93.
39. NAFTA, *supra* note 31, art. 2001. The FTC is to be comprised of cabinet-level representatives from Canada, Mexico, and the United States. *Id.* at art. 2001(1). Key issues addressed by these committees and working groups include trade in goods, rules of origin, customs, agricultural trade and subsidies, investment, movement of business people, and government procurement. Robert, *supra* note 31, at 94.
40. NAFTA, *supra* note 31, art. 2002.
41. Robert, *supra* note 31, at 94.
42. *Id.*
43. Steinfatt, *supra* note 29, at 27. It should be noted that while NAFTA is becoming more entrenched within the trade framework of its three members, it pales in its integration level compared to the European Union. Unlike the EU, the "institutional apparatus of the NAFTA is fairly small and inter-governmental in nature." *Latin America and the Caribbean in the World Economy*, *supra* note 27, at 40.
44. Steinfatt, *supra* note 29, at 27.
45. *Id.* at 28.
46. *Id.*
47. *Foreign Investment in Latin America and the Caribbean*, *supra* note 29, at 38. The U.N. points out that:

> the presence and operation of many [multinational corporations] in the country [ie., Mexico] today is... in great measure a result of the integration schemes established with the rest of the subregion, especially in the North American Free Trade Agreement (NAFTA) with the United States... [The] NAFTA framework has encouraged certain types of investment which other countries of the region do not receive.

Id.
48. *Id.*
49. *Id.*

It is the lure of investment rewards that has been the ultimate catalyst for investor-state disputes and will be of focus in the next section of this paper.

III. Investor-State Dispute Resolution Mechanisms

A. Common Market of the South

In the area of investment disputes MERCOSUR has created, as one author notes, an "excellent system which will ensure free competition in the region."[50] Under the Protocol of Colonia for the Promotion and Reciprocal Protection of Investments in MERCOSUR ("Protocol of Colonia"), signed 17 January 1994,[51] and the Protocol on Promotion and Protection of Investments Coming from Non-MERCOSUR State Parties ("Protocol of Buenos Aires"), of 5 August 1994[52] both inter-regional and third state investors acquire access to the regime's dispute settlement mechanisms.[53]

The preamble to the Protocol of Colonia recognizes the mutually beneficial contribution investment provides to the overall well being and functioning of MERCOSUR.[54]

---

50. Row at *supra* note 14, at 102. The author of this paper believes that this statement may be somewhat overly optimistic.
51. The Protocol of Colonia for the Promotion and Reciprocal Protection of Investments in MERCOSUR, Jan. 17, 1994, [hereinafter Protocol of Colonia], *available at* http://www.cvm.gov.br/ingl/inter/mercosul/coloni-e.asp (last visited Feb. 7, 2002).
52. The Protocol on Promotion of Investments Coming from Non-MERCOSUR State Parties, Aug. 5, 1994, [hereinafter Protocol of Buenos Aires], *available at* http://www.sice.oas.org/trade/mrcsrs/decisions/an1194e.asp (last visited Feb. 7, 2002).
53. "Intra-MERCOSUR foreign investment is governed by the Protocol of Colonia... Non-member country investment is controlled by the Protocol on Foreign Investment [Protocol of Buenos Aires]." David M. Gilmore, *Free Trade Area of the Americas: Is it Desirable?* 31 U. Miami Inter-Am. L. Rev. 383, 400–01 (2000).
54. The Protocol of Colonia, *supra* note 51, preamble. The Protocol states:

> Convinced that the creation of favorable conditions for the investment of investors of one of the Contractor parties in the territory of another Contracting Party will intensify the economic cooperation, and will speed up the process of integration between the four countries; Recognizing that the promotion and protection of such investments based on an agreement will contribute to stimulate the individual economic initiative and will increase the prosperity in the four States.

Articles 1 and 2 provide definitions of "investment" and "investors," respectively. The Protocol goes on to prescribe that investments from others members states be afforded treatment "not less favorable" than those investments from domestic or third state investors (arts. 2 & 3). The Protocol also prohibits performance requirements (art. 3(4)), allows for compensation in cases of expropriation (art. 4), guarantees the repatriation and transfer of monies (art. 5), and reaffirms the dispute resolution system under the auspices of the Protocol of Brasilia for state-to-state disputes (art. 8). *See also* Salazar-Xirinachs, *supra* note 4, at 80.

In regards to national treatment, the member states asserted numerous exceptions. Sectors include real estate in border areas, air transportation, shipbuilding, uranium mining, fishing (Argentina); mineral mining, hydraulic energy, health care, telecommunications, leasing of rural property, shipping (Brazil); real estate in border areas, telecommunications, electricity, water and telephone services, postal services, petroleum importation (Paraguay); and

Intra-regional investor-state disputes are covered under Article 9 of the Protocol.[55] Initially, all controversies between investors of a MERCOSUR party and a MERCOSUR state itself are to be "settled by friendly consultations."[56] If negotiations between the investor and the state have proved fruitless after six months, the investor is afforded three options.[57] The investor may submit his/her claim to (1) the national courts of the MERCOSUR member where the investment took place; (2) international arbitration; or

---

electricity, hydrocarbon, atomic energy, railroads, petrochemicals, audiovisual instruments (Uruguay).

55. Protocol of Colonia, *supra* note 51, art. 9. As mentioned earlier in this paper, *supra* note 19, the Protocol of Brasilia is to be applied in certain aspects of the MERCOSUR investment dispute settlement systems. Under article 8 of the Protocol of Colonia, controversies arising between member states relating to the application or interpretation of this agreement, must submit their claims under the rules of the Protocol of Brasilia.

Under the Protocol of Brasilia, disputes are to be settled amicably through direct negotiations between the states. *See* Protocol of Brasilia, *supra* note 19, art. 2. If the dispute is not settled within fifteen days, *id.* art. 3(2), the state parties submit their complaints to the Common Market Group. *Id.* art. 4(1). If the CMG is unsuccessful in reaching a decision within thirty days, *id.* art. 6, the matter is sent to a three-person, *id.* art. 9(1), arbitration proceedings. *Id.* art. 7(1). The arbitration panel is then given up to ninety days to enter an award. *Id.* art. 20. The arbitration awards are final and nonappealable. *Id.* art. 21(1). If the losing state party is not compliant with the panel's decision, the other state parties to the dispute may implement temporary compensatory measures. *Id.* art. 22(2); *see also* Thomas Andrew O'Keefe, *An Assessment of MERCOSUR'S Present Legal Framework and Institutions and How They Affect MERCOSUR'S Chances of Success*, 6 AUT INT'L PRACTICUM 14, 16 (1993).

Under the Protocol of Brasilia, all dispute matters are to be handled on the governmental level. *See* Treaty of Asunción, *supra* note 13, Annex III, para. 1; Protocol of Brasilia, *supra* note 19, arts. 25–32. However, "in the case of foreign investment claims under the Colonia Protocol or the Foreign Investment Protocol [Protocol of Buenos Aires], private claimants are granted direct *jus standi* before international arbitral tribunals for claims against state parties." Horacio A. Grigera Naon, *Symposium: Free Trade Areas: The Challenge and Promise of Fair vs. Free Trade Panel V: Regionalism and the Transfer of Sovereignty*, 27 LAW & POL'Y INT'L BUS. 1073, 1107 (1996). Under the current Protocols "private parties may... directly submit, without prior exhaustion of local remedies, foreign investment claims against MERCOSUR host countries to international arbitral bodies that will make their decisions primarily on the basis of widely accepted international standards for the protection of foreign investment and investors." *Id.* at 1108.

This is also one of the fundamental features of NAFTA Chapter 11, and its provisions "for individual investors to sue foreign nations directly to enforce the agreements guarantees... Through investor-state provisions, public international law has become more private... In general, capital-exporting countries favor investor-state provisions to protect their citizens from lesser-developed countries' temptation to confiscate foreign assets." Rene Lettow Lerner, *International Pressure to Harmonize: The US Civil Justice System in an Era of Global Trade*, 2001 B.Y.U. L. REV. 229, 233 (2001).

It has been pointed out that the Colonia and Buenos Aires Protocols contain provisions that may be applied to resolve disputes between private investors and host states similar to the processes in various bilateral investment treaties. Guira, *supra* note 28, at 261.

56. Protocol of Colonia, *supra* note 51, art. 9(1).
57. *Id.* art. 9(2).

(3) a future permanent system of controversy resolution with private parties to be established under the Treaty of Asunción.[58] Regardless of which method the investor selects, the decision will be definitive.[59] Under article 4 of the Protocol, if the investor is not content with the decision reached in one of the three systems of resolution, the aggrieved party may appeal to international arbitration[60] either under the Convention on Solution of Controversies Relative to Investment between National States and Other States (ICSID Convention) or an ad hoc arbitration court established under the guidelines of arbitration promulgated by the United Nations Commission for International Commercial Law (UNCITRAL).[61] Decisions under arbitration then will be deemed final, and the member state must execute the rulings in accordance with its domestic legislation.[62]

Under the Protocol of Buenos Aires, the members of MERCOSUR acknowledge that a system of generally accepted legal principles is necessary to attract third state investment

58. *Id.* art. 9(2)(I–III).
59. *Id.* art. 9(3).
60. *Id.* art. 9(4).
61. *Id.* art. 9(4)(a & b). In regards to the ICSID rules, where either the host or home state of the investment or investor is not an ICSID contracting party, the dispute is subject to the ICSID Additional Facility Rules. *Id.* art. 9(4)(a); *see also* Maryse Robert & Theresa Wetter, *Toward an Investment Agreement in the Americas: Building on the Existing Consensus, in* TRADE RULES IN THE MAKING, *supra* note 4, at 408–409. Argentina, Paraguay, and Uruguay are signatories to the ICSID Convention. Brazil has not acceded to the agreement. *ICSID-List of Contracting Parties, available at* www.worldbank.org/icsid/constate/c-states-en.htm (last visited Feb. 15, 2002).

    There appears to be a dearth of arbitration referrals to ICSID in regards to investor-MERCOSUR state dispute settlement. Two proceedings of note involve Argentina, France, and the United States. However, these cases do not involve MERCOSUR instruments (i.e., Protocol of Buenos Aires), but prior bilateral investment treaties. *See* Compañia de Aguas del Aconquija S.A. and Vivendi Universal v. Argentina Republic (Case No. ARB/97/3), 40 I.L.M. 426(2001) [Argentina-France BIT] *and* Lanco Int'l, Inc. v. Argentine Republic (Case No. ARB/97/6), 40 I.L.M. 457(2001) [Argentina-U.S. BIT].

    In general, it has been noted that, as an aggregate, the dispute settlement system under MERCOSUR has been rarely used. "The group has not agreed on common policies on matters ranging from customs codes to competition policy and investment subsidies; most disputes are still settled by presidential intervention rather than agreed rules." *Some Realism for MERCOSUR: Better a Genuine Free-Trade Area Than a Phoney Customs Union*, THE ECONOMIST, 31 Mar. 2001, 2001 WL 7318346; Under the investment dispute regimes, ad hoc arbitration panels may be constituted. However,

    > [i]n practice, disputes have been settled politically by the MERCOSUR presidents themselves. [Until recently] this system has worked: to safeguard the whole project the presidents have been prepared to compromise, and when need be, rewrite the rules. But this carries a cost in reducing certainty. Until a tested and politically-neutral dispute-settlement mechanism is in place, investors thinking of setting up, say in Uruguay, cannot be certain of guaranteed and barrier-free access to the Brazilian market.

    A Survey of MERCOSUR: The Road to a Single Market—MERCOSUR Needs Less Red Tape But More Common Rules, 12 Oct. 1996, 1996 WL 11247185.
62. Protocol of Colonia, *supra* note 51, art. 9(6).

and protect the interests of investors from these countries.[63] In general, "it operates in substantially the same manner as the Protocol of Colonia."[64] Like the Protocol of Colonia, the Protocol of Buenos Aires adheres to the principles of fair and equitable treatment,[65] national treatment,[66] most-favored-nation treatment,[67] free transfer of monies,[68] and compensation for expropriation.[69]

In sum, the MERCOSUR investor-state dispute settlement system is fairly simple, at least relative to the bloc's North American counterpart. It remains shallow after a decade in existence. It has been noted that MERCOSUR is "not as sophisticated and complex in the articulation of rules to cover specific situations, as in the NAFTA model."[70] The final section of this paper examines the argument that the current investor-state dispute resolution framework under MERCOSUR remains woefully inadequate, and that attempts to radically restructure the current system are necessary to avoid upsetting of the delicate balance of interests present in the Southern Cone.

B. North American Free Trade Agreement

Unlike the Protocol of Buenos Aires, designed to protect investments of states outside of MERCOSUR,[71] NAFTA promulgates rules, under its Chapter 11, to protect only

63. Protocol of Buenos Aires, *supra* note 52, preamble.
64. Gilmore, *supra* note 53, at 401. One major difference, is that upon the unsuccessful resolution of an investment dispute to be settled amicably, the aggrieved investor has six months to submit the claim to either arbitration or a national court. Protocol of Colonia, *supra* note 51, art. 9(2). The Protocol of Buenos Aires prescribes the amicable negotiation–arbitration court process only "within a reasonable period of time." Protocol of Buenos Aires, *supra* note 52, art. 2(H)(2).
65. Protocol of Buenos Aires, *supra* note 52, art. 2(C)(1).
66. *Id.* art. 2(C)(2).
67. *Id.* An exception to this principle is contained in art. 2(C)(3). "The State, Parties shall not extend to investors from Third States, the benefits of any treatment, preference, or privilege, resulting from: (a) their participation or association in a free trade area, customs union, common market, or similar regional agreement; (b) an international agreement totally or partially related to tax matters."
68. *Id.* art. 2(E).
69. *Id.* art. 2(D).
70. Guira, *supra* note 28, at 257.

> Thus far, MERCOSUL [the Portuguese acronym for the Common Market of the South] has opted for an integration model with supranational institutions. This has been a critical failure, particularly because a permanent court along the lines of the European Court of Justice is sorely needed. Only a supranational tribunal can resolve the two fundamental questions for full implementation of the Treaty of Asunción: control of the legality of the acts of the communitarian bodies and Member States, and the uniform interpretation of Community Law.

de Araujo, *supra* note 19, at 35.

71. *See* text *supra* note 55. To an extent, the Protocol of Buenos Aires on investment in MERCOSUR acts as a universal "bilateral treaty" by permitting third state investors facilitated access to remedies in national courts or international arbitral panels.

those investors of enterprises from Canada, Mexico, and the United States.[72] Chapter 11 provides a "comprehensive series of rights" for investors of one NAFTA signatory investing in the territory of another signatory.[73] These rights include national treatment,[74] most-favored-nation treatment,[75] protection from performance requirements,[76] free transfer of funds,[77] and protection from governmental takings.[78] Actions of national, state, provincial, and local governments are valid bases for the assertion of claims under the Chapter 11 investment protection rules.[79]

Once a dispute has arisen, the investor and host state must attempt to settle the claim through consultations or negotiation.[80] If this process proves unsuccessful within the three-year limitations period,[81] the aggrieved investor must deliver an intention to submit a claim to arbitration at least ninety days prior to the submission.[82] At the discretion of the investor, the claim may be governed under: (1) the ICSID Convention, provided that both the NAFTA state investor and the NAFTA host state are parties to

72. NAFTA, *supra* note 31, at Ch. 11. Chapter 11 of NAFTA refers to the protection of investments from "investor[s] of a Party" and claims submitted on behalf of either the investor, *id.* art. 1116, or on behalf of the enterprise, *id.* art. 1117. Under NAFTA, to be considered an "investor of a Party" an enterprise must be organized under the laws of Canada, Mexico, or the United States. Robert, *supra* note 31, at 193. NAFTA has no requirement that the enterprise be controlled by nationals of a NAFTA signatory state. *Id.* In contrast, "civil law countries have traditionally relied . . . on the place where the management or seat of the company is located. The two MERCOSUR protocols on investment have elected that criterion." *Id.* at 194. *See also* Grigera Naon, *supra* note 55, at 1155. Under NAFTA Chapter 11, "if a company is controlled by non-member investors, and does not carry on substantial business activities in the member country of incorporation, it is not considered a national investor of a member country."

    Section B of Chapter 11 deals specifically with the "settlement of disputes between a party and an investor of another party." Article 1115 states that "this subchapter establishes a mechanism for the settlement of investment disputes that assures both equal treatment among investors of the Parties in accordance with the principle of international reciprocity and due process before an impartial tribunal."
73. David A. Gantz, *Potential Conflicts between Investor Rights and Environmental Regulation under NAFTA's Chapter 11*, 33 GEO. WASH. INT'L L. REV. 651, 652 (2001).
74. NAFTA, *supra* note 31, art. 1102.
75. *Id.* art. 1103. Article 1104 states that all NAFTA members must give investors the better of the treatments required under articles 1102 and 1103.
76. *Id.* art. 1106.
77. *Id.* art. 1109.
78. *Id.* art. 1110. This article includes expropriation, nationalization, and measures "tantamount to nationalization or expropriation" of an investment.
79. Lucien Dhooge, *The Revenge of the Trail Smelter: Environmental Regulation as Expropriation Pursuant to the North American Free Trade Agreement*, 38 AM. BUS. L.J. 475, 487 (2001). "The national governments of the parties are charged with responsibility for assuring implementation of NAFTA's provisions, and are accountable in the event they are unable to secure state or provincial compliance." *Id.*
80. *NAFTA, supra* note 31, art. 1118.
81. *Id.* art. 1116(2); *Id.* art. 1117(2).
82. *Id.* art. 1119. Additionally, a six month period must elapse between the time the event giving rise to a claim occurred and submission of the claim. *Id.* art. 1120(1).

the Convention; (2) the Additional Facility Rules of ICSID, provided that either the investor or the host state, but not both, is a party to the ICSID Convention, or (3) the UNCITRAL Arbitration Rules.[83] Once an arbitration claim has been submitted, the investor party waives its right to obtain a remedy under the court system of the NAFTA state involved in the claim, unless for injunctive, declaratory, or other, nonmonetary related relief.[84]

Once submitted to arbitration, the disputing parties must select the panel, or Tribunal, which shall consist of three arbitrators, one selected by each party, and the third, known as the presiding arbitrator, appointed by agreement of the parties.[85] If, after ninety days of the claim submission, the Tribunal has not yet been assembled, the Secretary-General will intervene and appoint the appropriate arbitrators from a roster of forty-five arbitrators established by a consensus of the NAFTA states.[86] Once the Tribunal has reached a final decision, the body may award only monetary damages, any applicable interest, and restitution of property.[87] Punitive damages shall not be awarded.[88] The unsuccessful party must comply with the decision of the Tribunal without delay.[89] Each

83. *Id.* art. 1120. Currently, of the three NAFTA member states, only the United States is a signatory to the ICSID Convention. *ICSID-List of Contracting Parties*, *supra* note 61.

84. *NAFTA*, *supra* note 31, art. 1121(1) & (2). One claim of note focused upon the Tribunal's interpretation of the article 1121 waiver provisions. In *Waste Management, Inc. v. United Mexican States*, the claimant, a U.S. waste disposal company, filed a dispute under the ICSID Additional Facility Rules against the State of Guerrero and the municipality of Acapulco for breaches of articles 1105 and 1110. ARB(AF)/98/2, 40 I.L.M. 56 (2001), *available at* www.state.gov/s/l/c3753.htm (last visited Feb. 19, 2002). Waste Management filed a waiver to bring the claim to a NAFTA Tribunal. However, once the waiver was filed, Waste Management's subsidiary pursued further related claims against Acapulco under Mexican law. The Tribunal held that the claimant's waiver was inadequate, and that the panel lacked jurisdiction in this matter. *See id.* §31 of the arbitral award of 2 June 2000. For further analysis of this case, *see* Bernard Oxman & William Dodge, *Arbitration—NAFTA—Jurisdiction—Waiver of Right to Initiate or Continue Other Legal Proceedings—Effect of Pursuing Municipal Law Claims in Municipal Court*, 95 AM. J. INT'L L. 186 (2001).

Under NAFTA article 1121, a claimant waives his or her right to "initiate or continue before any administrative tribunal or court under the law of any Party,... any proceedings with respect to the measure of the disputing Party that is alleged to be a breach" of a NAFTA obligation. "In short, the Article 1121 waiver protects against claimants 'double-dipping' and maintaining cases in two different forums simultaneously, with respect to the same measures that allegedly caused them injuries." Jacob S. Lee, *No "Double-Dipping" Allowed: An Analysis of Waste Management, Inc. v. United Mexican States and the Article 1121 Waiver Requirement for Arbitration under Chapter 11 of NAFTA*, 69 FORDHAM L. REV. 2655, 2657 (2001).

85. *NAFTA*, *supra* note 31, art. 1123.

86. *Id.* arts. 1124(2), (3).

87. *Id.* art. 1135(1). Tribunal decisions are reached by simple majority. *ICSID Rules*, art. 25, *available at* www.worldbank.org/facility/33/htm (last visited Feb. 18, 2002). Also, panel awards have no precedential force (i.e., they are binding only between the disputing parties). NAFTA, *supra* note 31, art. 1136(1).

88. *Id.* art. 1135(3).

89. *Id.* art. 1136(2). This rule is tempered by article 1135(3). Under this section, the prevailing party must wait: (i) 120 days, or (ii) after revision or annulment proceedings have been completed if the award was made under the ICSID Convention. If the award was granted under

state party is obligated to provide for the enforcement of Tribunal awards in its individual territory.[90] If this party fails to comply, the government of the investor may request the Commission to establish a panel under the rules of Chapter 20.[91] Under the provisions of Chapter 20, the noncompliant party may face suspension of NAFTA benefits.[92]

As the NAFTA regime evolves, the investment protection provisions under its Chapter 11 will "become most significant in terms of conflicts between free trade and investment flows, and other governmental objectives, such as protection of the environment."[93]

As noted earlier, available investor-state dispute resolution mechanisms under MERCOSUR appear to rarely have been employed to their fullest. In contrast, recent years have "witnessed an increase in the frequency and importance" of NAFTA investor-state claims, particularly involving American investors against Canada and Mexico, and Canadian claims against the United States.[94] This increase is evident of the rules in Chapter 11,

---

the ICSID Additional Facility Rules or the UNCITRAL Arbitration Rules, the prevailing party must: (i) wait three months after the rendering of the award, and no party has commenced a proceeding to revise, set aside, or annul the award, or (ii) a court has dismissed or allowed a request to revise, set side, or annul the award and there is no further appeal pending.

90. *Id.* art. 1136(2).
91. *Id.* art. 1135(6).
92. *Id.* art. 2019.
93. Gantz, *supra* note 73, at 652.

> Protection of investment is an integral part of NAFTA. [It has been] noted: Trade and investment flows are interdependent. To achieve the benefits of economic liberalization, investment barriers must be addressed as comprehensively as trade barriers. Hence, a chapter on investment was an essential element of an agreement that was to provide the basis for hemispheric free trade.

Id.

94. Todd Weiler, *Foreign Investment in the United States*, 35 INT'L LAW. 363, 363 (2001). As of 19 February 2002, at least thirteen NAFTA investor-state arbitrations have either concluded or are still pending. *See* United States Department of State website, *at* www.state.gov/s/l/c3439.htm (last visited Feb. 19, 2002). In many of the Chapter 11 actions brought, environmental regulatory issues have been involved to some degree. Gantz, *supra* note 73, at 659.

Some cases of note include Azinian v. United Mexican States, the first case decided on the merits by a NAFTA tribunal. *Id.* at 702; case report available at www.state.gov/s/l/c3750.htm (last visited Aug. 15, 2002). In this case, an American investor claimed that the City of Naucalpan terminated its landfill and waste management operation contract without cause. The Tribunal found in favor of Mexico in a case that "demonstrated neither arbitrary government action nor discrimination against foreign investors nor any factual evidence of an expropriation." *Id.*

In Ethyl Corp. v. Government of Canada, a panel created under Canada's Agreement on Internal Trade found that Canada's ban on gasoline imports containing an additive called MMT created an unfair trade environment. 38 I.L.M. 708 (1999); case report available at www.state.gov/s/l/c3745.htm (last visited Aug. 15, 2002). In exchange for withdrawal of its Tribunal claim, Ethyl received $13 million from Canada. The importation ban was soon thereafter removed by the Canadian government.

The classic "not-in-my-backyard" argument, David A. Gantz, *Reconciling Environmental Protection and Investor Rights Under Chapter 11 of NAFTA*, 31 ENVTL. L. REP. 10646 (2001)

which are aimed to "ease and facilitate investment by being clearly workable and predictable for all interested parties... Enhancing investors' ability to recover for breaches of Chapter 11 is often treated as the unwritten subtext of the goals set forth in Article 102 of Chapter One."[95]

However, while both investors and lawyers appreciate the institutional depth and structure of Chapter 11, the question is at what cost to national sovereignty. The final section of this paper will conclude that, while the investment dispute settlement system under NAFTA far exceeds the capabilities of MERCOSUR at this time, the former regime must exercise greater caution in weighing environmental concerns and sovereignty against the desirable input of foreign investment.

---

came to the fore in Metalclad Corp. v. United Mexican States. In this case, an American investor contracted to open and operate a hazardous waste facility in the state of San Luis Potosi. Soon thereafter, the governor of the state declared the landfill site to be a protected zone for rare cacti. The NAFTA Tribunal awarded Metalclad $16.7 million, some of which was set aside. CSID Case No. ARB(AB)/97/1; case report available at www.state.gov/s/l/c3752.htm (last visited Aug. 15, 2002).

This case marked the first time one of the NAFTA member states lost a case brought against it under the Chapter 11 investor-state dispute resolution mechanism. *See* Lucien Dhooge, *The North American Free Trade Agreement and the Environment: The Lessons of Metalclad Corporation v. United Mexican States*, 10 MINN. J. GLOBAL TRADE 209, 213 (2001). For further analysis of this case and the "firestorm of criticism" from environmentalists that followed. *Id.*

In S.D. Meyers v. Government of Canada, an Ohio corporation filed claims alleging a taking of property rights by Canada. Case report available at www.state.gov/s/l/c3746.htm (last visited Aug. 15, 2002). The claimant had a polychlorinated biphenyl (PCB) processing plant in Ohio. Canada had in place a law banning exports of PCB to the United States (for disposal), in effect protecting Canada's only PCB treatment plant in Swan Hills, Alberta. The arbitrators found that Canada violated the national treatment and minimum standards of treatment provisions of NAFTA. For in-depth analysis of this case, *see* Brian Trevor Hodges, *Where the Grass is Always Greener: Foreign Investor Actions Against Environmental Regulations under NAFTA's Chapter 11: S.D. Meyers, Inc. v. Canada*, 14 GEO. INT'L ENVTL. L. REV. 367 (2001).

In Methanex Corp. v. United States, the Canadian investor, a manufacturer of methanol, alleges injuries suffered due to California's ban on the use of a gasoline additive known as MTBE. Case report available at www.state.gov/s/l/c5818 (last visited Aug. 17, 2002). Methanol is a key ingredient of MTBE. Methanex contends that the ban violates the fair and equitable treatment, national treatment, and expropriation provisions of NAFTA. As such, Methanex claims damages of $1 billion. The case is still pending.

Like the *Metalclad* case, Methanex's claims have been decried by environmental concerns. Several environmental groups, including Greenpeace and the Sierra Club have "called upon NAFTA's Free Trade Commission to suspend proceedings challenging environmental protections... until such time as the contracting parities clarify the relation of environmental laws to NAFTA's investor-state provisions." Dhooge, *supra* note 79, at 479. All claims and arbitration decisions adjudicated under Chapter 11 are available at http://www.state.gov/s/l/c3439.htm.

95. Andrea Bjorklund, *Contract without Privity: Sovereign Offer and Investor Acceptance*, 2 CHI. J. INT'L L. 183, 183 (2001). Of course, NAFTA Chapter 11 protections "need not, and should not, be read to mean that any NAFTA investor can recoup the losses it suffered in any investment deal gone awry." *Id.* at 186.

IV. Conclusion

In regards to NAFTA, recent years have produced a trickle of claims, which began in the late 1990s, and are "now resulting in a slow but steady stream of substantive and procedural case law that promises to contribute substantially to international economic law in general[.]"[96] While this inevitably produces a rich legal framework from which to draw, Chapter 11 has the potential to evolve into an "out of control monster," creating an overwhelming influx of litigation and frivolous claims.[97] This increase has the potential of opening floodgates, swamping the arbitration mechanism, and creating a system of economic compensation for alleged wrongs, while simultaneously and tacitly promoting environmental degradation.[98] This concern seems more legitimate in light of the *Metalclad* and *Methanex* cases.

Overall, however, NAFTA has rapidly evolved into probably the most overwhelmingly successful regional arrangement. One element of this success and attractiveness has been its reliable investor-state dispute resolution system. Allowing individuals to directly approach governments and seek redress is fundamental to the democratic expectations of the NAFTA countries, and indicates a greater evolution towards privatization of international law. While the current system surely requires some revision, at the current time, the feared juggernaut of litigation has not yet occurred. As alluded to earlier, the nexus of expropriation–environmental concerns pervades any mention of Chapter 11 reformation. While *Metalclad* and *Methanex* could produce disconcerting, if not outrageous results, governments and investors must exercise restraint to avoid the risk of judicial harassment and rampant corporate greed.

For MERCOSUR and its investor-state system, the situation is dramatically different. Recent economic and political problems in the leaders of MERCOSUR, Argentina and Brazil, will only exacerbate the situation. MERCOSUR was created to promote trade harmonization. However, trade and investment are elegantly intertwined. While the Protocols of Colonia and Buenos Aires provide a progressive framework and "incorporate

96. Weiler, *supra* note 94, at 373.

97. Daniel M. Price, *NAFTA Chapter 11—Investor-State Dispute Settlement: Frankenstein or Safety Valve*, 26 CAN.-U.S. L.J. 107, S9 (2001). Mr. Price points out that predictions about misuse of Chapter 11 remain premature due to the small amount of decisions handed down. *Id.*

98. NAFTA, *supra* note 31, art. 1114.1:

> nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure, otherwise consistent with this Chapter, that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns.

However, the drafting "leaves something to be desired... In the event of a conflict between Article 1114:1 and Article 1110:1, is the 'any measure otherwise consistent with this Chapter' language in Article 1114:1 designed... to subordinate Article 1114(a) to Article 1110:1, or is it hopelessly circular?" *See* Gantz, *supra* note 73, at 679–680.

One should note that while the objectives of NAFTA article 102 specifically refer to the desire to "increase substantially investment in the territories of the Parties," NAFTA, *supra* note 31, art. 102(1)(c), no mention of protection of the environment is made. Gantz, *supra* note 73, at 680.

comprehensive investment disciplines,"[99] the complete MERCOSUR system could produce apprehension to prospective investors. The overall MERCOSUR system has been designed to reflect its objective of "economic integration thorough political cooperation rather than institutionalism."[100] However, without greater commitment by the MERCOSUR states to implement rules, in particular investor-state resolution provisions, investor confidence will inevitably decline. This ambivalence is exemplified by the fact that both the Colonia and Buenos Aires Protocols have not yet entered into force.[101] This is because the national legislatures of the signatory states have not fully integrated these agreements into their juridical systems. In contrast, the NAFTA system is relatively comprehensive and at full implementation. While daunting, its repletion and predictability provides reliability and confidence.

In conclusion, hemispheric integration has come to the fore in recent years as progress, albeit incremental, towards a more expansive free trade system, or Free Trade Area of the Americas, has occurred. Once successfully established, investment rules will prove dominant and "investor-state dispute settlement will be essential to ensuring the effectiveness of those rules."[102]

99. Robert & Wetter, *supra* note 61, at 390.
100. Taylor, *supra* note 3, at 867–68.
101. Salazar-Xirinachs, *supra* note 4, at 81; *see also* text, *supra* note 24.
102. Price, *supra* note 97, at S9.