New barriers to investor–state relations post-NAFTA

DISCIPLINING GOVERNMENTS

The legal regulation framework imposed by the North American Free Trade Agreement (NAFTA) has undoubtedly influenced investment strategy in North America. The inclusion of Chapter 11 (Investment) was a turning point in company–state relations not only within North America, but also outside the region. The chapter’s framework became a model that was reproduced almost identically in new negotiations with other countries. However, this legislation would have lacked power if Chapter 11 had not been accompanied by a dispute settlement mechanism intended to settle claims filed before two extraterritorial courts: the International Centre for Settlement of Investment Disputes (ICSID) at the World Bank, and the United Nations Commission on International Trade Law (UNCITRAL). Thanks to this process, companies gained the right to put governments on trial outside their national courts and to demand compensation from national authorities.

This was an important victory not only for companies, but also for those international agencies that, since the 1960s, had tried to impose an international foreign investment protection regime. This purpose was partially achieved when the United States and Canada, two powerful countries, endorsed NAFTA. Its adoption produced the proliferation of new chapters on investment in other free trade agreements (FTAs).

When companies first filed demands against the three North American governments, both the business community and governments responded with mixed reactions because this process raised the possibility that any of them might be sued. Thus, one of the implicit purposes contained in Chapter 11, originally designed to counteract Mexican nationalism, was successful. Chapter 11 became an instrument for Canadian and US companies who decided to implement a sort of “settling of scores,” breaking up the informal partnership they had established while lobbying for the agreement.

As well, the payment of a substantial compensation awarded by the companies, but adjusted by the courts, gave investors a new level of certainty.

CANADIAN MINING: THE BIG WINNER

The protection provided by NAFTA to corporate North America explains the progress Canadian mining companies have made under the new state–investor regime. The same opportunities have encouraged the establishment of Canadian financial activities in consumer banking, the relocation of some operations of the Canadian aviation industry, and growing Mexican investment in key sectors of the US economy.

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Groter flexibility

Although the CCRFTA is considered successful, the case of Costa Rica represents the weakest link in the agreements negotiated by Canada. Canadian negotiators intended to use this agreement to position Canada strategically in Central America vis-à-vis the United States. The agreement does not include a specific chapter on investment because both countries had negotiated a Bilateral Investment Treaty (BIT) in 1998. One of the main obstacles of the Canada–Costa Rica Free Trade Agreement (CCRFTA) has been the imposition of visa requirements for all Costa Ricans entering Canada. This has discouraged the promotion of foreign trade in Costa Rica and has particularly benefited US brokers hired to promote the economic interests of Costa Rica in the United States and Canada.
Concerning the Canada–Peru Free Trade Agreement, Canadian negotiators introduced, for the first time, an explicit definition of “indirect expropriation or equivalent.” The clear definition was intended to guide the extraterritorial courts and stop the indiscriminate and inaccurate use of the term.

Owing to strong opposition toward a free trade agreement with Colombia, where respect for human rights and labour are contentious issues, Canadian negotiators used article 816 to establish that “each party should encourage the parties operating within its territory or jurisdiction to incorporate voluntarily international standards of corporate social responsibility within their domestic policies.” Ottawa expects Canadian companies to observe business ethics as set out in the agreement.

CHINESE DIRECT INVESTMENT

The growing presence of Chinese investment in North America is a factor that has directly influenced the investment strategies of the three NAFTA countries. While business executives in Mexico and Canada have decided to invest abroad, Chinese investment in North America reached record levels in 2008. However, the arrival of Chinese investment in North America has not been without controversy.

In 2008, Mexico and China concluded a BIT, and in 2005, Canada initiated a process of analysis and consultation on a possible FTA, or at least a BIT, with China. Reactions in Canada have been largely positive. Provincial chambers of commerce regard Chinese investment as a positive step, and the governments of British Columbia, Alberta, and Saskatchewan have signed an economic partnership that creates the largest inter-provincial free market whose major goal is to promote trade with Asia. The first major undertaking of the New West Partnership will be a joint mission to China and Japan in 2010.

Of the three NAFTA countries, the United States is the biggest exporter of capital to China; in contrast, Canadian investment in China (Hong Kong included) represented only 1.5 percent of its total foreign investment in 2009. China has established subsidiaries in North America for two main reasons: to transfer its final manufacturing production process to those countries that impose tariff barriers on Chinese products, and to gain access to domestic markets such as NAFTA.

SECURITY: THE LATEST NON-TARIFF BARRIER

The United States and Canada have introduced new regulatory restrictions on foreign capital investors. In 2005, Canada initiated an amendment to the Investment Canada Act (C-10), which protects certain economic sectors on national security grounds. This amendment was similar to legislation passed by other G8 countries. Parliament approved the Act in 2009, adding section IV.1 (Investments Injurious to National Security). The Minister of Industry is in charge of revising all foreign investment that could threaten Canadian security. It is noteworthy that these changes in Canadian law are attributed to the pressure exerted by the US House Defense Services Committee on the Canadian government to restrict Chinese acquisition of major Canadian energy corporations.

While the US policy to attract foreign investment is very liberal, the process to receive capital is complex because a different government office examines each case according to its assessed economic impact. There is legislation, such as the Defence Production Act (section 721), that brought about the Committee on Foreign Investment in the United States (CFIUS) in 1972. Unlike Canada, screening foreign investment is the responsibility of the US president who, thanks to the Exxon–Florio amendment (1988), can initiate an investigation of a company if it is suspected of threatening national security. In 1993, the Byrd amendment established that any attempt to merge, acquire, or purchase a US company could be investigated if it were suspected of undermining national security. In 2005, the CFIUS, along with the US Congress, prevented the China National Offshore Oil Corporation’s acquisition of the Union Oil Company of California (UNOCAL).

Measures aimed at controlling foreign investment in the United States have continued apace. In 2007, an amendment to the Defence Production Act was introduced, and it led to the Foreign Investment and National Security Act, which also broadens the scope of federal oversight to the economic field.

MEXICO AT THE MARGIN

Mexico receives much less Chinese investment than the United States and Canada. Mexico is a gateway for Chinese capital not only to the rest of the NAFTA region, but also to Latin America. Despite the fact that Mexico objected to China’s accession to the WTO in 2001, Mexico did not adopt similar restrictive measures as Canada and the United States. Although article 30 of the Mexican Act on Foreign Investment (1993) contains provisions on investment and national security, the article has not been applied to veto the inflow of foreign investment.

LESSONS LEARNED

NAFTA has standardized the way state–investor disputes are handled, leading to both greater security for investors and greater state-to-state tensions. The presence of Chinese investment in North America has changed the dynamics between the NAFTA partners considerably. US and Canadian concerns about
Ocra. In addition to political coordina-
tion and cooperation among the three
countries, the IBSA forum has become
a model for projects benefiting poorer
nations, thus demonstrating in practice
that solidarity is not an attribute solely of
the rich.

We have also held summits between
South American and African countries
(ASA), as well as with Arab countries
(ASPA). Taking into account their specific
complementary natures, we have de-
dsigned policies and built bridges con-
necting regions that were far apart. This
political move resulted in remarkable
progress in economic relations. Brazilian
trade with Arab countries grew fourfold
in seven years. Trade with Africa in-
creased fivefold, to more than US$26
billion, surpassing trade with traditional
partners such as Germany and Japan.

These new coalitions are helping to
change the world. In the economic arena,
the replacement of the G7 with the G20
as the main international body has reset
the course of production and inter-
national finance and constitutes evidence
that in the absence of emerging coun-
tries, decisions regarding the world econ-
omy lack legitimacy and effectiveness.

Moreover, in the field of international
peace and security, Brazil and Turkey
were able to persuade Iran to take on the
commitments provided for in the Tehran
Declaration. This agreement makes clear
that new perspectives and approaches
are necessary to tackle issues previously
dealt with exclusively by the permanent
members of the UN Security Council.
Despite initial resistance to an initiative
nurtured outside the closed circle of
nuclear powers, we are certain that the
resulting dialogue will serve as the basis
for future negotiations and a final solu-
tion for that issue.

Good foreign policy requires pru-
dence. But it also requires boldness. It
should not be timid or based on an inferi-
ority complex. It is usual to hear that
countries should act in accordance with
their means, a time-worn phrase that is
almost too obvious, but the greatest
mistake a nation could make is to under-
estimate its means.

For almost eight years now, Brazil has
acted with boldness and, like other
developing countries, has changed its
place in the world. Today, such countries
are regarded, even by occasional critics,
as actors bearing increasing responsibil-
ities, entitled to play a role that is ever
more central to the decisions that affect
the destiny of the planet.

NOTE
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