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A Tailor-Made (*Legal*) Suit? The Actual Scope, Power, and Functioning of NAFTA Chapter 11's Rules and Institutions for the Settlement of Cross-Border Disputes

¿Un traje (legal) hecho a la medida? Funcionamiento, capacidad y alcance reales de las reglas e instituciones del Capítulo 11 del TLCAN para resolver disputas fronterizas

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Abstract

Numerous scholars argue that the rules, mechanisms, and bodies established under NAFTA's Chapter 11 for the settlement of foreign direct investment disputes have undermined the policy-making capabilities of governments in the U.S., Mexico, and Canada for promoting public welfare in their countries. This article argues that Chapter 11 has instead contributed to reaffirming governments' power to enact and uphold social-oriented domestic laws. It demonstrates that Chapter 11's dispute settlement mechanisms were created and operate according to the interests of the national governments in facilitating and increasing the flows of trade and capital investment between countries without compromising their sovereignty and policy-making powers.

Key words: dispute settlement, NAFTA Chapter 11, North America, regional institutions.

Resumen

Numerosos académicos argumentan que las reglas, mecanismos y organismos establecidos con el Capítulo 11 del TLCAN para resolver las disputas de inversión extranjera directa han disminuido las capacidades de los gobiernos de Estados Unidos, México y Canadá para establecer políticas públicas dirigidas a promover el bienestar social en sus países. Este artículo argumenta que, por el contrario, el Capítulo 11 ha contribuido a reafirmar la capacidad de los gobiernos para promulgar e implementar leyes locales orientadas a lo social; demuestra que los mecanismos para solucionar disputas del Capítulo 11 se crearon y operan de acuerdo con los intereses de los gobiernos nacionales de facilitar e incrementar los flujos de comercio e inversión de capital entre los países sin comprometer su soberanía y sus facultades para instrumentar políticas públicas.

Palabras clave: resolución de disputas, Capítulo 11 del TLCAN, América del Norte, instituciones regionales.

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Introduction*

The North American Free Trade Agreement's Chapter 11 has been a subject of great interest for scholars. Its proposal, negotiation, and implementation have been widely analyzed and discussed in the literature (see Gantz, 1999; Dumberry, 2001; Brower, 2002; Hart and Dymond, 2002; Jones, 2002; Kurtz, 2002; Aguilar Álvarez and Park, 2003; Staff and Lewis, 2003; McRae and Siwiec, 2010; Karamanian, 2012). Most of that interest has arisen from the controversial nature of the rules, mechanisms, and bodies it established to protect foreign direct investment (FDI). The most common concern expressed by scholars with regard to this chapter relates to the operation of a dispute settlement mechanism that allows business actors to challenge the decisions and actions of North American national and sub-national governments that might have damaged their investments and, if successful, to receive compensation for them.

Some scholars argue that the operation –and even the mere existence– of such a mechanism has enabled investors and firms to undermine the power of North American governments to enact or uphold domestic social-oriented legislation that is, or might appear to be, unfavorable to their businesses (see Matiation, 2003; McBride, 2006; Clarkson, 2008; Wood and Clarkson, 2009). For instance, Runnalls and Fuller argue that the implementation of Chapter 11 has produced a "disturbing lack of balance between the protection of private interests and the need to promote and protect the public welfare" in North America (2001, p. viii). Similarly, Aguilar Álvarez and Park (2003) argue that Chapter 11 has caused a detrimental shift in domestic policy-making, which has moved away from the promotion of public interest toward the protection of private interests. These and other similar views have generated a consensus in the current scholarship on NAFTA, which classifies Chapter 11 as an instrument that "goes too far in favoring investors over [public] interests" (Van Harten, 2009, p. 43). A number of policymakers and non-governmental organizations (NGOs) express similar concerns over the operation of Chapter 11 and its dispute settlement mechanism. For instance, Elizabeth May (2013), leader of the Green Party of Canada, has stated,

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"Far from being of benefit to governments and their citizens, Chapter 11 has proven to fundamentally erode a government's ability to enact laws, regulations, and policies" aimed at protecting the welfare of its citizens. Likewise, the Mexican Action Network Against Free Trade has denounced Chapter 11 for allegedly undermining the ability of the North American governments, especially Mexico's, to protect the public interest by enabling private companies "to sue for damages before nearly secret [Chapter 11] tribunals," whose rulings endanger workers, the environment, and public health in the North American countries (RMALC, 2009).[1]

I argue, however, that most of these scholars, policymakers, and analysts provide a partial account of the performance of Chapter 11's rules and bodies and their effects on governmental actors. This account is based on the *assumption* that the instrument inherently benefits foreign investors at the expense of the policy-making power of national and sub-national governments. In this article, I demonstrate that, far from undermining the power of the North American governments to legislate on public welfare issues within their borders, the operation of Chapter 11 rules, mechanisms, and quasi-regional dispute settlement bodies has contributed to reaffirming the actions and decisions of government actors for the protection of the public interest.

To advance this argument, I demonstrate first that the negotiation and implementation of Chapter 11 responded *mainly* to the interests of the North American national governments –not business actors, as is commonly held– by delivering an institutional and legal framework that contributed to increased FDI flows in the region.[2] I argue that government actors aimed at increasing individuals and firms' confidence in the safety of their investments *without* creating new rights for foreign investors or the protection of those investments. Then, I discuss how the parties to NAFTA achieved such a seemingly contradictory outcome. I argue that the governments did not negotiate and establish international laws on the protection of FDI, or create administrative bodies and dispute resolution mechanisms with extensive powers, as is commonly argued. Instead, the national governments delivered an agreement that set cross-border rules with limited scope for the *promotion* of foreign direct investment, and *established quasi-regional bodies*, *not permanent regional institutions*, to administer the agreement's provisions and arbitrate disputes arising from the interpretation, implementation, or transgres-

[1] U.S. and Canadian NGOs, such as the Québec Network on Continental Integration and the Alliance for Responsible Trade, routinely join the demands of the Mexican Action Network Against Free Trade for opening the proceedings of Chapter 11 tribunals to public scrutiny. This is, however, a misunderstanding of the nature of tribunals. In fact, no provision in Chapter 11 suggests that their proceedings must be confidential or that the parties intended them to be so (Romero Jiménez, 2001).

[2] I use the term "legal framework" to describe the existence of a set of "rules [at the regional level] that are generally followed and may be subject to coercive enforcement" (Westbrook, 2008, p. 349) rather than only the existence of laws at the domestic level enforced by national or sub-national courts.

sion of its rules. By doing this, the national governments ensured that the Chapter 11 provisions would not compromise their sovereignty and policy-making powers.

Through the in-depth analysis of three case studies, this article shows how Chapter 11 has contributed to reaffirming, rather than undermining, the power of nation-states to enact and uphold social-oriented domestic legislation. In general, Chapter 11 institutions have contributed to asserting the precedence of government actors and their decisions over the claims of foreign investors on the protection of their investments within the North American countries.

A Methodological Consideration: Chapter 11 or nafta?

The institutional framework for managing Chapter 11 can be analyzed separately from the rest of nafta. Yet, it could be argued that this instrument is not a stand-alone or side agreement and thus cannot be analyzed separately without compromising its comprehensiveness. It could be further argued that Chapter 11 did not establish an institutional structure of its own to manage its provisions because such a structure exists at the entire agreement –not the chapter– level.

To address these possible methodological objections, I would argue, then, that nafta was not the result of a single trilateral negotiation for the liberalization of trade and investment in North America. It was instead the sum of 1) the review and renegotiation of previous bilateral trade agreements between the U.S. and Canada; 2) the establishment of new trilateral rules for opening further trade and investment opportunities among the North American countries; and, 3) country-specific provisions and exceptions that were negotiated on a trilateral and dual-bilateral basis. It can be argued, then, that nafta is the sum of a large number of rules on a wide range of trade and investment issues that, despite their interrelatedness, have been generated in different contexts and regulate different aspects of the various exchanges among the North American countries. nafta is then an agreement that incorporates various related but separate agreements that do not significantly rely on each other for their implementation or interpretation. On this basis, Chapter 11 can be analyzed as if it were a separate agreement.[3]

[3] This is evident in the text of the agreement itself. nafta is made up of eight parts, unevenly separated into 22 chapters. Each part is a group of chapters covering a range of similar trade and investment issues. Each part and chapter regulates a different aspect of the trade and investment exchanges among the North American countries. They separately outline the specificities of the day-to-day implementation and management of trade- and investment-related issues among the North American countries. With 22 chapters, nafta is a very broad agreement, of which Chapter 11 is only "a slice" (Thomas, 2001, pp. 64-65).

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Furthermore, the agreement-level institutions (that is, the Free Trade Commission and the Secretariat) that would have supported the administration of Chapter 11 were never established in the way the NAFTA mandated. Instead, a set of national and quasi-regional institutions and bodies (that is, the national sections and tribunals) assumed their responsibilities and have operated in a manner that is not consistent with the agreement's provisions. In practice, Chapter 11 institutions and bodies operate independently from the institutions that would have managed the agreement as a whole. Therefore, Chapter 11 already operates as a separate agreement and can be analyzed as such.

The Limited Legal and Institutional Framework For Cross-border Investment in North America before NAFTA

Through the elaboration and implementation of Chapter 11, the parties to NAFTA achieved a seemingly contradictory outcome. They created cross-border rules that seemed strong enough to protect foreign direct investments –so as to increase economic exchanges among their countries– while avoiding the creation of a regional institution that might challenge their power and sovereignty by enforcing these rules. To understand how the parties achieved this outcome, it is necessary to review the nature and limited scope of the institutional framework that governed cross-border direct investment in North America before NAFTA.

Before the agreement came into effect, there was no set of rules for governing FDI *at the trilateral level* in North America. Various circumstances accounted for this. First, the value of the FDI exchanged among the North American countries was relatively small before the implementation of NAFTA.[4] In this environment, the establishment of a set of *regional* rules for the protection of FDI was largely unnecessary, and little demand existed for it from foreign investors at the time. Nonetheless, the national governments expected that the increased confidence among foreign investors resulting from the implementation of this instrument would facilitate and increase the flow of investment capital among their countries.

Second, the North American countries had already eliminated most domestic rules and requirements that restricted or distorted investment, as a result of the implementation of the Canada- U.S. Free Trade Agreement (CUSFTA) and, to a lesser extent, the General Agreement on Tariffs and Trade (GATT).[5] Lastly, even before the end

[4] At the start of the 1990s, the value of intra-regional trade in North America came to US$240 billion, while the same figure for intra-regional FDI amounted to as little as US$6.9 billion (Salvatore, 2007, p. 5; OECD, 2012).
[5] Later transformed into the World Trade Organization (WTO).

of the GATT negotiations for the liberalization of global investment (that is, the Agreement on Trade-Related-Investment Measures, or TRIMS), the three North American countries had already limited, eliminated, or were progressively phasing out a large number of rules, requirements, and barriers to FDI as well as domestic regulations with distorting effects on imports, in an effort to attract capital (UNCTAD/WTO, 2006, p. 163; UNCTAD, 2007).[6] This institutional framework, made up of a bilateral and a global agreement, governed cross-border investment in North America up until the 1990s. The expected increase in trade-related investment resulting from the implementation of NAFTA led potential investors to demand the creation of *regional* rules that would protect FDI in other North American countries –especially in Mexico, which was seen as a country with a weak rule of law (Laird, 2001, p. 224). Once implemented, NAFTA provisions superseded CUSFTA and outdid those of GATT/WTO, including its then-forthcoming agreement on TRIMS.

Given the close relationship between these agreements and the similarity of their objectives, some authors argue that NAFTA only reiterates or further strengthens the provisions contained in the other two agreements (see Taylor, 2000; Freeman, 2009). Similarly, Mann and Von Moltke (2002) argue that NAFTA's provisions for the protection of FDI merely underpin at the regional level the treatment already accorded to foreign investors elsewhere. Similarly, Gantz (1999, p. 1026) argues that Chapter 11 merely provides the North American countries with yet another choice amid the already existing range of alternatives on the international level for addressing investment-related disputes. However, these scholars overlook a crucial feature of Chapter 11, which made it a significant and innovative institutional development in the North American context: it created, in principle, a cross-border legal framework with well-defined procedures for the protection of FDI that did not previously exist at the regional level in North America.[7] It purportedly advanced the rights that foreign investors had *vis-à-vis* the national governments and created arbitration mechanisms that did not exist in previous agreements.[8] Its rules go beyond the limited dispute

[6] It is for this reason that the Agreement on Trade-Related Investment Measures (TRIMS), which prohibited trade-related investment measures, was not a breakthrough in the North American context, as it did not provide foreign investors with new rights or remedies for protecting their investments.

[7] Perezcano Díaz (1999, p. 95) argues that "the right [that Chapter 11 conferred] upon investors to have direct access to international arbitration is a valuable and remarkable remedy in the North American context. NAFTA's predecessor, [that is, CUSFTA], did not have investor-to-state arbitration. Chapter 11 was then an extraordinary" achievement in the development of the regional legal framework for the protection of FDI.

[8] For instance, Stiglitz argues that "hidden in NAFTA was a new set of rights –for business– that potentially weakened democracy throughout North America. Under NAFTA, if foreign investors believe they are being harmed by regulations (no matter how well justified), they may sue for damages in special tribunals without the transparency afforded by normal judicial proceedings. If successful, they receive direct compensation from the federal government. Environmental, health, and safety regulations have been attacked and put into jeopardy" (2004).

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review mechanisms of previous agreements and provide transnational actors direct access to them. Chapter 11, then, did not simply expand existing agreements. It created instead cross-border rules in the form of (would-be) rights for transnational actors and obligations for national governments and established an arbitration mechanism to uphold such entitlements and commitments.

The Cross-border Rules: The Commitments and Obligations Of the National Governments and the (Would-be) Rights of Foreign Investors

The establishment of commitments and obligations for the parties concerning the treatment of foreign investors and their investments in the territories of other NAFTA countries is *the* central feature of Chapter 11. These rules are laid out extensively in 139 articles, which revolve around two main themes: according national treatment to foreign investors in North America, and ensuring national governments' non-interference with the management and operation of foreign investments within their borders.[9] Chapter 11 goes to great lengths to set out the parties' commitments and obligations, the nature, scope, and power of the institutions that will handle the application of its provisions, and the rules that will govern the start of a dispute-settlement procedure.[10] Together, these commitments and obligations for national governments are aimed at creating a predictable business environment for foreign investors and ensuring that they are accorded fair treatment when investing in other NAFTA countries.[11] They are intended to provide certainty to foreign investors that governments will not inter-

[9] Although a detailed analysis of each one of these articles would go beyond the scope of this article, it can be found in Jones (2002).

[10] For the purposes of this article, the most important commitments and obligations set by Chapter 11 are 1) according national or most-favored-nation treatment (MFN) to each other's investors and investments, whichever is better (Article 1103). MFN is a principle of international trade established in the GATT/WTO agreements, which requires trading partners to treat each other equally. This means that if a country grants another special treatment, it has to do the same for all other GATT/WTO member states. In the NAFTA context, this entails national governments agreeing to maintain a level playing field among their national investors and investments and those of other NAFTA countries, and to accord to investors of another NAFTA country treatment no less favorable than that they accord to investors of any other party or non-party to NAFTA; 2) Not imposing on investors conditions related to the performance and management of their investments (Article 1106); and, 3) refraining from nationalizing or expropriating an investment or taking measures "tantamount" to nationalization or expropriation (Article 1110). Given that the term "investment" is broadly defined in the chapter, most foreign direct investments are covered by its provisions and bind the national governments to protect them (see Article 1101) (NAFTA Secretariat, 2014b).

[11] Such commitments and obligations are worded in Chapter 11 as follows: "Each Party shall…." Here, it is important to bear in mind that the parties to NAFTA, and consequently Chapter 11, are the national governments of the United States, Canada, and Mexico, even if its provisions are also intended to protect foreign investors from the actions, decisions, or omissions of provincial and state governments that these nation-states are responsible for in terms of international law.

fere with the establishment, acquisition, management, and general operation of their investments. And, except for some measures related to environmental and health protection (see Article 1114), the rules preclude governments from taking any arbitrary or unjustifiable action that may constitute a restriction on foreign investment (NAFTA Secretariat, 2014b).

One of the most important misunderstandings about Chapter 11 involves the interpretation of the commitments and obligations it sets for national governments and the rights that it purportedly accords to foreign investors.[12] Although Chapter 11 explicitly sets out commitments and obligations for the national governments, it does not explicitly establish rights for foreign investors. Instead, it establishes cross-border rules that *closely* resemble –but are not– private rights for these transnational actors.[13] For instance, Chapter 11 states that national governments shall not actively hinder an investment made by a foreign investor (see Articles 1106, 1107, and 1108). It does not establish, however, that foreign investors have the right to invest without interference from governments. The wording and interpretation of this and other provisions are very important. While it has been *perceived* that these provisions created rights for foreign investors, in fact, they did not.

In line with most accounts of the NAFTA negotiations, I argue that the creation of these rules in Chapter 11, made up of both explicit commitments and obligations for the national governments and perceived rights for foreign investors, was not unintended. According to existing accounts, the demand for negotiating and implementing these rules and dispute settlement mechanisms came from business actors who wanted to protect their investments in other North American countries, most notably Mexico.[14] Nevertheless, in opposition to most accounts, I argue that the conception, negotiation, and implementation of these rules responded mostly to the interests of the national governments in increasing intra-regional FDI flows, which were quite limited in value before NAFTA entered into force. The demands of risk-averse individual investors and firms for the establishment of a *regional* framework for the protection of FDI influenced the debate about NAFTA. The national governments, however, were interested in negotiating, drafting, and implementing rules that advanced their interests in attracting FDI to their countries, simply by "build[ing] investor confidence

[12] For example, Wallace argues that "NAFTA's Chapter 11 gives foreign investors from NAFTA countries [the right] to seek money damages in private international arbitration against the national government of the country in which they are investing" (2004, p. 366). Likewise, Clarkson states that Chapter 11 gives "very broad rights to NAFTA corporations [sic] [who] may arbitrarily allege violation of their property rights and make extravagant claims for remuneration" (2008, p. 84). Such misrepresentations of Chapter 11 are common in the literature.

[13] Such would-be rights are worded in Chapter 11 as follows: "No Party may…."

[14] A noteworthy exception is Brower and Steven (2001).

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throughout the region" (Brower and Steven, 2001, p. 195), rather than necessarily protecting foreign investors in their territories or their national investors abroad. In other words, the creation and implementation of Chapter 11 reflect the interests of the national governments in delivering an agreement that increased FDI in the region *without significantly enhancing* the rights of investors. To do so, the national governments only improved the partial framework that existed in North America for the protection of such investments, as discussed below.

The National and Regional Institutions of NAFTA and Chapter 11

To administer the implementation of NAFTA, including Chapter 11, and address possible issues that might arise from the interpretation or application of its provisions, the parties to the agreement established two permanent regional institutions: the Free Trade Commission (FTC) and the Secretariat. The former is an administrative body made up of the ministers or secretaries responsible for international trade in each of the three North American countries. The latter is an institution that supports the FTC in day-to-day administration of the agreement.

According to NAFTA provisions, the two institutions have –or should have had– important responsibilities in administering Chapter 11. The Free Trade Commission is charged with periodically reviewing the agreement's operation (including Chapter 11) and clarifying the meaning of its provisions if and when necessary. The Secretariat supports –or should have supported– the FTC in overseeing the implementation of the agreement and promoting the achievement of its objectives. While limited, these were important functions, as they gave the FTC the authority to interpret the cross-border rules (Articles 1131 and 1132) and to deliberate and determine the original meaning and intent of these rules. What is more, given that the power to interpret the agreement would necessarily determine the development and outcome of possible disputes between actors located in different national jurisdictions –one of them being a national government–, it can be argued that this provision gave the FTC a quasi-supranational and quasi-judicial character. These provisions also gave the Secretariat the power to handle possible claims for arbitration, thus making it a mediator in the relations between transnational and governmental actors.

Nonetheless, in practice, these institutions operate in a manner that is not consistent with the provisions of Chapter 11. This divergence between the regional institutions' operations as laid out in the text and in reality has restricted their scope and power *vis-à-vis* the national governments. This is especially visible in the structure and responsibilities of the FTC and the Secretariat. As originally proposed and negotiated, these institutions would have had ample responsibilities, mainly related to overseeing and supporting the work of the NAFTA committees, working groups, and bodies (Cameron and Tomlin, 2000: 48; see also McRae and Siwiec, 2010).[15] Yet, when the U.S. failed to provide funding for their establishment and operation, problematically, the responsibilities of the Free Trade Commission and the NAFTA Secretariat were assigned to three separate quasi-subsidiary administrative offices called "national sections" (McRae and Siwiec, 2010: 380). The operation of these offices is inconsistent with the provisions of Chapter 11.

The original function of the national sections was to serve as liaison between the national governments and the regional institutions to enable better communication and thus a more efficient implementation of the agreement. Given this objective, the national sections were intended to operate separately as "mirror-images of each other" (NAFTA Secretariat, 2014b). This means that they are headed and staffed by personnel appointed by their respective national governments and funded by the country where they are based. In effect, however, this structure leads national sections to operate as representations of their corresponding nation-states. In what can be seen as a conflict of interest, the national sections took the place of and assumed the functions and responsibilities originally entrusted to the Free Trade Commission and the Secretariat. In doing so, they effectively became the gatekeepers of the cross-border rules, which were allegedly created to regulate the actions of the national governments and protect the rights of foreign investors. Thus, the governments themselves administer NAFTA, including Chapter 11, through their national sections.

Not even the interpretation and further elaboration of the agreement have been undertaken by the Free Trade Commission as originally planned. Instead, these responsibilities have been undertaken by *ad hoc* tribunals established under the provisions of Chapter 11. As will be shown in the following sections, Chapter 11 tribunals and arbitral panels operate outside the regional framework of NAFTA in a non-permanent and non-subsidiary basis. In brief, the tribunals and arbitral panels are not part of either the FTC or the NAFTA Secretariat, yet have assumed functions that were originally –and solely– entrusted to those institutions.

I argue that this fragmented mode of operation problematically divides the responsibilities that the regional institutions would have had over the administration and implementation of the cross-border rules, including the settlement of disputes related to Chapter 11. This undermines the regional institutions in favor of national bodies and multilateral dispute resolution mechanisms, both in turn biased toward

[15] The NAFTA institutions would have then worked similarly to how the Councils and Secretariats of the Commissions for Environmental (CEC) and Labor Cooperation (CLC) work(ed) in the NAFTA side agreements, the North American Agreements on Environmental and Labor Cooperation (NAAEC and NAALC, respectively).

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national governments. It is important, then, not to overstate the significance of Chapter 11 for the development of a North American institutional architecture for the protection of foreign direct investment. While Chapter 11 did assign responsibilities to regional institutions to administer, interpret, implement, and further elaborate cross-border rules, the national governments did not establish the regional institutions in the way the agreement mandated, and instead assigned those responsibilities to national offices controlled by the national governments themselves and thus biased in their favor.

Chapter 11 Tribunals and Arbitral Panels

The lack of permanent institutions is a feature of NAFTA that extends to the arbitration of disputes that might emerge from the use of Chapter 11 cross-border rules. It is crucial to note that dispute settlement in Chapter 11 is not conducted through regional mechanisms or by permanent bodies that deliberate impartially on possible disputes between foreign investors and governmental actors. Instead, dispute settlement is conducted in accordance with rules set out in existing multilateral mechanisms outside the structure of NAFTA, namely, the International Centre for Settlement of Investment Disputes (ICSID) and the Convention and Additional Facility Rules of the United Nations Commission on International Trade Law (UNCITRAL).[16]

In practice, Chapter 11's dispute resolution mechanism works as follows: if an investor in any of the NAFTA countries deems that a party to the agreement has breached its obligations under Chapter 11, they may file a claim before the relevant national section. The disputing parties first attempt to settle the claim through consultation or negotiation. If the matter is not addressed or solved within a period of six months, the submitter can request its claim be arbitrated by an *ad hoc* NAFTA tribunal. If the claimant goes on with the arbitration, it foregoes its right to initiate or continue any other dispute settlement procedure available to it (Article 1121). The investor then decides under which rules the dispute will be arbitrated: those of the ICSID, the UNCITRAL Convention or UNCITRAL's Additional Facility.[17] Once this has been decided, the

[16] Both mechanisms predate NAFTA and had been used to conciliate and arbitrate international trade-related investment disputes. However, it would not be possible to argue that the national governments favored the use of these instruments due to the experience of their corresponding institutions in handling investment disputes. For instance, although the ICSID was founded in 1966 and to date is the leading international arbitration institution devoted to investor-state dispute settlement, it was not until 1990 that it first arbitrated an investment treaty case (ICSID, 2012, p. 5).

[17] In practice, given the states' variable participation in these bodies, generally only two sets of rules are available to investors to arbitrate a dispute at any given time.

claimant must notify the disputing party of its intention to submit a claim. After receiving this notification, if the matter is still unresolved, both parties must consent to the arbitration of a tribunal, which will be established and operate under the aforementioned multilateral rules. The tribunal examines and deliberates on the dispute in accordance with NAFTA and "applicable rules of international law" (NAFTA Secretariat, 2014b).[18]

In short, to settle regional investor-state disputes, Chapter 11 relies on non-subsidiary, non-permanent bodies that deliberate on these matters on the basis of international rules. The Chapter 11 dispute settlement mechanism is thus not regional, but quasi-regional.[19] Its operation is based upon multilateral, not regional, rules. In fact, Chapter 11 only covers the final stage of the arbitration process: the implementation of the award. If the tribunal decides against one of the parties to NAFTA, that is, the national governments of the United States, Mexico, or Canada, the decision is binding and enforceable. Under the provisions of the agreement, the parties themselves are to provide for the enforcement of the award in their jurisdiction (Article 1134), not the arbitral panels. The tribunal is then dissolved and its final decision is only binding between the disputing parties (Article 1136). As a result, the rulings of NAFTA tribunals do not create precedent.

The Chapter 11 dispute settlement mechanism, therefore, does not have the vast scope and powers that have usually been attributed to them. Its institutions lack the structure and power to *fully* address investor-state disputes that might emerge in North America as a result of dealings between business and governmental actors. While the regional institutions nominally created under NAFTA would have had significant responsibilities and roles in the management of the agreement, their functions are actually undertaken by the national sections. Meanwhile, dispute settlement is conducted by non-subsidiary bodies under multilateral rules. In summary, while Chapter 11 might appear to be more extensive than other agreements formally, it is far less extensive institutionally.[20] This means that its institutions are not only far less powerful that the text of Chapter 11 might suggest, but that the institutions themselves do not exist in the way the agreement established.

[18] Chapter 11 does not go further in determining the responsibilities of the tribunal, describing the way in which it is expected to act or establishing whether it must reach a final decision on the dispute. All these issues are left to the tribunal itself to decide. The chapter only stipulates that such a decision must be made in accordance with NAFTA's intent regarding the promotion of cross-border investment (Article 1131).

[19] I also refer to the tribunal as quasi-regional given that, more often than not, only two out of the three North American countries are represented and participate in the arbitration.

[20] For instance, the WTO maintains standing bodies for both dispute resolution and appealing decisions.

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The Operation of the Cross-border Rules And the Regional Bodies

Therefore, Chapter 11 does not constitute a comprehensive regional framework for the protection of FDI. On the contrary, at different moments, the responsibilities of its regional institutions are assumed by governmental and multilateral actors. The national sections oversee the implementation of its provisions, while the arbitration of investor-state disputes resulting from the use, application, and interpretation of its rules is conducted by bodies outside the NAFTA structure, which are temporary in nature and are precluded from creating precedent for future action. Even the implementation of the final rulings of tribunals established under its rules is subject to acceptance by the corresponding national government, which could still challenge the tribunal's decision. Such a fragmented framework effectively makes Chapter 11's regional institutions redundant.

The provisions of Chapter 11 effectively put the national governments in charge of most of the mechanisms for the protection of FDI. National governments' interests are represented by two different institutions at three different moments in the use, application, interpretation, and modification of rules. The first is at the start of the arbitration process, when transnational actors first engage with the institution through the national sections. The second is in cases in which the FTC is asked to interpret the agreement. Even at that moment, rather than reaching consensus on the meaning and intention of the cross-border rules as originally established in the agreement, in practice, trade ministers submit their own national governments' interpretation of the NAFTA provisions in question. The third is when the national governments themselves implement the final ruling in their own jurisdiction. As Kaufmann-Kohler puts it, "The difficulty here lies in the [three] hats worn by the States" (2011, p. 192), who act as gatekeepers, reviewers, and implementers of the cross-border rules.

Tribunals and even national governments themselves have undertaken one of the most crucial roles that Chapter 11 provides for regional institutions (specifically the FTC): interpreting the rules of the agreement when tribunals fail to understand the appropriate meaning of the text on which they are expected to deliberate (Article 1131). "In theory, if all three trade ministers agree that a NAFTA provision should be interpreted in a certain way, tribunals must obey them –no matter how far that interpretation may stray from the [originally intended] meaning of the text" (Grierson-Weiler, 2013). In practice, however, it is not expected that the trade ministers will interpret the provisions of Chapter 11 in a way that significantly differs from the position of their corresponding national governments. What is more, even when such interpretations have been essential to the arbitration of a dispute, the FTC has been sidelined (see

Metalclad v. Mexico and *Canadian Claimants v. United States* discussed below). For this reason, I argue that neither the Commission nor the Secretariat play any significant role in the arbitration of Chapter 11 disputes.

When it comes to arbitrations, Chapter 11 favors the use of multilateral mechanisms and international rules over regional ones. It also opts for the establishment of temporary tribunals and arbitral panels over the creation of a permanent adjudicatory body in charge of administering, ruling, and arbitrating on the operation and implementation of Chapter 11. Finally, it also puts the national governments in control of most of the arbitration procedure, thus leaving little opportunity for transnational actors or regional bodies and institutions –*ad hoc* or otherwise– to use, improve, and further the cross-border rules established by the chapter. Given the failure to establish regional institutions that can entirely manage the cross-border rules, the dispute resolution mechanism established by Chapter 11 has been used and engaged with less often than scholars and other observers originally expected.

To further support this argument, in the next section I analyze the outcomes of instances in which investors used Chapter 11 provisions to seek arbitration and solution to disputes arising from their operation and investments in other North American countries. I aim to demonstrate that the non-existence of *regional* rules on dispute arbitration, along with the aforementioned limitations of the regional bodies, have resulted in very limited use of the cross-border rules about the protection of FDI.[21] I review three cases where foreign investors have used the cross-border rules to denounce possible violations by the national governments of Chapter 11 provisions. As we will see, these arbitrations were largely unsuccessful for the investors, even in cases in which the national governments did pay claimants *some* compensation.

Metalclad v. the Government of Mexico And the State of San Luis Potosí (1996)

In the Metalclad case, a U.S. corporation filed a claim with the Mexican National Section against the government of Mexico and the state of San Luis Potosí. Metalclad argued that the national and state governments had violated Chapter 11 investor-protection provisions when they wrongfully refused to permit its subsidiary to open

[21] This statement does not imply that little FDI is being exchanged between the North American countries. It means instead that there is little engagement *with the rules* set by Chapter 11 for the protection of FDI, which might indicate that investors are either making strategic and carefully-planned investment decisions or resorting to dispute-resolution mechanisms other than those of Chapter 11 when investing in other North American countries, or doing both at the same time.

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and operate a toxic-waste management facility that the company had built in the country. In the claimant's view, the authorities' actions constituted a direct and indirect expropriation of Metalclad's investment, which was unlawful under NAFTA's Article 1120 and international law. The arbitration was undertaken under the provisions of the ICSID Additional Facility Rules.

The core of the dispute lay in the interpretation of the word "expropriation" in Article 1110, which states that no party may directly or indirectly nationalize or expropriate an investment (NAFTA Secretariat, 2014a). Metalclad argued that various actions of the municipal and state governments had permanently prevented it from operating the site, definitely cancelling any possibility of opening the industrial waste landfill it had built in Mexico. In the company's view, the local and state governments had thus taken measures *tantamount to* nationalization or expropriation of its investment. The local and state governments disputed this claim and argued that the company had not met the conditions to construct or operate the facility. In its position as respondent, the federal government stated that it was prepared to proceed on the assumption that the normal rule of state responsibility applies, that is, that it was responsible for the acts of all its three levels of government and thus prepared to compensate the claimant if the arbitration was successful (Perezcano Díaz, 1999, p. 46).

The tribunal was uncertain whether the actions taken by the state and municipal governments constituted an expropriation of the investment as provided in Chapter 11 and it required Article 1131 to be interpreted. Although Chapter 11 states the FTC should have been asked to do this, that did not happen. Instead the other two national governments not involved in the dispute, Canada and the U.S., provided their particular interpretation and agreed that Metalclad had incorrectly applied the term "expropriation" (Bettauer, 1999, p. 5; Escobar, 1999, p. 1).

The tribunal also asked for interpretation of Article 1102. This provision ensures national treatment will be accorded to foreign investors by *national governments*, but omits whether municipal-level governments are bound by its provisions. Given that the claimant filed its claim against the governments of Mexico and the state of San Luis Potosí for a failure of state and *municipal* governments to abide by Chapter 11 provisions, the tribunal was unsure whether Article 1102 applied to the case. However, the FTC was not called upon to interpret Chapter 11. The national governments took this task upon themselves. The U.S. government argued that the "natural meaning" of these provisions, taken together, is that the actions of local governments are subject to the provisions of Chapter 11. It also affirmed that "it believes [that this is what] the other Parties intended" (Bettauer, 1999, p. 2). Mexico agreed with this reading. Canada did not pronounce on the issue, but neither did it oppose the interpretations of the U.S. and Mexico.

The tribunal concluded that Mexico had violated the provisions of NAFTA's Chapter 11 by failing to ensure a transparent and predictable framework for Metalclad's investment. However, the tribunal did not totally side with Metalclad and deemed that the company had overestimated the cost of its losses and the damages incurred and only awarded a partial payment of the latter.[22] Soon after, however, the Mexican government challenged the decision and final award in its entirety before the Supreme Court of British Columbia. The court upheld the tribunal's decision for the most part, but conceded to Mexico on one key issue. The federal government argued that the tribunal had exceeded its jurisdiction when it incorrectly read and incorporated transparency requirements into Chapter 11, which were not present in the original text, and used this inadequate reading of NAFTA as a basis for the payment of damages (Faynblyum, 2013).[23] The partial success of this appeal led to a marginal reduction of the final award, which resulted in a payment of US$15.6 million from Mexico to Metalclad.

It cannot be said then that Chapter 11 provisions significantly altered the actions of Mexico's municipal, state, or federal governments. In the end, the municipal and state governments managed to stop the operation of the Metalclad facility, and the investor failed to recover most of its investment. Further, it can be affirmed that despite the unfavorable NAFTA tribunal ruling, Mexico's federal government prevented the NAFTA tribunals from expanding its commitments under Chapter 11, that is, the aforementioned transparency requirements. Furthermore, even if Metalclad was compensated for the loss of its investment, the award was far less than what the company had originally requested, and it is safe to say that the company was dissatisfied with the resolution of the arbitration and ensuing appeal. In this regard, Metalclad's chief financial officer, Anthony Dabbene, commented that Mexico actually won the arbitration inasmuch as "Chapter 11 can't hurt them as much anymore.... Our case has shown it is almost frivolous to pursue your rights" (2001, cited in Abray, 2001). In the Metalclad case, as in subsequent cases, rather than a remedy, Chapter 11 worked as an "end-game alternative, to which an investor turns when it has given up on the investment and simply wants to recoup as much of its losses as it can" (Dodge, 2013, p. 5).

[22] Metalclad had originally sought compensation in the amount of US$43 million (Pearce and Carvajal Isunza, 2001, pp. 5-6). However, the tribunal only awarded it around US$16.7 million in damages, less than half the alleged cost of its investment in San Luis Potosí.

[23] Such provisions were only contained in Chapter 18, which applies to disputes between national governments and not disputes between national governments and investors. Therefore, when the tribunal claimed that Mexico had failed to ensure a transparent and predictable framework for Metalclad's investment, it went beyond the provisions of Chapter 11. Given that Chapter 11 is an instrument that does not significantly rely on other parts of the agreement for its interpretation, application, or administration, and the Free Trade Commission is the only regional body able to revise and modify the provisions of the agreement, the tribunal was seen to have exceeded its powers.

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Canadian Claimants v. the United States (2005)

Between March and June 2005, 107 Canadian citizens and corporations in the live cattle sector in Canada filed an equal number of separate claims against the United States for banning imports of beef and cattle from Canada after the first case of bovine spongiform encephalopathy (BSE) in that country since 1993. The claimants alleged that the U.S. ban, in place between May 2003 and July 2005, had caused "great and unnecessary harm to their investment in the [North American] integrated market in beef and cattle" (Woods and Grierson-Weiler, 2005, p. 4).[24] In their view, by closing the U.S. border to Canadian products, the U.S. had violated the provisions of Chapter 11's Article 1102, which warrants national treatment to North American investors in the territories of other NAFTA parties.

The ban was aimed at reducing the risk of transferring diseases to and contaminating the U.S. food chain. However, the claimants alleged that there was no scientific or evidence-based rationale for prohibiting the entry of livestock from Canada (Woods and Grierson-Weiler, 2007, pp. 5-6).[25] In the claimants' view, these actions (and the lack of any comparable restrictions on exportation of U.S. live cattle to Canada) suggested that the underlying intention of the U.S. federal government had not been preventing and containing BSE, but establishing a dominant position for U.S. investors in the so-called North American market. According to the claimants, by closing the border to Canadian trade, the U.S. had acted in an arbitrary and protectionist manner in favor of U.S. investors, which constituted a violation "in spirit, and in fact, of NAFTA" (Friesen, 2004). In August 2006, having negotiated with the claimants, the U.S. National Section accepted the claims and announced that they would be consolidated into a single case to be arbitrated by a NAFTA tribunal.[26]

From the beginning, the U.S. alleged that Chapter 11 provisions did not apply to this case. In its view, the claimants had not made, were not making, and did not seek to make investments in the territory of the United States (as defined by Chapter 11 Article 1139). Instead, the alleged "investments" had been made in Canadian terri-

[24] Whenever possible, the discussion of these cases is based on the public documents made available by the national sections and the NAFTA Secretariat rather than scholarly commentaries about them. The sources are referenced as such after the names of the counsels of the parties that presented these claims or subsequent rejoinders, or the members of the arbitral panel that ruled on these cases. Therefore, these sources do not express or reflect the views of individuals, but their positions as claimants, respondents, or members of arbitral panels.

[25] For instance, they argued that the U.S. Department of Agriculture and the World Organization on Animal Health had both determined that Canadian livestock posed minimal risk to the U.S. food industry and consumers.

[26] As a result of this negotiation, the various cases were consolidated into a larger case named *Canadian Cattlemen for Fair Trade v. United States of America*.

tory by Canadian citizens and corporations. Given that the U.S. had no obligation under NAFTA with respect to investments made in the investors' own country, a NAFTA tribunal had no jurisdiction to arbitrate this dispute, and the claims should be dismissed in their entirety. The claimants alleged that they had indeed invested in the "North American market," since the aim of NAFTA is to foster investment opportunities in North America through the creation of a continental market protected against discrimination and unfair measures "regardless of where the investment is located" (Woods and Grierson-Weiler, 2007, p. 13). Therefore, even if their investments had been made in Canada, they should be considered investors in the "North American free trade area" in terms of the object and purpose of Chapter 11.

According to the U.S., the claimants had misinterpreted and/or were attempting to distort the provisions and objectives of Chapter 11 by overlooking its nature as a legal instrument that sets down rules governing investments by North American nationals *in the territories of other NAFTA countries*. The claimants' interpretation of Chapter 11 constituted, then, a "radical departure" from what the national governments had negotiated, agreed upon, and committed to through NAFTA (Clodfelter, Menaker, and Benes, 2006, p. 3). Finally, the U.S. government argued that any other reading of Chapter 11, different to those that the national governments had intended, would lead to "absurd" results.[27]

In light of these differing interpretations of the definition of "investor," the parties agreed that the tribunal should first determine whether it had jurisdiction over the consolidated case before arbitrating it. The issue at the core of the dispute was whether an actor that produces and distributes products for the North American "free trade area" can be considered a foreign investor, even if they are investing in their own territories (Böckstiegel, 2006, p. 4). On October 2007, the NAFTA tribunal held hearings on this issue with the U.S., Canadian, and Mexican national governments to determine what the correct interpretation of the term "investor" in Article 1139 was. Canada did not pronounce on the issue (Woods, Harrison, Lalonde, et al., 2007, p. 8). These actions were contrary to the provisions of NAFTA, which establishes that only the Free Trade Commission (FTC) shall resolve disputes arising from the interpretation or application of the agreement and that all decisions of the commission shall be made by consensus.

[27] For instance, allowing "every national of a NAFTA Party that believes its business has been adversely affected by a border measure of another [Party to be considered as] an 'investor' entitled to invoke Chapter 11's dispute resolution procedures" (Clodfelter, Menaker, and Benes, 2006, p. 3). The U.S. government argued that in previous arbitrations, Canada and Mexico had concurred that the provisions of Chapter 11 only applied to investors that have made or are seeking to make investments in the territory of the disputing party. Therefore, Chapter 11 was not intended to protect the property of national investors inside their own countries.

These violations of the cross-border rules did not go unnoticed. The claimants declared that they were "well-aware" that NAFTA established that the FTC had to deliberate and agree upon the interpretation of the agreement and that the regional institution had neither been consulted nor provided such an interpretation (Woods and Grierson-Weiler, 2007, p. 45). The U.S. acknowledged that the FTC had not been asked to make an interpretation of the agreement. Yet, it argued that it was wrong to suggest that the FTC is the only means by which the national governments may interpret their agreement. In their view, the national governments can, and routinely do, interpret the treaty "in many ways [and not only through the FTC, thus] the suggestion that a particular formality is required for there to be an agreement among NAFTA Parties is incorrect" (Clodfelter, Menaker, Sharpe, et al., 2007, p. 14).[28] The tribunal and the national governments therefore transgressed Chapter 11 rules by adopting the U.S. and Mexican interpretations of Article 1139, foregoing the lack of an interpretation by Canada and failing to formally request that interpretation from the FTC.

Contrary to the provisions of NAFTA, the tribunal took upon itself the task of interpreting Chapter 11, and in January 2008, it issued its final ruling on the case. Based on its own interpretation, it determined that there was *insufficient* evidence to demonstrate the existence of an agreement between the parties regarding the interpretation of NAFTA or the application of its provisions. In other words, it acknowledged the lack of a formal interpretation by the Free Trade Commission. However, it argued that a "practice" exists in the application of Article 1139 and that that practice established how NAFTA should be interpreted and applied. It concluded "that some [past] decisions provide support to the interpretation *the present Tribunal* has chosen" (Böckstiegel, Bacchus, and Low, 2008, p. 120). Given that all the claimants' investments were located in Canada and the claimants did not seek to make, were not making, and had not made any investments in the United States, the dispute could not be arbitrated under Chapter 11, and that the tribunal did not have jurisdiction to consider the claims for the alleged breach of the rules. Having determined this, it dismissed all the claims against the United States.

Vito G. Gallo v. Canada (2007)

The *Gallo v. Canada* case resembles the Metalclad case inasmuch as what gave rise to the dispute were not the actions of the Canadian federal government, but those of

[28] The U.S. further argued that "more than anyone [that is, foreign investors or regional institutions], the parties to the treaty are best situated to understand the sense of the treaty that they concluded and what they truly intended" (Yasseen, 1976 cited in Clodfelter, Menaker, Sharpe, et al., 2007, p. 13).

the province of Ontario. According to the claimant, Vito G. Gallo, a U.S. citizen, the dispute arose from the passage of the Adams Mine Lake Act on April 2004 by the aforementioned provincial government.

In his view, passing the act into law constituted an expropriation or a measure tantamount to expropriation of his investment in Canada. He argued that the act denied him and his company access to courts to ensure the payment of adequate compensation for the expropriation of the Adams Mine, a site that he had allegedly purchased in 2002 as the sole shareholder of Ontario Inc.[29] This enterprise had been established with the sole purpose of owning, controlling, and operating the mine as a landfill. However, when the public and various Canadian non-governmental organizations opposed the project, claiming that the potential for contamination resulting from the plant's operation would be too high, the Legislative Assembly of Ontario introduced the Adams Mine Lake Act, which revoked all permits related to the mine and prohibited any person from disposing of waste at the site, an action which purportedly put the firm out of business by reducing the site's value to nil or even negative (Gallo and Swanick, 2007, p. 18) The dispute, however, did not arise from the expropriation itself, but from the proposed amount that the investor would receive as compensation.[30] As a result of this disagreement, on October 2006, Gallo filed a notice of intent to submit a claim to arbitration against Canada for breaching its obligations under Chapter 11 Articles 1105 and 1110.[31]

Gallo filed the notice of arbitration for the case requesting the establishment of a tribunal to arbitrate the dispute under UNCITRAL rules. He further claimed that a NAFTA tribunal had jurisdiction to hear the case inasmuch as he and his company fulfilled the requirements for being considered a foreign investor and foreign investment, respectively. In principle, these circumstances made the case admissible for arbitration.[32] Nonetheless, the tribunal determined that the acceptance of a claim for

[29] The actual name of the company was 1532392 Ontario Inc. In this article, however, I refer to it only as Ontario Inc.

[30] The act declared that nothing in it constituted an expropriation or detrimental action, and consequently any cause of legal action against the province of Ontario was inadmissible. However, it granted Ontario Inc. an undisclosed amount as compensation for its loss of the site, but not for the loss of possible profit (that is, the gains that the company expected to make as a result of its operation) (Fernández Armesto, Castel, and Lévy, 2011, p. 51). After the act was enacted in June 2004, Ontario Inc. negotiated with the province in an effort to raise the amount of the compensation to include payment for the loss of possible profit, but no agreement was reached.

[31] Specifically, Gallo claimed that, by enacting the Adams Mine Lake Act, Canada had failed to afford him fair and equitable treatment as a foreign investor and full protection and security for his investment as provided by NAFTA and international law, thus breaching Chapter 11's provisions on minimum standard of treatment and expropriation and compensation. He sought US$355 million in damages from the Canadian government.

[32] It is important to highlight here the role of the legal counselors, who have made a regular practice of confirming the possible jurisdiction of a NAFTA tribunal, to prevent incidents such as that of *Canadian Claimants v.*

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arbitration required that the claimant provide *convincing* evidence to prove its case. The tribunal considered that its first task was "weighing the evidence regarding the factual record to establish to what extent the facts actually happened as [Gallo] is now averring they did" (Fernández Armesto, Castel, and Lévy, 2011, p. 53). This decision was innovative in terms of institutional action, as it implied that the tribunal would examine the plausibility of the facts alleged by disputing parties (and especially the claimant's), rather than simply assuming their veracity. The tribunal, therefore, *de facto* expanded its responsibilities from arbitrator to inquirer, adopting a quasi-judicial function that went beyond the original provisions of Chapter 11.

The tribunal issued multiple procedural orders, amendments, and guidelines aimed at clarifying and organizing the evidence presented by Gallo. Yet it eventually determined that Gallo's factual record "was full of unusual circumstances and outright mistakes," which did not clarify how he had acquired, financed, and managed the Adams Mine site (Fernández Armesto, Castel, and Lévy, 2011, p. 54). Based on the inquest, the tribunal determined that the evidence available suggested that Gallo, in conjunction with Canadian real estate developer Mario Cortellucci, had attempted to commit fraud against the province of Ontario and Canada.[33] However, the tribunal did not assert that the claimant had acted fraudulently. In the end, it did not attempt to pursue a criminal case against the claimant, only determining whether it had jurisdiction to arbitrate the dispute. In light of its findings, in September 2011, the tribunal determined that it had no jurisdiction to consider Vito G. Gallo's claims, dismissed the case, and ordered Gallo to pay US$450 000 to Canada to cover the costs of the arbitration.

Based on the outcome of the case, I argue that the tribunal acted in the interests of the national government of Canada and declined to advance the interests of the claimant. To do so, it furthered its own powers without necessarily altering the cross-border rules. It assumed an investigative function, in a manner closer to the responsibilities of domestic courts, rather than solely arbitrating the dispute. In doing so, it exerted a quasi-judicial function that NAFTA had not stipulated. The tribunal over-

United States. By using, applying, and interpreting Chapter 11 provisions, counselors have gained experience and knowledge about the rules and have carried this accumulated understanding on to their following cases. For instance, Todd J. Grierson-Weiler, one of the counselors to the claimant in *Gallo v. Canada*, had also been counselor in *Canadian Cattlemen for Fair Trade v. United States of America*. This experience, however, did not translate into increased success in ensuing Chapter 11 arbitrations. This example provides further support for the argument that an analysis of the current institutional framework provides a better basis for explaining the outcome of these cases than the expertise of claimants and their counselors.

[33] From the documents released by the tribunal, it can be inferred that Gallo and Cortellucci appeared to have entered into an oral agreement to make the former appear as the owner of Ontario Inc. before a NAFTA tribunal to file a claim for arbitration against Canada under the provisions of Chapter 11, in return for a share of the compensation sought.

stepped its responsibilities as an arbitrator and turned into an investigator, greatly in favor of the respondent. By taking this stance, it set a clear "line between foreign and domestic investors [that] needs to be respected. [That is, the] privileges conferred to the former are not to be abused by the latter" (Farber and Martin, 2012, p. 3). In the view of the tribunal, the claimant had attempted to use Chapter 11 provisions to sidestep domestic legislation by portraying himself as a foreign investor whose investment had been damaged.

The decision thus showed that NAFTA tribunals "will not put up with attempts by domestic investors to manufacture a NAFTA challenge" (Gray, 2011). The tribunal itself acknowledged this position in its final award. It claimed that "the case at hand is an excellent example of the tension between claimant's requests to expand treaty protection . . . and the Tribunal's obligation to apply the treaty on the terms and with the subjective scope agreed between NAFTA contracting parties" (Fernández Armesto, Castel, and Lévy, 2011, p. 66). Given that Chapter 11 arbitration cases rely on an *ad hoc* ruling, the expanded functions of the tribunal came to an end. However, its performance in the case indicates that the development of regional bodies does not necessarily go against the interest of the nation-state. To the contrary, in this case, it furthered them by signaling to "U.S. or Mexican investors who decide to take Canada to court under NAFTA [to] think twice" about the legal and financial consequences of their challenges under Chapter 11 (Gray, 2011).

The Limited Use of the Cross-border Rules

Chapter 11 rules, including the actions of the regional institutions and bodies that it created, have done relatively little to advance the rights and protection that North American investors are afforded with respect to their investments in other North American countries. More importantly, these rules and institutions have not contributed significantly to the expansion or consolidation of the cross-border rules on the protection of FDI. So far, the Chapter 11 institutions (the Free Trade Commission and NAFTA Secretariat) and its *ad hoc* and temporary bodies (the panels and arbitral tribunals) have largely represented or incorporated the interests of the national governments. On a number of occasions, the national governments have transgressed or side-lined the rules of Chapter 11, both individually, as defendants in a dispute, and jointly, as interpreters of the cross-border rules in lieu of the FTC.

Foreign investors have acknowledged the impediments and challenges associated with filing claims under Chapter 11. The uncertainty, expenses, and extended duration of NAFTA tribunal arbitrations have deterred would-be users of these rules. What

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is more, in the few cases that transnational actors have used its provisions, the outcome has mostly been patently adverse. As of 2014, out of the 33 claims filed against the three North American governments combined, and whose cases had already been accepted, arbitrated, and closed, only 8 were successful for the claimants. Two out of every three times that a foreign investor has proceeded with arbitration against a North American government, the outcome has been unfavorable to them. In almost one out of every five times, going into an arbitration against a North American government has resulted in further losses to the individuals or firms involved, due to a tribunal decision to award compensation for arbitration costs to the national governments. In most cases, foreign investors would have incurred lower monetary losses if they had not used the Chapter 11 provisions.

Even when the outcome has been favorable to them, claimants have expressed their dissatisfaction with the tribunal decisions.[34] Given the remedial nature of Chapter 11 disputes, the claim that foreign companies flagrantly and frequently abuse Chapter 11 to overturn domestic legislation is exaggerated at best (Hufbauer and Goodrich, 2004, p. 47; see *Apotex Holdings Inc. and Apotex Inc. v. United States*). On the contrary, when foreign investors have attempted to use Chapter 11 to overturn legislation aimed at protecting the public interest, the tribunals have sided with the national and sub-national governments (see *Glamis Gold Ltd. v. United States*).[35]

Due to these conditions, only a very small number of transnational actors have engaged with Chapter 11. As of 2014, only 43 claims had been filed and accepted for arbitration against the three NAFTA countries, most of them against Canada, followed by the U.S. and Mexico, in that order (DFATD, 2013; Secretaría de Economía, 2013; U.S. Department of State, 2013).[36] That is fewer than two claims filed per year against any

[34] For instance, Barry Appleton, counsel to Ethyl Corporation in its case against Canada, dismissed concerns about the potential use of the agreement as a mechanism to weaken domestic laws. In his view, such “claims are ludicrous [because] NAFTA doesn’t strike down laws; it awards damages” (2000, cited in Valance, 2000).

[35] *Glamis Gold v. the United States* provides further evidence that when the instrument has been used to challenge the decisions of national and sub-national governments, more often than not, the outcome has been favorable for governmental and even non-governmental actors pursuing the protection of the public interest. In this case, Glamis Gold, a Canadian mining company, filed a claim for arbitration for an alleged breach of the U.S. obligations under Chapter 11 when the U.S. federal and California governments prevented it from mining in an area that was “near to, although not part of, Native American lands and areas of special cultural concern” (Young, Caron, and Hubbard, 2009). As part of the procedure, the tribunal accepted *amicus curiae* submissions, which are neither prohibited nor provided for in the text of Chapter 11, from relevant stakeholders, namely the Tribal Council of the Quechan Indian Nation, and the non-governmental organizations Friends of the Earth, Sierra Club, and Earthworks. The tribunal took into account these submissions when it issued its final decision, dismissing all claims against the United States, and upholding the governments’ decisions to protect the environmental and cultural value of the nearby areas, which might have been subject to damage due to mining activity.

[36] Although data from Canada and Mexico indicates that foreign investors have made other attempts to file claims against these governments, the figures are not significantly higher. Until 2014, 15 letters indicating the intention to file a claim had been addressed to Canada. Six of those have already been withdrawn, and

of the three North American governments. Furthermore, while from 1990 to 2011, FDI flows multiplied tenfold, in the same period the number of Chapter 11 claims fell to zero (Farías Pelcastre, 2014).[37] This is because, overall, Chapter 11 rules remain burdensome and unclear for foreign investors, the group allegedly favored by its rules. It could be argued that this outcome could be result of a better and greater understanding and awareness from national governments on the rights of foreign investors and/or the foreign investors on the circumstances still limiting the making of cross-border investments. However, this is very unlikely in a context marked by a ten-fold increase in foreign direct investment.

Instead, this lack of engagement with Chapter 11 is due to the weakness of the institutional structure put in place by the agreement and the inherent bias of its dispute settlement mechanisms toward national and sub-national governments. Contrary to commonly held views, the "NAFTA arbitration panels are composed of seasoned experts in international law," who are not easily convinced that a party has breached its obligations under NAFTA (Herman, 2011). As Brower and Steven argue, "The arbitrators participating in [Chapter 11] cases are highly competent members of academia and the international bar, with experience and expertise in the relevant areas of law exceeding that of the vast majority of the domestic judiciary in each of the three NAFTA countries, [and whose decisions have largely] rendered in the State Respondent's favor" (Brower and Steven, 2001, pp. 200-201). What is more, when tribunals have assumed the responsibility of the FTC in interpreting Chapter 11 articles (which goes against the agreement's provisions), most times that interpretation has been favorable to governmental actors (for instance, see *Fireman's Fund Insurance Company v. Mexico*). As can be seen in the cases analyzed above, the tribunals have consistently favored and upheld the actions and decisions of national and sub-national governments that have been the subject of Chapter 11 arbitrations.

the other nine remain inactive. Yet, because none of this resulted in a formal notice of arbitration, they do not constitute claims and therefore are not included in the figures for Canada (DFATD, 2013). Similarly, as of 2014, four notices of intent had been served to Mexico. However, none of them has resulted in a formal notice of arbitration. One notice of arbitration against Mexico remained inactive and unlikely to be accepted for arbitration (Secretaría de Economía, 2013).

[37] This regional trend seems to be consistent with that at the global level where increasing investment flows "do not appear to correlate to the absence of multilateral rules on investment" (Kurtz, 2002). In other words, increased flows of foreign investment do not necessarily result in increased claims for arbitration.

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Conclusions

As I indicated by the three cases above, Chapter 11 rules and the regional institutions and bodies that it created have done relatively little to advance the would-be rights and protection that North American investors are afforded with respect to their investments in other North American countries. Contrary to commonly held views, despite being one of the most detailed set of rules established by NAFTA, Chapter 11 created one of the agreement's weakest institutional frameworks for upholding and enforcing those rules. At first glance, this seems paradoxical.

According to a number of scholars, Chapter 11 was intended to suit the needs of a very specific type of transnational actor in North America: foreign investors. Yet, to date, only a limited number of such actors have engaged with and made use of the cross-border rules established by Chapter 11. Compared to the side agreements on the environment and labor, which have fostered cross-border exchanges, created and improved cross-border rules, and even expanded and strengthened its corresponding regional institutions (see Farías Pelcastre, 2014), Chapter 11 sets out a number of rules that are scarcely used by transnational actors and, when used, have largely favored the national governments. As of 2014, out of 11 cases against Canada that had already been accepted, arbitrated, and closed, only 3 were successful for the claimants and resulted in total or partial payment of damages. Out of the 12 cases against Mexico already accepted, arbitrated, and closed, only 5 were successful for the claimants and resulted in payment of damages. Out of 10 claims filed against the U.S., none has been successful for the claimants.

In conclusion, Chapter 11 did create cross-border rules that *closely* resemble a right for transnational actors –individuals and firms alike– to challenge governmental actors before a quasi-regional tribunal without the assistance of their home country's government. It also enabled them to receive compensation for the *effects* of inadequate action of NAFTA governments. However, it did not create regional institutions that can translate those disputes into significant challenges to the power of national or sub-national governments to legislate on social-oriented policy issues or create more effective and better cross-border rules on protection of foreign direct investment for future use. All things considered, the scope and power of Chapter 11 rules and mechanisms are quite limited. And, contrary to common views, its quasi-regional bodies –that is, the Arbitral Panels and Tribunals– have contributed to limit the use of cross-border rules and protect the public interest by upholding the decisions and actions of national and sub-national governments in North America, and hence their ability to protect public welfare.

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