Withdrawing Canada from the treaty-based international investment arbitration system

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April 21, 2021

A brief submitted to the Standing Committee on International Trade regarding its study of investor–state dispute settlement mechanisms: selected impacts.

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On behalf of the Canadian Centre for Policy Alternatives (CCPA), I'd like to thank the Standing Committee for this opportunity to provide feedback into its study of the impacts and future of investor–state dispute settlement (ISDS) in Canada.

I have been researching the ISDS regime for more than two decades as Founding Director of the CCPA's Trade and Investment Research Project. My comments here draw from my most recent report, *The Rise and Demise of NAFTA Chapter 11*, which is freely available from the CCPA website at this link (hyperlinked).[1]

The removal of ISDS from the renegotiated NAFTA was a critical victory for democratic sovereignty over investor power. Within three years, the Canada–U.S.–Mexico Agreement (CUSMA) will eliminate ISDS between Canada and the United States and significantly scale it back between the U.S. and Mexico.

At the conclusion of the CUSMA negotiations in October 2018, Chrystia Freeland, then foreign affairs minister, described the elimination of ISDS as a proud achievement of the government. "ISDS elevates the rights of corporations over those of sovereign governments. In removing it, we have strengthened our government's right to regulate in the public interest, to protect public health and the environment," she said.

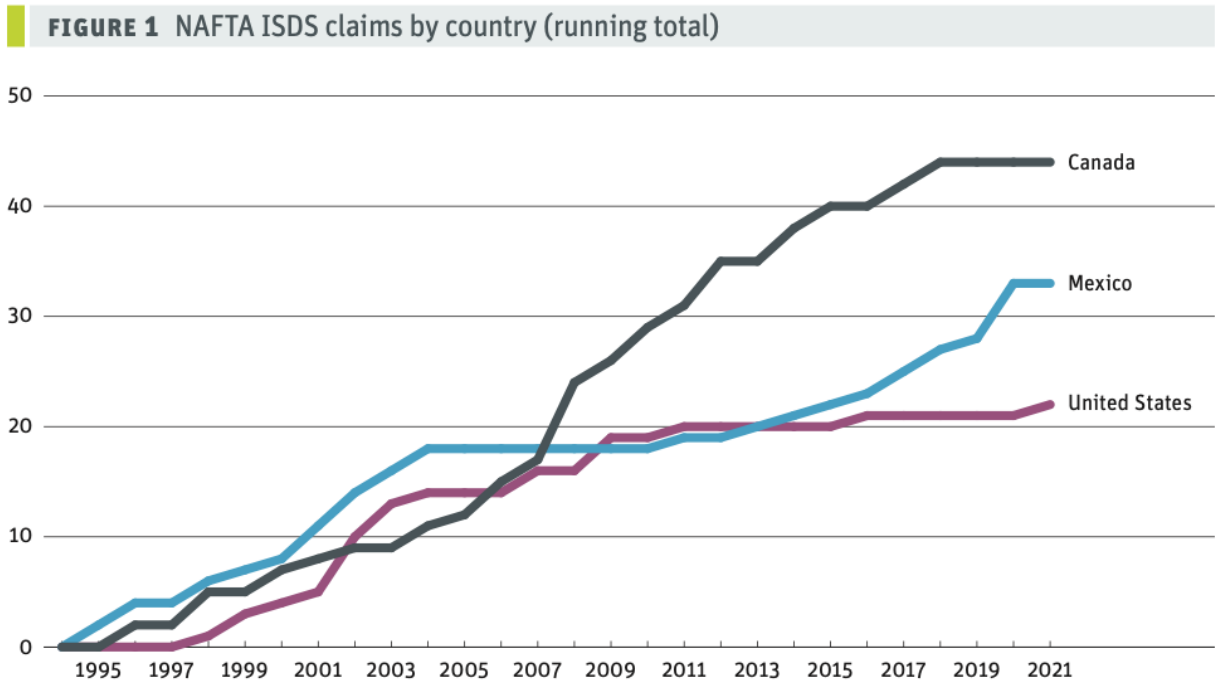
Investor–state dispute settlement clauses in international trade and investment treaties allow foreign investors to bypass the domestic courts and sue governments directly before private international arbitration tribunals. Prior to NAFTA, ISDS had been a feature of bilateral treaties between developed and developing countries, but the signing of the North American treaty marked the first time that investment arbitration was part of a comprehensive regional trade agreement. Since then, more than 3,000 bilateral and regional treaties have been signed that include an ISDS system.

[1] Footnotes and citations in the report are omitted from this brief.

Under ISDS rules, arbitration can be invoked unilaterally by foreign investors, who do not need to seek consent from their home governments and are not obliged to try to resolve a complaint through the domestic court system before launching a claim. Under NAFTA Chapter 11, for example, Canada, the U.S. and Mexico consent to submit investor claims to binding arbitration, allowing investors to forego using the domestic courts altogether.

While national governments alone are responsible for defending ISDS cases, government measures at the federal, provincial, state and local levels can and frequently have been targeted by investors. Cases are decided by tribunals of three members: one chosen by the investor, one chosen by the challenged government, and a third selected by mutual agreement. Tribunal decisions are final and not appealable on their merits in national courts.

Investors can challenge not only discriminatory actions by governments but even non-discriminatory policies they allege are unfair or frustrate their legitimate (in the opinion of the arbitrators) expectations of profit. In fact, NAFTA Article 1105, which enables investors to challenge non-discriminatory measures that allegedly fall short of minimum standards of treatment under customary international law, has been invoked by investors in over 90% of NAFTA claims (see table of disputes in my report, *The Rise and Demise of NAFTA Chapter 11*).



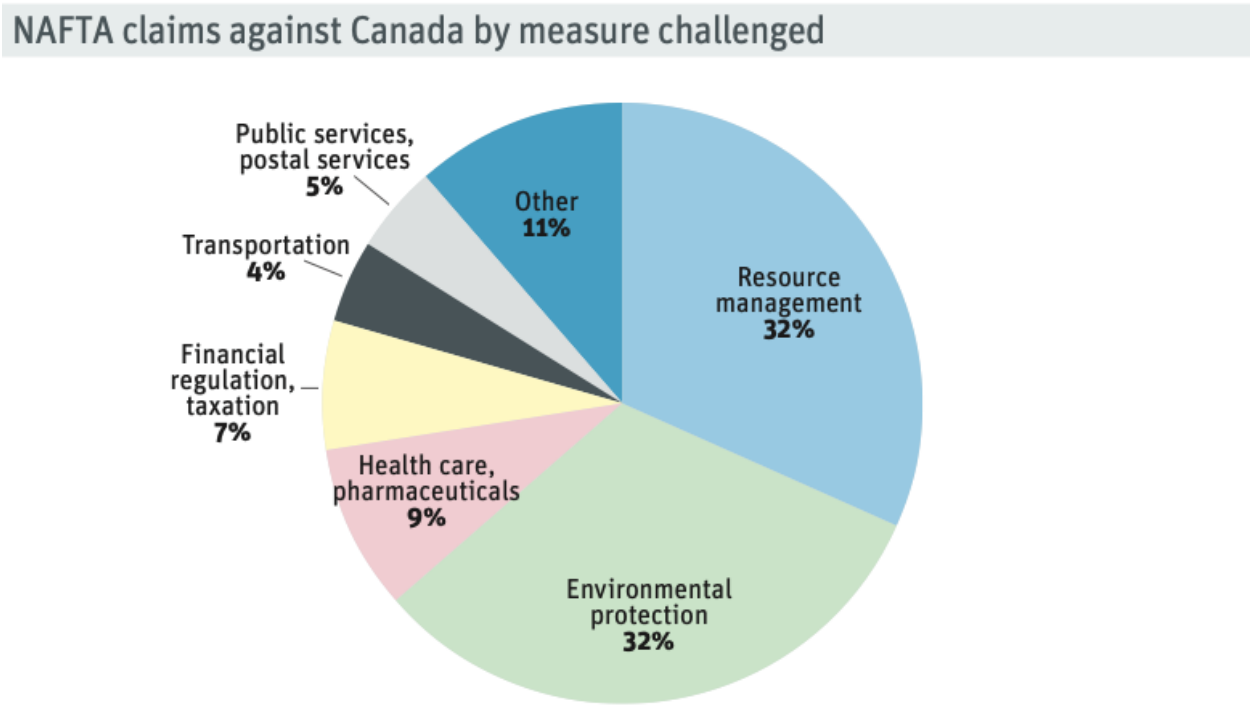
Source for graph: *The Rise and Demise of NAFTA Chapter 11*, by Scott Sinclair (CCPA).

Canada remains the principal target of foreign investors under NAFTA Chapter 11 (see Figure 1, above). It has now been sued 44 times. The number of known claims against Mexico has recently risen sharply, but at 33 still falls short of Canada's share. Despite its size and economic might, there have only been 22 claims against the U.S.

To date, Canada has lost or settled (with compensation) 10 claims. Canadian governments have paid out more than $263 million in damages and settlements. In addition, Canada has incurred more than $113 million in unrecoverable legal costs (up to March 2020), according to data acquired through an access-to-information request. These figures do not include added interest on payments to investors, which typically accrue from the date the alleged NAFTA violation occurred.

Environmental measures frequently targeted

But the damage done by NAFTA Chapter 11 goes beyond the sums of money extracted from Canadian taxpayers. The worst consequence was empowering foreign-owned corporations to use a private justice system to challenge vital and legitimate public policy measures. Environmental protection and natural resource management measures have been a favoured target, accounting for more than 60% of the claims against Canada (see figure below).



Source for figure: *The Rise and Demise of NAFTA Chapter 11*, by Scott Sinclair (CCPA).

Canada and the U.S. began to correct a great injustice when they agreed to remove investor–state dispute settlement from the new NAFTA. This step significantly reduces both countries' vulnerability to investor–state disputes. All but one of the 44 claims against Canada under

NAFTA Chapter 11 have been brought by U.S. investors. Likewise, Canadian investors have been responsible for 20 of the 22 claims against the U.S.

Getting rid of ISDS was also a remarkable victory for the social movements who have tirelessly campaigned against it, and the legal experts whose critical opinions of ISDS have fundamentally weakened any case in support of it. Going forward, the repudiation of ISDS in CUSMA will greatly decrease the deterrent or chilling effect of ISDS on government policy initiatives, at least in Canada and the U.S. This is critical, especially as citizens and social movements insist that North American governments take bold actions to address climate change and economic injustice.

Of course, the substantive obligations in CUSMA's investment protection chapter will still apply and can be enforced through state-to-state dispute settlement. These strictures may therefore continue to cramp the policy space of elected governments hoping to introduce measures, such as Green New Deal policies, that go against powerful corporate interests. But since enforcing these rules is now discretionary, we can expect this weapon to be employed more sparingly than ISDS, especially if all three countries are moving in the same policy direction.

There is still a long way to go to fully eliminate the threats from ISDS, both at home and abroad. Despite Minister Freeland's strong criticism of ISDS when CUSMA was signed, the Canadian government is enmeshed in an extensive web of bilateral and regional accords containing ISDS. The largest is the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), in which a NAFTA-style ISDS system covers major capital exporters such as Japan and Australia. The United Kingdom, Canada's third largest source of foreign direct investment after the U.S. and the European Union, has expressed interest in joining the CPTPP.

Canada has comprehensive trade agreements with South Korea, Chile, Colombia, and some other smaller countries, that include ISDS. In addition, Canada has 38 Foreign Investment Promotion and Protection Agreements (FIPAs) in force, the most significant of which is the Canada–China FIPA. Most of these bilateral treaties contain some form of ISDS.

The Canada–Moldova FIPA was signed on June 12, 2018, during the CUSMA talks, and entered into force on August 23, 2019. Canadian officials are also pursuing an ISDS chapter in the planned, but stalled, free trade deal with the Mercosur trading bloc (Brazil, Argentina, Uruguay and Paraguay), and they appear ready to include some form of ISDS in looming negotiations with the U.K., Ukraine and Indonesia.

Under questioning from NDP trade critic Daniel Blaikie at the House of Commons trade committee, a senior Canadian trade official testified that, "the investment chapter outcome that we have in the CUSMA is really a reflection of the unique North American context. While under CUSMA we don't have ISDS with the U.S., we still maintain ISDS with Mexico under the CPTPP." Summing up, the official emphasized that "Canada maintains the flexibility to negotiate variable outcomes with respect to our various partners on ISDS, and we would determine whether or not we would be seeking ISDS on a case-by-case basis."

Canadian investors, especially from the mining and energy sectors, are aggressive users of ISDS against other governments. Under the Canada– Colombia FTA, for example, three Canadian mining firms are suing the Colombian government because of measures to ban mining in the *páramo*, environmentally sensitive alpine wetlands that provide over 70% of the country's water supply.

Such attacks against public interest and environmental protection regulations are a stain on Canada's international reputation and undermine environmental protection efforts that benefit the global community. For such reasons, and as Canada's own experience under NAFTA Chapter 11 underscores, it is highly desirable to end the threat that ISDS poses to the public interest nationally and globally.

Recommendations

While there is clearly much work to be done to pressure the Canadian government to abandon its support for ISDS, Osgoode Hall Law School professor Gus Van Harten, one of Canada's and the world's foremost experts on ISDS, wisely counsels the government to "adopt the perspective of quiet determination to withdraw from its ISDS risks and costs where possible and whenever possible."

It will take time to unravel the tangled knot of agreements containing ISDS. But it is a worthwhile effort that can be accomplished. Other democracies, notably South Africa, have shown how it can be done.

Canada should take the following steps to phase out ISDS:

1. Don't include ISDS in any future agreements or ratify pending agreements that contain ISDS.

2. Communicate to all Canadian FIPA partner countries Canada's willingness to renegotiate based on a new template that does not include ISDS.

3. For those countries who don't agree to renegotiate, withdraw from the FIPA as soon as possible, by giving notice of termination under the terms of those agreements (including the Canada–China FIPA).

4. Similarly, for Canada's bilateral free trade agreements, offer partners the opportunity to renegotiate the investment provisions based on a new model that does not include ISDS. Such provisions were typically included at Canada's insistence, and current or future governments in Colombia, Chile, or South Korea can reasonably be expected to grasp this opportunity.

5. Following the CUSMA example, seek to renegotiate regional trade agreements to remove ISDS. The CPTPP will pose a significant, long- term challenge in this regard. But right away, Canada can follow the example of participants such as New Zealand and negotiate bilateral side letters, or understandings, that neither party consents to ISDS proceedings involving the other.

6. If the U.K. wishes to accede to the CPTPP, Canada should insist on a side letter disavowing ISDS between the two jurisdictions and should not agree to ISDS in any bilateral Canada-U.K. trade and investment pact.

7. Canada should communicate to the EU and its member countries that it no longer supports CETA's proposed, but still unratified, Investment Court System, and that its position is that these provisions should never be implemented.

As Van Harten noted in his recent testimony before this committee, such a project would likely take a generation to complete. But many of these steps could be taken right away and would bear immediate fruit in reducing the risks and costs, both economic and social, associated with ISDS.

Finally, it is a customary principle of international law, codified in the Vienna Convention on the Law of Treaties, that subsequent treaties among the same parties and dealing with the same subject matter take priority over previous ones. Earlier treaties can only be applied to the extent that they are compatible with later ones. It is therefore possible that rather than having to undo investment protection treaties one by one, a provision inserted in a future United Nations treaty or global climate change accord could neuter ISDS challenges among the signatories with a single stroke of the pen.

There are other reasons to be hopeful. U.S. sponsorship was pivotal to the proliferation of ISDS. Just as the early NAFTA Chapter 11 cases turbocharged the ISDS regime in North America and globally, its undoing in USMCA might animate the reverse process of dismantling the system. In Europe, there is anger over lawsuits from investors demanding massive compensation for the phasing out of fossil fuels. In the Global South, dozens of countries, large and small, have chosen to extricate themselves from damaging investment treaties.

While it will not be an easy task, the prospects for dismantling ISDS are better today than ever. We urge the committee to recommend strongly that Canada continue the process of eliminating ISDS from all its international agreements.