

**Center for International Environmental Law * Earthjustice * Environmental
Investigation Agency * Friends of the Earth US * Sierra Club**

Via Electronic Filing

January 25, 2010

Ms. Carmen Suro-Bredie, Chairman
Trade Policy Staff Committee
Office of the United States Trade Representative
Washington, D.C.

**Re: Request for Comments on the Proposed Trans-Pacific Partnership Trade Agreement,
74 Fed. Reg. 66720 (December 16, 2009)**

Dear Ms. Suro-Bredie:

We appreciate this opportunity to submit comments on the proposed Trans-Pacific Partnership Free Trade Agreement with Singapore, Chile, New Zealand, Brunei Darussalam, Australia, Peru and Vietnam. Our organizations believe that trade agreements can enhance environmental protection and promote a more sustainable form of development both here in the United States and among our country's trading partners. We are eager to support trade policy that simultaneously promotes economic prosperity as well as the larger societal goals of economic justice, poverty alleviation, healthy communities, human rights and a sound global environment.

Our organizations, however, are concerned that the current model of US trade policy is not achieving these goals but is, rather, damaging the US economy and undermining the public policy making space needed to ensure the highest levels of protection for our citizens and the natural environment. Similarly, we are concerned that among many of our trading partners, existing trade agreements are, at their best, failing to bring promised economic benefits to more than a small sector of business elite, and at their worst contributing to significant harm to livelihoods, the environment and the pursuit of good governance.

Further, meaningful reform of US trade policy must grapple with the profound interconnectedness of trade and environmental policy in a world where anthropogenic climate change threatens to remake coastlines, create millions of refugees, and induce water and food shortages among other impacts if strong short-term course changes are not made. Priority must

be given to rethinking how the US can achieve or facilitate emissions reductions, on the one hand, and promote lower carbon development pathways in its trading partners on the other.

Since a lack of transparency has plagued US trade policy making in the past, we enthusiastically support President Obama's goals of "increasing transparency and promoting broader participation in the debate."¹ We are similarly encouraged by President Obama's commitment to review and reform US trade policy in favor of policies that meet the public interest both at home and abroad. The proposed Trans-Pacific Partnership Trade Agreement (TPP) provides an important opportunity to lay out the framework for a new approach to US trade policy that truly benefits the environment, fosters development and promotes economic prosperity for workers both here and abroad.

Our organizations, dedicated to protecting the environment and promoting public health and sustainable development, have been closely involved in trade policy making over the last several decades. Our organizations, either presently or in the past, have served as members of the Trade and Environment Policy Committee (TEPAC), engaged with the United States Trade Representative (USTR), educated and advised Members of Congress and relevant committees of jurisdiction, and played a key role in informing the public. In the context of the proposed TPP negotiations, we draw upon these experiences to share several lessons about the reforms and improvements that are required if US trade policy is in the future to meet the objectives it has thus far failed to meet.

We cannot emphasize enough the vital importance of undertaking a review of our existing trade policy before embarking on what USTR considers will be a "high-standard, 21st century agreement with a membership and coverage that provides economically significant market access." The USTR should undergo formal, public review of its trade policy before engaging in the TPP. A comprehensive and fully transparent review will facilitate achieving the economic and sustainable development goals outlined by USTR.

Form of a TPP agreement and the structure of negotiations

We note with some concern that we already have in force bilateral free trade agreements (FTAs) with four of the seven countries currently listed as proposed partners in the TPP. The existing bilateral FTAs contain widely divergent levels of protection for public health and the environment. For instance, while improvements were made to the labor and environment chapters of the Peru FTA(2007),² the Chile FTA contains no such improvements. Also, marking a vital and much needed fix in US trade policy, the Australia FTA contains no provisions for an investor-state dispute resolution mechanism, while all other FTAs replicate the harmful investor-state dispute resolution model.

¹USTR "2009 Trade Policy Agenda Report." <http://www.ustr.gov/node/4442> (Accessed January 25, 2010)

² The US-Peru agreement is formally called the Peru Trade Promotion Agreement, or Peru TPA, but for clarity within this document we use the FTA designation when referring to Peru in conjunction with other agreements..

At this stage, it remains unclear how the proposed TPP negotiations will relate to these existing bilateral agreements. If the TPP is to truly be a regional agreement, to which additional countries can later accede, it will be necessary to create one harmonized regional trade policy and not a collection of bilateral arrangements from which additional countries can pick and choose. It should go without saying that no country's environment or labor commitments under standing agreements should be lowered as a result of participation in the TPP.

We also believe that it is critical to conduct a thorough assessment of the environmental impacts of any existing trade agreements with potential TPP countries. The United States Trade Representative (USTR), in coordination with other another relevant agencies, should conduct this assessment, as well as carry out periodic reviews of the economic, social and environmental impact of our trade agreements domestically and within our trading partners. It is difficult for the USTR to negotiate in the best interests of the United States without having a sense of how our trading partners have complied with their existing obligations or how the agreement has impacted the US. We similarly recommend that the results of this review be made widely available to the public well in advance of the US engaging in negotiations.

Peru is an important case in point of these structural questions. The US-Peru Trade Promotion Agreement was ratified in December 2007, and only came into force in January 2009. In fact some of its most significant environmental provisions, within the Annex on Forest Sector Governance, will only be fully enforceable in July of this year. It is early yet to understand the impact this agreement's innovations on environment, labor and intellectual property will have; moreover, USTR and partner agencies have put an enormous amount of time and effort into its implementation. It would be a significant waste of effort and momentum to reopen the Peru TPA through the TPP in a way that puts the existing provisions in doubt.

Determination of eligibility for potential trading partners

We believe that trade agreements can be important tools to facilitate sustainable development provided that the trading partners have the appropriate legal and institutional structures to address the challenges of more liberalized trade. These structures include transparent and participatory negotiations in which citizens of all trading partners have an opportunity to understand and comment on the trade agreement. They also require a baseline of environmental and other characteristics of a trading partner to determine how trade might affect the environment of our trading partner. That assessment will help determine whether a prospective trading partner has the appropriate laws, regulatory and enforcement capacity, and funding to address the challenges of more liberalized trade. They also include appropriate monitoring of the impacts of trade to determine if corrective action should be taken in light of any adverse impacts caused by the trade agreement.

The benefits of expanded trade with the United States should be reserved for those countries that demonstrate a genuine commitment to basic principles of good governance and

democracy. We therefore recommend that before notifying their intent to enter in to negotiations, the US Government should be required to make an initial determination of the countries' eligibility as a potential trading partner based on, inter alia, the country's commitment to and realization of free and democratic political processes as well as human rights. As environmental organizations, we recognize that basic failures of rule of law and democratic governance make environmental protection and the valuable assistance provided by civil society engagement extremely burdensome, if possible at all.

Determination of environmental impact

Current trade policy has thus far failed to adequately account for the effects of trade liberalization on the environment in both the US and among our trading partners.³ Similarly, the rapid pace of expanded trade often overwhelms the limited capacity of domestic regulators. Contrary to the paucity of evidence showing that countries lower their environmental standards to attract investment and other benefits of trade, evidence does show that trade agreements can have profound adverse environmental impacts. While these scale effects have been widely reported by NAFTA's Commission for Environmental Cooperation and others, the United States has failed to prevent scale effects in subsequent FTAs. For example, the environmental reviews required by Executive Order 13,141 only focus on environmental impacts in the United States and, as appropriate, global and transboundary impacts.⁴ When the future trading partner is a developing country, the review thus misses scale effects in the country or region most likely to experience the most significant environmental impacts from a trade agreement. As the GAO concludes in its 2009 assessment (see below), "the environmental reviews we examined for these FTAs do not provide in-depth or comprehensive descriptions of the myriad environmental challenges faced by FTA partners."⁵

To overcome this deficiency, all trade negotiations should be subject to environmental assessments that analyze the current state of environmental governance in the potential trading partner(s), the likely impact of the agreement on the environment in the trading partner countries, and the cost to the US (federal and state governments) of assisting trading partner(s) in implementing the environmental provisions. Such an assessment will help ensure that the United States and its trading partners fully understand the potential environmental consequences of greater trade liberalization in order to put in place the appropriate institutional and legal capacity to cope with environmental problems that may emerge from trade liberalization. Significantly,

³ See for example, Gallagher, Kevin. "Free Trade and the Environment: Mexico, NAFTA, and Beyond," Americas Program Policy Brief, Interhemispheric Resource Center, September 17, 2004. (Published in Spanish in *La Jornada en la Economía*, August 9, 2004, "Libre Comercio y Ecología: El Paraiso Contaminante." & Wold, Chris.

"Evaluating the NAFTA and Commission for Environmental Cooperation: Lessons for Integrating Trade and Environment in Free Trade Agreements." 28 *St. Louis University Public Law Review* 201 (2008).

⁴ Exec. Order No. 13,141, 64 Fed. Reg. 63,169 (Nov. 16, 1999) (Environmental Review of Trade Agreements) The TPA Act provides that environmental reviews will be conducted consistently Executive Order 13,141. 19 U.S.C. §3802(c)(4).

⁵ Government Accountability Office, *International Trade: Four Free Trade Agreements GAO Reviewed Have Resulted in Commercial Benefits, but Challenges on Labor and Environment Remain*, GAO-09-439, 59 (July 2009)

these steps should be taken prior to the FTA entering into force so that early responses can be taken to avoid problems. During the early stages of negotiating a trade agreement, a list of environmental priorities should be created specifically for the agreement being considered. Subsequent post-implementation monitoring will then test the assumptions of the environmental assessment and track environmental changes.

In so doing, the United States can begin to address the environmental shortcomings of FTAs recently reported by the GAO. In 2009, the GAO reviewed four trade agreements (Jordan, Chile, Singapore and Morocco) to assess “progress through FTAs in (1) advancing U.S. economic and commercial interests, (2) strengthening labor laws and enforcement in partner nations, and (3) strengthening partners’ capacity to improve and enforce their environmental laws.”⁶ Critically, GAO found that:

U.S. agencies responsible for the implementation of the environmental provisions and cooperation mechanisms lacked key steps in monitoring and enforcing trade agreements (1) identifying problems, (2) setting priorities, (3) gathering and analyzing information, (4) developing responses, and (5) taking enforcement action... We found that USTR does not proactively monitor the implementation of environmental provisions and that OES lacks a structure to manage and monitor implementation of environmental projects.⁷

Clear and marked improvements in USTR’s ability to monitor and effectively enforce environmental (and other) provisions of US trade policy are urgently needed.

Lessons from the Peru TPA implementation experience

While we recognize that the improvements in the “May 10th [2007] agreement” regarding the labor, environment, and intellectual property chapters of previously-negotiated agreements marked a step forward, our organizations are firmly of the view that these improvements were merely a step in the right direction and do not mark the end of the needed revisions to trade policy. A more comprehensive review and reform of the environment and other chapters is needed to ensure high levels of environmental protection. Moreover, the early experience of the Peru Trade Promotion Agreement, the only agreement subject to the May 10th revisions that has actually been ratified (December 2007) and gone into force (January 2009), clearly demonstrates that inadequate implementation of obligations will significantly undermine any success claimed by the agreement’s adoption. The following recommendations are based both on our specific recent experience with Congress and the USTR in implementing the Peru TPA and on our long-standing engagement in and analysis of the environmental implications of US trade policy.

The experience of Peru TPA implementation, while still early, has to date has been marked by controversy and setbacks on the Peruvian side. While it would not be accurate to lay the blame for events in Peru entirely on the TPA, and in particular on the US government’s

⁶ Ibid., p.2

⁷ Ibid., p. 61

conduct in implementation of the environmental chapters, there are at least two lessons that we must take from this process for future FTAs:

Greater emphasis on process: The first lesson is the importance of defining stronger mechanisms for transparent and consultative processes during implementation (beginning *before* certification), not only in the US but also in the trading partner – and ensuring that these mechanisms are used appropriately. While USTR and US NGOs were moderately successful in achieving a working relationship of information sharing, no comparable process was established by the Peruvian government, which was enacting far more substantive changes to its laws. The Peruvian government’s lack of consultation with its civil society, in combination with a political strategy that took advantage of the window opened by TPA implementation to make sweeping changes to the country’s legal framework, has contributed to serious internal social conflict for our trading partner and damaged the US’s image to some extent among the public through association with this conflict.

Adequate timeframe before certification: The second lesson is the deleterious impact of a rushed process, driven by political imperatives rather than robust assessment of a country’s status of implementation. If a country has not met its obligations, it should not be rewarded with either ratification or certification of the agreement. Therefore clear benchmarks for performance need to be established by a clearly-defined and independent mechanism, with dedicated and substantial funding, to monitor and facilitate implementation of the Environment chapter and other environmental provisions associated with the TPA. The independent mechanism should include a meaningful and effective citizen submission process and should provide for capacity building initiatives and comprehensive implementation plans, including explicit timelines. In some instances, insufficient technical and resource capacity is a real and substantive constraint on the ability of our trading partners’ ability to meet their obligations under the agreement. If a country is failing to meet either their obligations or the benchmarks by which the US government can assess progress, the US should provide assistance to ensure that our trading partners are on a path towards meeting their environmental obligations.

It is clear from the Peru experience that as US trade policy takes a more integrated approach to environment and labor standards, these lessons only increase in significance due to the broad set of stakeholders and areas of regulation that are at stake.

Across the board exceptions for environment and public health

It is vital to ensure that the trade and investment rules in FTAs do not undermine environmental laws, regulations and governmental actions. To this end, FTAs should include a clear set of across-the-board general exceptions for environmental and public health protections that are not arbitrarily discriminatory. FTAs recently negotiated by the United States apply such exceptions only to particular provisions and do not include a full set of exceptions for other provisions, such as those addressing investor rights, services and government procurement.

Investment chapter recommendations

United States foreign policy as well as trade and investment policy, should have as a core objective the promotion of sustainable development. Interests in expanding exports and investment opportunities must be balanced with the broader public interest of improving livelihoods, reducing poverty and inequality, and promoting environmental sustainability. Thus, expansion of investment can and must be made compatible with the protection of the public interest in the United States and overseas. In this regard, the review process as well as any proposed TPP negotiations provides an opportunity to correct the shortcomings of the past and chart a new course for investment rules that emphasizes a balanced approach to ensuring both investor rights and responsibilities.

Our organizations are deeply encouraged by President Obama's commitment to reforming the investment chapter of free trade agreements. As environmental organizations, who have joined our colleagues from labor, development, faith and consumer non-governmental organizations in raising concerns about the impact of our current model on the capacity of U.S. and foreign government authorities to protect the public interest, we strongly support President Obama's assurances that he "will ensure that foreign investor rights are strictly limited and will fully exempt any law or regulation written to protect public safety or promote the public interest. And I will never agree to granting foreign investors any rights in the U.S. greater than those of Americans." The Trade Act of 2002 establishes a congressional mandate requiring that investment rules not grant foreign investors greater substantive rights than U.S. investors are afforded under U.S. law. We believe this principle should be fully respected and ensured in the negotiation of any future agreement. This fundamental failure to meet the "no greater rights" test occurs in at least several critical parts of the investment rules in our current trade policy. In advance of TPP negotiations, we feel that this is crucial to ensure that US trade policy meets the minimum requirements laid out by President Obama.

Specifically, previous investment chapters create a set of rights for investors (including foreign investors in the U.S.), but fails to establish obligations for investors and corporations in the communities in which they operate. Further, by establishing "investor-State" dispute settlement procedures that will allow foreign investors, including foreign subsidiaries of US companies, to challenge U.S. and foreign public interest laws and regulations directly, investment chapters have provided a potent tool for foreign investors to assert the imbalanced rights provided by the treaty. Moreover, claims made under these agreements will be decided by ad hoc panels that are not trained in or bound by U.S. Supreme Court precedent; nor are the decisions of these panels subject to review by U.S. courts to ensure that they do not deviate from U.S. law or grant greater rights to foreign investors than are accorded to U.S. investors. In addition to these three issues of particular concern regarding the "no greater rights" standard, namely expropriation, fair and equitable treatment standard, and the definition of investment, we are concerned that extant investment rules include provisions that unduly constrain the necessary

regulatory flexibilities of the State, or allow investors to attack public interest laws and regulations.

We note with approval that the U.S.-Australia FTA investment chapter does not contain an investor-state dispute mechanism. This is positive for several reasons. Experience with cases being brought under existing agreements (chiefly NAFTA and numerous bilateral investment treaties or BITs) demonstrates that individual investors are pushing for expansive readings of the substantive obligations in those agreements. Further tilting international investment rules in favor of investors at the expense of the ability of governments to regulate in the public interest is a threat to good governance and public welfare. It should be noted however that while the absence of an investor-state dispute mechanism in the US-Australia FTA is a significant improvement, the underlying provisions U.S.-Australia FTA investment chapter are largely unchanged from those negotiated in recent U.S. FTAs, including the Singapore, Chile and Peru FTAs, and thus remain problematic.

The May 10th, 2007 Agreement between Congressional leadership and USTR reaffirmed the importance of this requirement to ensure that foreign investors are not afforded greater rights than Americans under US law in our trade agreements, however it fell short on implementation. The agreement merely notes in the preamble “that foreign investors are not hereby accorded greater substantive rights with respect to investment protections than domestic investors under domestic law where, as in the United States, protections of investor rights under domestic law equal or exceed those set forth in this Agreement.” Although the preamble of a treaty does not constitute a source of obligation per se, it does provide guidance in interpreting the meaning and scope of the agreement’s obligations and in this regard we welcome the additional interpretive guidance included in the Peru FTA. The NAFTA and the WTO agreements demonstrate the importance of including references to important public policy goals such as environmental protection and sustainable development in situating the respective agreements in the broader international legal context. However, we maintain that the May 10th agreement did not contain the necessary statutory changes to ensure that the basic principle of not affording greater substantive rights to investors is met in our trade policy.

Our organizations believe that the investment chapters of future trade agreements should not pose threats to public interest protections for sustainable development, the environment, health and safety, and workers’ rights. We offer the following comments to ensure that the minimum benchmark outlined by President Obama is met, allowing US and foreign governments to protect the public interest.

a. Dispute Settlement recommendations

The dispute resolution mechanism contained in the investment chapters of previous FTAs pose significant risks to the public interest. When international dispute resolution is appropriate,

the investment chapter should provide for state-to-state dispute settlement, which guarantees the crucial role of governments in determining and protecting the public interest. We therefore recommend that the administration replace investor-state dispute settlement with a state-to-state mechanism. If the administration continues to include an investor-state dispute settlement mechanism, investors should be required to exhaust domestic remedies and should require the agreement of both states party to the agreement before filing a claim before an international tribunal. If either Party does not agree, the States to take up the dispute in a state-to-state dispute resolution process. Similarly, the dispute resolution mechanism should also provide a screen that allows the Parties to prevent frivolous claims or claims which otherwise may cause serious public harm. Moreover, any investor-State dispute settlement process should be completely transparent, with briefs and other documents available to the public, citizens afforded the right to submit amicus briefs, and proceedings open to the public. Lastly, just as the World Trade Organization dispute settlement process has benefited tremendously from an appeals process, so to would any investor-State dispute settlement process. Significantly, the appeals process must allow for appeal of errors of law. These elements of dispute settlement are vital to any process intended to adjudicate matters of important public policy.

Allowing investors to take claims to international tribunals without first requiring domestic courts with expertise in these matters to review the claim, develop a factual record and provide interpretations of relevant domestic law invites international tribunals to misread domestic laws, unintentionally undermine public policy, and reach inconsistent and erroneous decisions. This is particularly inappropriate where the domestic legal system is well-developed, such as in the United States.

Removing cases from domestic legal systems also undermines incentives for countries to establish a sustainable rule of law. Requiring foreign investors to exhaust domestic remedies would help to build the capacity of developing country judicial systems to address disputes concerning foreign investment and would help build and sustain the rule of law in countries hosting foreign investments. Rather than allowing investors to jump immediately to international tribunals, they should at least be required to test the domestic legal system in host countries. It is a U.S. foreign policy objective to strengthen judicial systems in developing countries; this should not be undermined by U.S. trade and investment policy.

Further, the provisions contained in the investment should comply with U.S. and international law, both of which require exhaustion of domestic remedies. Under U.S. law, investors must exhaust all available procedures for obtaining compensation before bringing a regulatory takings claim under the Takings Clause of the Fifth Amendment. International law similarly requires that foreign investors exhaust domestic administrative and judicial remedies before pursuing claims before international tribunals. In human rights cases, for example, claimants are required to exhaust domestic remedies before bringing a claim to an international tribunal. Under the UN Convention on the Law of the Sea (UNCLOS), exhaustion of domestic remedies is a condition of admissibility for claims where required under international law. By

analogy, the international criminal court does not substitute for domestic courts, and cases are inadmissible if local courts are investigating or prosecuting them, unless the local courts are unwilling or unable genuinely to carry out the investigation or prosecution, having regard to the principles of due process established in international law.

Requiring foreign investors to exhaust domestic remedies does not mean that they must unnecessarily subject themselves to costly delay when domestic courts provide no chance of a meaningful remedy. Under both U.S. and international law, exhaustion is not required when local remedies are unavailable or unreliable, or the local tribunals are not independent. Any provisions establishing an investor-State mechanism in US trade policy should follow this model by only allowing direct access to international dispute settlement without prior exhaustion of domestic remedies when the arbitrators determine that the foreign investor has established that: 1) domestic laws or judicial processes do not afford the investor due process of law for the rights that have allegedly been violated; 2) the investor has been denied access to domestic remedies or has been prevented from exhausting them; 3) there has been, or is likely to be, unwarranted delay in the domestic tribunal's rendering of a final judgment; 4) domestic remedies are otherwise unavailable; or 5) where both State Parties agree that the dispute should proceed directly to government-to-government dispute resolution.

Similarly, governments that are parties to the agreement should have the opportunity to prevent investment cases from proceeding if, for example, the claim is inappropriate, without merit, or would cause serious public harm. Providing such a screen for direct investor-State disputes would in no way impede the ability of a government itself to bring a claim against the other government. If both countries do not agree to bar a claim within a fixed period of time, then the direct investor-State claim would be allowed to proceed.

b. Appointment of Arbitrators

The clear preference in our trade policy for investor-State arbitration is often rationalized as an independent, neutral and impartial mechanism for the resolution of disputes. These terms, however, are not interchangeable. Arbitration may be independent from domestic courts, but it is neither neutral nor impartial. In fact, given that the investor is allowed to appoint one of the arbitrators that decide a public law dispute, there is an inherent bias in the mechanism. The commercial arbitration approach our current trade policy is unsuited for investment arbitration. It leads to conflicts of interests, profiling of arbitrators as either pro-State or pro-investor, and a biased system of dispute settlement that favors the interests of a particular class of investors above the public interest. There is no good reason for allowing the investor involved in a dispute to appoint an arbitrator. The better approach is for the States party to the agreement to appoint arbitrators on an ad hoc basis. This approach would preserve the integrity of the public law framework that is essential to the adjudication of the public interest issues that arise in investment arbitration.

There are other advantages to having the Contracting Parties appoint the arbitrators. First, this approach would help ensure respect for the intent of the treaty drafters in their definition of the applicable law. In this regard, some investment tribunals, such as GAMI and Corn Products International, have gone outside the bounds of the law as understood by the Contracting Parties. Second, it gives both Contracting Parties notice of the dispute, which enables the non-disputing party sufficient time to make submissions to the Tribunal if it chooses to do so. Third, this approach engages the Contracting Parties in a constructive partnership in implementing the agreement and resolving investment disputes that may arise. This procedural change could help address the inherent bias in investment arbitration. This view, however, does not endorse investor-State as an adequate mechanism to resolve disputes between investors and host States, especially where no exhaustion of domestic remedies is required. As noted above, the better approach is to design a State-to-State dispute settlement mechanism for the resolution of investment disputes.

c. Definition of expropriation

Our current trade policy fails to define expropriation in a manner consistent with U.S. law, using only some of the critical factors established by the Supreme Court in determining what constitutes a takings case. The omission of other Supreme Court factors results in an imbalanced standard that inappropriately privileges the investor. In setting out some of the indispensable factors that must bind decisions on whether an “indirect expropriation” has occurred, we believe each of the problems we identify must be addressed to ensure that US trade policy does not breach the ceiling of U.S. law.

We have identified the following factors and the relevant areas of US case law as follows. Government regulatory action taken to address a public nuisance cannot be considered a taking, or expropriation (*Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1029 (1992)). The Supreme Court has ruled that a governmental regulatory action must be analyzed in terms of its permanent interference with a property in its entirety in order to determine whether a taking has occurred. This standard prevents segmenting a property, whether measured in terms of area or time, as clearly articulated in the Supreme Court’s *Tahoe-Sierra* case, which rejected a taking claim arising out of a temporary moratorium on development. (*Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 122 S. Ct. 1465 (2002)). In considering whether a regulatory action constitutes an expropriation, investment provisions must clearly include the standard established in Supreme Court jurisprudence that an adverse effect on economic value does not by itself constitute an expropriation, no matter how serious the adverse effect, “[O]ur cases have long established that mere diminution in the value of property, however serious, is insufficient to demonstrate a taking” (*Concrete Pipe & Products v. Construction Laborers Pension Trust*, 508 U.S. 602, 645 (1993) (emphasis added)).

Similarly, the Supreme Court distinguishes between land and “personal property,” noting in particular that, “In the case of personal property, by reason of the State’s traditionally high

degree of control over commercial dealings, [the owner] ought to be aware of the possibility that new regulations might even render his property economically worthless (at least if the property's only economically productive use is sale or manufacture for sale)" (Lucas v. South Carolina Coastal Council, 505 U.S. 1003, 1028 (1992)).

d. Definition of Investment

The definition of "Investment" in our current trade policy is much broader than the real property rights and other specific interests in property that are protected under the Takings Clause of the U.S. Constitution. The definition includes "every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk." Under the U.S. Constitution, in contrast, such broad economic interests are not considered forms of property that are protected by the Takings Clause, nor do investment provisions recognize the Supreme Court's holdings that property interests are limited by background principles of property and nuisance law. Lucas v. South Carolina Coastal Council, 505 U.S. 1003, 1029 (1992).

Furthermore, the definition in our current trade policy was extended to explicitly include "futures, options, and derivatives," and it exceeds customary international law for state responsibility for injuries to aliens. These types of instruments have played a troublesome role in the recent financial crisis experienced by the United States. Their inclusion also introduces a concerning element of uncertainty in relation to their application to instruments designed to address climate change, such as carbon offsets or other financial instruments relating to carbon mitigation.

e. Minimum Standard of Treatment

In regard to the minimum standard of treatment, we are deeply concerned that the standard in existing trade policy is completely unbounded and open-ended, with no clear definition. The standard therefore could be interpreted by tribunals in ways that go far beyond U.S. law. For example, we are concerned that the term "fair and equitable treatment" has been included as an essential element of the standard. While we welcome the clarification that "fair and equitable" treatment "includes" procedural due process, this in no way eliminates the significant potential of a broader, open-ended interpretation of the standard. "Fair and equitable treatment" opens the door to outcomes in investment cases that are in no way limited by, or consistent with, U.S. law. The explicit limitation of the minimum standard of treatment provision to "customary international law" corrects one serious flaw with the NAFTA approach, which referenced only "international law." Of course, the content of customary international law with respect to the treatment of aliens is not crystal clear, and arbitral panels have applied this standard in idiosyncratic fashion, e.g., *Occidental v. Ecuador* and *CMS Gas v. Argentina*.

There is no right corresponding to “fair and equitable treatment” under U.S. law. The closest U.S. law analogue is the Administrative Procedure Act (APA), which allows a court to review federal regulations to determine whether they are “arbitrary or capricious.” But the APA’s standard is presumably more difficult for claimants to prove than “fair and equitable” (which invite a balancing of all facts and circumstances), and the APA does not apply to many governmental actions (e.g., legislation, court decisions, actions by state, local and tribal governments, and exercises of prosecutorial discretion) that are covered under investment agreements. Moreover, the APA does not provide for monetary damages (as these investment provisions would allow); only injunctive relief is allowed. Finally, the APA requires U.S. courts to accord substantial deference to government decisions; there are no equivalent doctrines in treaties or other international law, to our knowledge.

In addition, the “fair and equitable” language, if viewed as an independent standard, is extremely dangerous to good governance. It would invite an investment tribunal to apply its own view of what is “fair” or “equitable,” unbounded by any limits in U.S. law. Those terms have no definable meaning, and they are inherently subjective. Indeed, we wonder how they can have any principled meaning when applied to countries with such different histories, cultures, and value systems. The kind of second-guessing of governmental action – e.g., legislation, prosecutorial discretion, police action, court decisions, regulatory actions, zoning decisions, etc., at all levels of government – invited by this type of standard is antithetical to democracy.

As a result, future US FTAs should either omit any obligations relating to the minimum standard of treatment. To the extent that an obligation concerning procedural fairness is desired, such an obligation should be clearly articulated.

f. Performance Requirements

Previous investment policy proscribes the use of performance requirements. This norm is often justified on the basis that the market is more efficient in driving decisions regarding the conduct of economic activities. Accordingly, investment provisions prohibits the host State from requiring local content, forms of technology transfer, and other requirements related to the operations of the investment. The performance requirements section of previous FTAs, however, include a puzzling environmental exception for some but not all of its provisions. The exception singles out some paragraphs and not others and directs that they not be construed in a way to prevent a Party from adopting or maintaining legitimate environmental measures. It is not clear whether this means that the paragraphs not mentioned may be construed to prevent a Party from adopting or maintaining legitimate environmental measures, nor is it clear if that is the case why the exceptions are not applied more broadly.

The proscription of performance requirements removes an important tool to ensure linkages between investment and the local economy. These linkages are essential for an investment to contribute to the development of the local economy, and more broadly to the

sustainable development of the host State. For example, using local sources and engaging in joint ventures with local economic operators fosters local economic opportunities and effective transfer of technology and know-how. From a development perspective, these performance requirements are essential to ensure that foreign investments do not constitute enclaves that crowd out local investors, but instead effectively link with the local economies. Enabling adequate policy tools that help promote long-term sustainable development in our developing country partners is also important for the long-term security and prosperity of the United States.

g. Exceptions for Health, Safety and Environmental Measures

In disputes concerning health, safety and environmental (HSE) measures, the absence of general exceptions for HSE measures places the interpretive focus on the substantive investment disciplines, such as expropriation, the fair and equitable treatment standard as an element of the minimum standard of treatment, and the non-discrimination standards. In this regard, it has been argued that there is no need for a general exceptions clause given that the substantive rules already provide sufficient flexibility to the State for the adoption of measures necessary to address health, safety and environmental threats. While certain flexibility does exist in certain disciplines, this is a matter of interpretation that is left to each tribunal. Consequently, there is no certainty that an investment tribunal will interpret the substantive rules in a way that provides sufficient flexibility to safeguard the regulatory needs of the host State. As noted earlier, the lack of certainty reduces the ability of the State to respond to HSE risks. Moreover, it is far from clear that existing flexibilities are sufficient to fully safeguard measures designed and applied for the protection of health, safety and the environment. In this regard, a general exceptions clause makes explicit what may be implicit, thereby providing guidance to tribunals as well as certainty to the law in a critical area of public policy. Omitting a general exception for HSE measures introduces a high level of uncertainty regarding the legality of measures adopted by the State to protect its people and environment from HSE threats. This uncertainty reduces the ability of the State to effectively respond to HSE risks and must be amended in future trade and investment policy.

The General Agreement on Tariffs and Trade, for example, contains a general exception in Article XX for measures necessary for the protection of human, animal or plant life or health, or that relate to the conservation of exhaustible natural resources, provided that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade. These exceptions have been critical in ensuring that the United States can adopt measures to protect the environment and natural resources. For example, in *US-Shrimp Turtle*, the general exceptions in Article XX were critical to upholding the need for measures to protect endangered marine sea turtles.

In the particular context of treaties for the protection of investments, countries like Canada, China, India, New Zealand and Singapore, for example, have incorporated general

exceptions for the protection of health, safety or the environment, in varying formulations. Other countries, like Germany, have incorporated exceptions for particular disciplines, such as national treatment. These provisions are critical to ensuring that the State will be able to respond to HSE threats and provide protection to its people and environment, without having to risk liability under the agreement.

h. Agreements Relating to Natural Resources and Other Assets

The grant of arbitral jurisdiction over claims based on a breach of “an investment authorization” or “an investment agreement” involving natural resources and other government assets undermines domestic legal systems by removing an important class of disputes and by opening whole new areas of potential investor challenges to domestic regulatory programs. This expansion of investor-State arbitration is especially problematic because these disputes can involve judging not only the propriety of collecting royalties for natural resource extraction, but also the validity of measures adopted by government agencies to ensure compliance with regulations, such as permits.

The investment agreements covered by these jurisdictional grants are not commercial disputes, but involve important policy questions regarding public assets, including natural resources such as oil, gas, timber, water, etc. Moreover, the inclusion of “assets that a national authority controls” in the investment policy is broad enough to encompass, inter alia, disputes over government procurement, services, and a number of regulations and permits.

In particular, we are concerned that the new jurisdictional grants make any dispute and all issues arising out of investment agreements actionable for damages before unaccountable, ad hoc arbitral tribunals outside the host country legal system. Whether a party is in breach of investment agreements or authorizations should be determined under applicable U.S. law, and through the statutorily mandated process of administrative courts followed by appeal, if necessary, to U.S. federal courts. That comprehensive body of law defines the competence, rights and obligations of the U.S. government regarding its contracts, including those concerning natural resources. Similarly, that procedural system ensures fairness and consistency in dealing with the multitude of issues involved in U.S. government contracting. It is also critically important that legitimate U.S. regulatory decisions (e.g., regarding health, environmental, communications, energy, and nuclear issues) be tested in the U.S. court system and be subject to U.S. laws, not subject to second-guessing by ad hoc arbitrators.

i. Capital Controls

We are deeply concerned that the provisions on capital transfers in current trade and investment policy would limit governments’ ability to use legitimate measures designed to restrict the flow of capital in order to protect themselves from financial instability. The severe financial crisis experienced by the United States and the world in 2009 should lead to a serious re-thinking of these provisions. Without adequate measures to prevent and respond to severe

financial instability, broad sustainable development will remain out of reach for many developing countries. The increased frequency and severity of financial crises also hurts U.S. economic interests, as crisis-stricken countries devalue their currencies and flood the U.S. market with under-priced exports in order to recover.

Full capital account liberalization has not been shown to be necessary to stimulate investment flows, deepen capital markets, or enhance economic growth. In a March 2009 report, the International Monetary Fund (IMF) noted the capital controls in several countries mitigated the effects of the financial crisis. Further, the IMF has indicated support for the availability of capital controls as a policy tool and no longer insists on full capital account liberalization as a requirement for its borrowers. In June 2009, a UN communiqué on the financial crisis also indicated support for the use of capital controls as an appropriate and useful policy tool to weather the impacts of the crisis. The United States should ensure – for the sake of developing economies, international financial stability, and its own economic interests – that countries have the policy flexibility needed to impose capital controls in appropriate circumstances.

j. Most Favored Nation

The implications of the most favored nation (MFN) treatment provisions are widespread and affect important public interest issues. We are particularly concerned that the lack of clarity in the text concerning MFN leaves open the possibility that foreign investors covered by a trade agreement could use the MFN principle to assert rights provided by other investment agreements or treaties that a host government has entered into. This could result in investors using the MFN to claim greater rights than are provided under the agreement that was agreed to by their home country. Investors may be able to invoke MFN to circumvent these attempted limitations and gain the full set of rights accorded to foreign investors under NAFTA. Conversely, foreign investors who enjoy the right to MFN through an existing trade agreement or other treaty could cite that MFN obligation in demanding the full new set of rights – both substantive and procedural – granted to foreign investors in trade agreements.

The unfettered application of the MFN clause in investment agreements would thus push towards a harmonized and enlarged system for the protection of investments, where investors could pick the most favorable standards and dispute settlement mechanisms. Further, such expansive interpretations of the MFN clause blur the distinctions between procedural and substantive elements in international agreements, thereby threatening to expand investor-State arbitration to treaties contemplating other mechanisms for the resolution of disputes, e.g., Treaties of Friendship, Commerce, and Navigation and the General Agreement on Trade in Services.

To respect the fundamental public policy considerations that the Parties envisaged when entering into international agreements, explicit limitations to the MFN clause should be established either in its construction or as exceptions to its disciplines.

Conclusion

While trade policy can help the US and our potential trading partners achieve the twin goals of economic prosperity and sustainable development, long-standing concerns with the model of US trade policy must first urgently be addressed. The first step in ensuring such concerns are adequately addressed is ensuring that USTR in collaboration with Congress and relevant Congressional agencies undergoes a formal, comprehensive, inclusive and fully transparent review of US trade policy. We greatly look forward to working with Congress and the Administration to provide our analysis and recommendations throughout the review process. This review can then serve as a useful framework from which to begin trade negotiations with appropriate potential trading partner countries. Without such a review, we are concerned that many of the same mistakes and omissions of the past will be replicated in the TPP. We thank you in advance for your consideration of these comments.

Sincerely,

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