

ENVIRONMENTAL POLICY IMPLICATIONS OF NAFTA'S INVESTMENT CHAPTER

Professor Sanford E. Gaines
University of Houston Law Center

Questions Posed

- Do the facts of the cases indicate that foreign investors are escaping fair application of national environmental measures?
- Do government actions in response to Chapter 11 awards show “chilling” of environmental protection efforts?

Investor-State Arbitration

- 42 notices of intent to file a claim
 - 10 against Canada; 15 each against Mexico and US
- 5 cases centered on environmental regulation
 - 1 still pending (Glamis Gold, Ltd. and US)
- 4 cases complete
 - Metalclad Corp. and Mexico—1997-2001
 - Ethyl Corp. and Canada—1997-1998
 - S.D. Myers, Inc. and Canada---1998-2004
 - Methanex Corp. and US---1999-2005

Ethyl Corp. and Canada: MMT

- Environment minister's expressed concern:
Health effects from manganese inhalation
- Action under federal environmental law:
None---insufficient scientific evidence
- Measure adopted:
Legislation banning import or inter-provincial trade of MMT (Bill C-29)

- Ethyl's Chapter 11 Claim: Violation of national treatment
 - MMT a legal product, even after C-29
 - Trade ban prevents Ethyl (foreign investor) from distributing MMT to refiners throughout Canada
- Alberta and other provinces initiate proceeding under Agreement on Internal Trade
 - AIT tribunal finds insufficient health concern to support federal measure restricting internal trade

Result of Claim and Further Action

- 1 month after AIT ruling, government amends C-29 to remove MMT from trade ban list
- Government then settles Ethyl's Chapter 11 claim for US\$ 13 million (1998)
 - As part of settlement, government expressly asserts that there is no health basis for restricting MMT
 - This position reaffirmed by ministers of health and environment (2001) and study by NRTEE (2001)
- Canadian refiners phase out use of MMT
- Scientific studies of health effects from low-level manganese exposure and automotive pollution effects remain inconclusive and controverted
- Other countries: India—voluntary non-use
Australia—allowed

Methanex Corp. and US: MTBE

- California's expressed concerns:
 - Contamination of groundwater
 - Possible carcinogenicity
- Measure taken: California Senate Bill 521 (1997)
 - Study by Univ. of California (Nov. 1998); report to governor
 - Decision by governor to phase out MTBE by end of 2002 (March 1999)
- Complicating factors
 - Methanex does not produce MTBE; produces methanol, a key ingredient
 - Substitute for MTBE is corn-based ethanol, a US product

Methanex Arbitration Results

- Preliminary award on jurisdiction (2002)
 - Methanex has no investment in MTBE production, sale. Therefore cannot assert claim based on regulation of MTBE.
 - Methanex may pursue claim based on amended complaint alleging governor's corrupt intention to discriminate against Methanex and in favor of US ethanol producer ADM, in return for campaign contributions by ADM
- Final award (2005)
 - Governor's action based on objective scientific review under nondiscriminatory legislation
 - No credible evidence of collusion between Gov. Davis and ADM

Other Regulation of MTBE

- 16 US states have acted to restrict or eliminate use of MTBE
 - Major states (e.g., New York) concerned with groundwater contamination
 - Corn-producing states banning MTBE were never major users
- MTBE still widely used in Europe
- No regulatory action by USEPA on health concerns

Answers to Questions Posed

- Do the facts of the cases indicate that foreign investors are escaping fair application of national environmental measures?
- Answer: No.
- MMT
 - Measure reflected still-unsubstantiated health concerns
 - Measure not taken under environmental law; not consistent with federal environmental law or regulators' assessment of risk
 - Federal government used trade restrictions to advance mixed goals, mostly non-environmental (economic and political considerations)
- Compare with Metalclad
 - Environmental measure taken without full study or public discussion; no implementation of ecological protections
 - Even if a *bona fide* environmental measure, effectively expropriated investment and therefore requires compensation

■ MTBE

- Legislation responded to observed and widespread contamination of drinking water supplies
- Independent scientific study undertaken before, and as precondition for, regulatory action
- Facially nondiscriminatory measure affecting all producers of MTBE
 - Disparate impact on foreign investor allowed absent deliberate intention to favor domestic competitor
 - Compare with S.D. Myers
 - Tribunal finding of primarily protectionist intent
 - No “legitimate environmental reason” for export ban

- Do government actions in response to Chapter 11 awards show “chilling” of environmental protection efforts?
- Answer: Difficult to draw clear conclusions
- Evidence against chilling effect
 - Banning of MTBE by other states in US
 - Mexican Congress enacts more comprehensive hazardous waste management program
- Other environmental regulation decisions may, or may not, have been influenced by Chapter 11 concerns
 - Any chilling effect may be reduced by Methanex final award denying compensation

Overall Evaluation of Environmental Effect of Chapter 11

- In 2 cases, environment might have been better off *without* the challenged government action
 - Metalclad
 - Foreign investors discouraged from building much-needed modern hazardous waste management facilities in Mexico
 - Perpetuation of illicit waste disposal
 - S.D. Myers
 - Closing access to Ohio facility delayed destruction of PCB stocks in eastern Canada
 - Swan Hills, Alberta facility poorly operated and distant
 - Higher environmental risk for PCB disposal

- In 2 cases, no adverse environmental effect
 - Methanex/MTBE
 - California proceeded with MTBE ban even while Chapter 11 claim was pending
 - Other states also banned or restricted MTBE
 - Ethyl/MMT
 - Post-Ethyl studies of urban air quality (Toronto) indicate very low levels of manganese
 - Refiners in Canada (and other countries) voluntarily agree to stop use of MMT
 - Value of public pressure; non-regulatory approaches

Final Observations

- On procedure, environmentalist critique of investor-State arbitration had merit
 - NAFTA trade ministers have formally agreed to make arbitration proceedings more open and transparent, with opportunity for participation through *amicus* briefs
- On substance, claim of Chapter 11 threat to environmental protection is overdrawn
 - Earliest cases (Ethyl, Metalclad, and S.D. Myers) involved government use of environment as pretext for protectionist or political measures
 - Methanex final award should ease lingering concerns
 - Some environmental policy improvements after compensation awards, especially in Mexico post-Metalclad
 - Early wave of environmental cases has subsided
 - Several “environmental” claims never pursued
 - Only one environmental Chapter 11 claim in past 6 years