SCHOLARS
STRATEGY NETWORK

How Dispute Resolution Provisions in International Trade Pacts Threaten Democracy and the Rule of Law

Mark Barenberg, Columbia University
Peter Evans, University of California-Berkeley

Currently, America's political elites, lobbyists, and corporate insiders are negotiating major new international trade agreements – the Trans-Pacific Partnership and the Transatlantic Trade and Investment Partnership. Much of the discussion is proceeding in secret, even though all Americans have a stake in the outcome. In fact, international trade agreements are about much more than trade alone, because they establish a set of binding rules that affect investments, labor rights, environmental regulations and many other areas of governance in all of the countries that sign on to them. In addition to affecting economic winners and losers, these pacts also go to the heart of democratic sovereignty and governance by establishing dispute resolution procedures binding on all involved nations and their citizens.

Because pacts are negotiated far from public view, ordinary citizens and even their elected representatives often are barred from seeing the terms until it is effectively too late to debate and revise them. To uncover what may again be secretly in store, we focus on provisions for "Investor-State Dispute Settlement" included in earlier investment treaties and in such trade pacts as the 1994 North American Free Trade Agreement.

Who is Protected by Dispute Provisions in Trade Pacts?

Previous Investor-State Dispute Settlement provisions grant private investors special – and highly unusual – legal protections in the communities where they invest and in relation to the local, state, and national governments representing and governing those communities. International negotiators say they want companies to enjoy the same legal treatment regardless of where their owners live. That sounds fair enough, but the ambiguous definition of "equal treatment" leads in practice to extraordinary protections for investors, as the following principles and processes from previous trade pacts suggest:

- Previous provisions say that foreign corporations cannot be expropriated "directly or indirectly" or subjected to any measures that would be "tantamount to expropriation." Tribunals handling disputes can consider whether a local law diminished an investing company's reasonably expected gains in imports, exports, or market share. Thus, in a case brought under the North American Free Trade Agreement, a tribunal ruled in favor of a company denied a municipal permit to construct a hazardous waste landfill. Although the local government relied on studies showing that the landfill would harm the environment, the tribunal accepted the investor's claim that the permit should have been granted as a matter of course, because officials outside the municipality had said so.

- Investor-state dispute provisions typical in international trade pacts not only authorize foreign companies to claim compensation for losses they say are imposed by the democratically devised rules

of host countries; in addition, the investor companies can have their claims adjudicated outside of established legal systems. As illustrated in the landfill case just described, if a foreign company thinks that some U.S. city, town or state – or the federal government – has unreasonably interfered with its expectations, it can take the case to a "tribunal" that is not part of the U.S. judicial or administrative system. Under previous pacts, such tribunals consist of people, usually international lawyers, who make their livings by working for global corporations. One of the three is actually selected by the company bringing the claim; the challenged government selects the second; and the third must be agreeable to both parties. Quite apart from the host nation's laws, these three lawyers decide how to interpret the international investor protections and other pact provisions.

In short, by setting up a kind of "super-government" for foreign investors, this system routinely embedded in international trade pacts authorizes private attorneys to order the taxpayers of various nations to compensate companies for harms supposedly caused by their nation's own democratically enacted laws! Were that not problematic enough for Americans to contemplate, the new supranational system ends up beyond the reach of U.S. elected officials and judges. There is no provision for review by the U.S. Congress, executive branch officials, or the courts.

Tweaks Devised in Secret are Not Enough

Are trade pact dispute provisions really so imbalanced? True enough, after long and expensive litigation local communities and national governments have won cases brought under previous trade pacts. And in the face of public criticism, recently negotiated international trade pacts have tweaked some provisions. But the core difficulty is never addressed: Why should three lawyers, two of whom are anointed by a foreign corporation, be authorized to grant the corporation compensation for complying with sovereign, democratic policies? Democracy, sovereignty, and the rule of law are undermined regardless of the outcomes for particular cases.

Americans would be outraged if a party to a U.S. legal case could select the Supreme Court Justices who decide the case – and would be even more perturbed if a key party demanded that the Court use procedures that violate due process defined by our Constitution. Yet these are, in effect, the privileges granted to foreign companies under Investor-State Dispute Settlement provisions in typical international trade pacts. Today's negotiators working on the Trans-Pacific Trade Pact promise newly updated "high standards" – such as allowing third parties to file briefs in investor dispute cases; denying "sham corporations" the right to make claims; and authorizing the dismissal of frivolous claims. But no actual drafts have been provided, and the hinted updates are so minor as to indicate that the problematic core of earlier arrangements will persist.

Of course, the Trans-Pacific Partnership and other new pacts could, in principle, include procedures for adjudicating disputes with foreign companies that preserve rather than undermine democratic governance and the rule of law. But this is not likely to happen unless the American people are fully informed about emerging treaty provisions and the U.S. Congress has a full opportunity to revise and debate provisions before they become part of the rules that govern us.

Read more in Mark Barenberg and Peter Evans, "The FTAA's Impact on Democratic Governance," in *Integrating the Americas: FTAA and Beyond*, edited by Dani Rodrik, Alan M. Taylor, and Andrés Velasco (Harvard University Press, 2004), 755-789.