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International Investment, Expropriation and Environmental Protection

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ARTICLE

INTERNATIONAL INVESTMENT, EXPROPRIATION AND ENVIRONMENTAL PROTECTION

BY J. MARTIN WAGNER*

*Government could hardly go on if to some extent values
incident to property could not be diminished without
paying for every ... change in the general law
[S]ome values are enjoyed under an implied limitation
and must yield to the police power.*

—*Oliver Wendell Holmes*¹

I. INTRODUCTION

International law has long protected foreign property from expropriation—confiscation by the host-country government—by giving the owner of the property a right to compensation for the value of the lost property. In recent decades, foreign property owners have made claims for compensation based on governmental regulations, such as placing restrictions on the legal use of property, that do not actually remove the owner's title to

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1. *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 413 (1922).

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the property, but nevertheless substantially affect its value. As this doctrine of "indirect expropriation" has developed, international tribunals and legal scholars have cautioned that the obligation to compensate does not extend to regulations imposed pursuant to the exercise of legitimate government police powers, such as taxation and protection of human health and welfare. To require otherwise would, as Oliver Wendell Holmes noted, severely limit the ability of governments to promote the general welfare.

In recent decades, the harmful effect of human activities on the environment and the connection between environmental health and human well-being have become obvious. Recognizing these relationships makes clear the need for governmental restrictions on environmentally harmful activities. In addition, a key tenet of environmental protection is that those responsible for harming the environment should bear the cost of protecting it. In this light, one might imagine that environmental regulations would be safe from claims that their economic impact on private property constitutes indirect expropriation and thus gives property owners a right to compensation. In the past few years, however, several cases have challenged that assumption.

Like many other international agreements, the North American Free Trade Agreement (NAFTA) requires compensation for direct or indirect expropriation of foreign investment. In an unprecedented move, companies have begun to use this protection to challenge measures promoted by governments as necessary to protect the environment and human health. A U.S. company running a hazardous waste disposal facility in Mexico is seeking \$90 million in compensation from Mexico for losses incurred when the local government refused to permit operation of the plant because of its discovery that the local geology made it likely that the waste treated at the plant would contaminate local water supplies. Another U.S. toxic waste disposal company has claimed that Canada should pay it at least \$10 million for losses arising out of a 15-month Canadian ban on the export of a particularly volatile hazardous waste. Canada asserted that the ban was necessary to ensure that the waste would be treated safely, preventing contamination in

Canada and the United States that might arise if treatment was inadequate. In the most publicized case, a U.S. manufacturer of a gasoline additive settled a compensation claim against Canada, obtaining a payment of \$19 million (it had sought \$250 million) and convincing Canada to rescind a ban on the importation of the additive. Although Canada had initially promoted the ban as necessary to avoid risks that the additive posed to the environment and human health, part of the settlement included a statement by the Canadian government that it did not have "sufficient evidence" on which to base a "clear case" that the additive was causing the asserted harm.

As these NAFTA cases make clear, giving companies the right to base compensation claims on the economic impact of environmental regulations has a serious chilling effect on the ability and willingness of governments to implement such regulations. Governments that do so risk being penalized by having to divert precious governmental resources to defend the regulations against expropriation claims and to pay compensation payments if the defense is unsuccessful. Moreover, as the Canadian gasoline additive case suggests, such penalties may be great enough that a government may not be able to maintain a regulation it has deemed necessary. To make matters worse, the provisions on which these claims have been based are the model for efforts to expand investment protection regionally, in the Free Trade Agreement of the Americas (FTAA), and globally, in the Multilateral Agreement on Investment (MAI) or an equivalent global agreement.

Despite the claims that have been brought under NAFTA, and the one settlement reached, none of the cases has yet been resolved by a tribunal. Moreover, the companies making the claims have objected that the regulations have not really been environmentally motivated. It thus remains uncertain the extent to which the NAFTA investment protections apply to environmental regulations.

The Canadian government has expressed the desire to draft an interpretive "rider" to Chapter 11 to clarify and limit the

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investor-state provisions.² The Canadian trade minister has suggested that the United States and Mexico support this effort³ and the ministers have apparently agreed to “focus attention” on the issue at an April 1999 meeting in Ottawa.⁴ Canada has proposed making nations’ domestic laws on expropriation the standard for international panels to use in investor-state challenges.⁵ An attorney who has represented U.S. companies in three NAFTA investment challenges against Canada has objected that Canada’s position would result in “a definition of expropriation that’s less than the internationally accepted definition of expropriation.”⁶ However, as this Article demonstrates, international law does not require governments to provide compensation for the economic impact of most legitimate environmental laws or regulations. Such freedom to regulate is necessary if governments are to be able to protect the environment.

NAFTA does not clearly define the actions covered by its expropriation provisions. Interpretation of the provisions will thus depend in part on international law and the domestic traditions of the negotiating parties. This Article argues that both international and U.S. law preserve the right of governments to regulate to protect the environment without having to compensate for the impact of such regulations on investment. After a brief description of the relationship between foreign investment and the environment in Part II, the Article will describe the protection against expropriation provided by international agreements, briefly discussing bilateral investment agreements and then detailing the protection provided by NAFTA and the MAI in Part III. Part IV will then describe the challenges to environmental laws that have been brought un-

2. Greenwire, Feb. 23, 1999, at 22 (citing JOURNAL OF COMMERCE, Feb. 23, 1999).

3. See AMERICASTRADE, Dec. 24, 1998, at 22-23. According to the Canadian trade minister, both the United States and Mexico supported Canada’s efforts to narrow the interpretation of expropriation in the Multilateral Agreement on Investment (MAI) at an Organization for Economic Cooperation and Development (OECD) meeting. *Id.*

4. Greenwire, Feb. 23, 1999, at 22 (citing JOURNAL OF COMMERCE, Feb. 23, 1999).

5. See AMERICASTRADE, Mar. 11, 1999, at 1. Such a clarification would “state that no party may directly or indirectly nationalize or expropriate an investment in a manner that would be inconsistent with its own principles of domestic law.” *Id.* at 11.

6. Barry Appleton, *quoted in id.* at 12.

der NAFTA's investment chapter. Next, Part V will examine the treatment of indirect expropriation under U.S. and international law. Part VI will demonstrate that, under NAFTA and international expropriation and environmental law, environmental measures should not normally give rise to a right to compensation. Finally, the Article will conclude with some proposals for ensuring that NAFTA, and other investment agreements, do not interfere with the ability of governments to take action to protect the environment.

II. FOREIGN INVESTMENT AND THE ENVIRONMENT

The global influence of foreign private capital has increased substantially in recent years. For example, from 1990 to 1996, the amount of private capital flowing to developing countries increased over tenfold, from US \$22 billion to US \$244 billion.⁷

The increased flow of private capital directly affects environmental protection. Governments compete to attract this capital, in large part by changing regulations affecting foreign investments.⁸ One economist studying this phenomenon with respect to environmental regulations has concluded that

a concern to be attractive to foreign investors in a highly competitive global economy has kept a lid on local/national [environmental] standards or enforcement of standards. While there has not been a universal "race to the bottom," increased globalization [of foreign investment] ... has inhibited a "race to the top" and caused environmental commitments to be "stuck in the mud."⁹

7. See Gretta Goldenman, *The Environmental Implications of Foreign Direct Investment: Policy and Institutional Issues 2* (OECD Conf. on FDI and the Env't, Jan. 29, 1999), OECD Doc. CCNM/EMEF/EPOC/CIME(98)3 <<http://www.oecd.org/daf/env>> (on file with the author).

8. See *id.* at 2, 4 (citing 1997 UNCTAD study indicating that 90% of changes in laws governing foreign direct investment "were aimed at creating a more favourable climate for [investment]").

9. Lyuba Zarsky, *Havens, Halos and Spaghetti: Untangling the Evidence About Foreign Direct Investment and the Environment* (OECD Conference on Foreign Direct

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As a result of the conflict between the desire to attract investment and strong environmental protection, greater opening of markets to foreign direct investment “may lead to patterns of investment and production that are not desirable in that market conditions do not adequately allow for the internalization of social (including environmental) costs.”¹⁰ Internalizing environmental costs — meaning shifting the cost of environmental harm from society at large to the person causing the harm — is a fundamental element of environmental protection.¹¹ This principle, called the “polluter pays principle,” was recognized internationally in the Rio Declaration on Environment and Development:

National authorities should endeavor to promote the internalization of environmental costs and the use of economic instruments, taking into account the approach that the polluter should, in principle, bear the cost of pollution.¹²

Investment and the Environment, Jan. 29, 1999) OECD Doc. CCM/EMEF/EPOC/CIME(98)5 at 3. Zarsky concluded that, with respect to the environmental effects of investment, “regulation matters.” *Id.* at 20.

10. J(Hans) B. Opschoor, *Multilateral Agreements on Investment and the Environment* 9 (OECD Conf. on FDI and the Env’t, Jan. 29, 1999) <<http://www.oecd.org/daf/env>> (on file with author).

11. The polluter pays principle began as an economic principle formulated in the 1970s by the OECD. The OECD agreed that

[t]he principle to be used for allocating costs of pollution prevention and control measures to encourage rational use of scarce environmental resources and to avoid distortions in international trade and investment is the so-called “Polluter-Pays Principle.” This principle means that the polluter should bear the expenses of carrying out the above-mentioned measures decided by public authorities to ensure that the environment is in an acceptable state. In other words, the cost of these measures should be reflected in the cost of goods and services which cause pollution in production and/or consumption. Such measures should not be accompanied by subsidies that would create significant distortions in international trade and investment.

Recommendation on Guiding Principles Concerning International Economic Aspects of Environmental Policies, OECD, C(72)128 (1972) (hereinafter “OECD Guiding Principles”).

12. Rio Declaration on Environment and Development, United Nations Conference on Environment and Development, U.N. Doc. A/CONF.151/5/Rev. 1 (1992), princ. 16, reprinted in 31 I.L.M. 876, 879 (hereinafter “Rio Declaration”). The principle, which has been called “a general principle of international environmental law,” International Convention on Oil Pollution Preparedness, Response, and Cooperation, Nov. 30, 1990, pmbl., 30 I.L.M. 733, 736, has been adopted in numerous other international agreements. See, e.g., 1986 Single European Act, June 29, 1987, 1987 O.J. (L 169) art.

The decision to internalize the cost of pollution or other harm to the environment, rather than requiring society in general to bear that cost, goes to the very heart of the question of indirect expropriation. The United States Supreme Court has explained that the determination that the government must pay compensation for the impact of its action on property “is, in essence, a determination that the public at large, rather than a single owner, must bear the burden of an exercise of state power in the public interest.”¹³ Thus, requiring the government to provide compensation for the impact of environmental laws or regulations on property — *i.e.*, determining that “the public at large” must bear the burden of that regulation — is directly at odds with the polluter pays principle.

While this brief discussion clearly suggests that environmental laws and regulations should not give rise to a governmental obligation to compensate in any but the most extreme situations, some foreign investors have taken a different view. The resolution of this question is thus of great significance to both investors and governments:

[T]o the investor, the line of demarcation between measures for which no compensation is due and actions qualifying as indirect expropriations [that require compensation] may well make the difference between the burden to operate (or abandon) a non-profitable enterprise and the right to receive full compensation (either from the host State or under an insurance contract). For the host State, the definition determines the scope of the State’s power to enact legislation that regulates the rights and obligations of owners in instances where compensation may fall due. It may be argued that the

130r(2), as amended by the 1992 Maastricht Treaty, Feb. 7, 1992, 1992 O.J. (L/224/1), *reprinted in* 31 I.L.M. 247; Convention for the Protection of the Marine Environment in the Northeast Atlantic, Sept. 22, 1992, art. 2(2)(b) <<http://sedac.ciesin.org/pidp/texts/acrc/MEofNE.txt.html>> (on file with author); Convention for the Protect of the Marine Environment of the Baltic Sea, Apr. 9, 1992, art. 3(4) <<http://www.helcom.fi/conven92.html>> (on file with author); Helsinki Convention on the Protection and Use of Transboundary Watercourses and International Lakes, March 17, 1992, art. 2(5), 31 I.L.M. 1312, 1316.

13. *Agins v. Tiburon*, 447 U.S. 255, 260 (1995).

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State is prevented from taking any such measures where these cannot be covered by public financial resources.¹⁴

III. INTERNATIONAL INVESTMENT AGREEMENTS

Nations have codified protection against expropriation in various forms of international agreements. Although the most common source of such protection are bilateral investment agreements, nations have begun to include expropriation provisions in multilateral agreements. It is in the context of these agreements that the international community will determine whether environmental regulations may constitute a compensable expropriation.

A. BILATERAL INVESTMENT AGREEMENTS

In recent decades, nations have significantly increased their use of bilateral agreements to protect foreign investment from expropriation. In 1990, there were 435 bilateral investment agreements (BITs); by March 1998, that number had increased to 1300.¹⁵ In addition to providing protection for U.S. investments abroad, the United States sees its BITs as having a “significant impact” on the worldwide adoption of U.S. policies on the treatment of foreign investment in countries undergoing economic reform, and laying “the policy groundwork for broader multilateral initiatives in the [OECD] and eventually, the [WTO].”¹⁶

14. RUDOLF DOLZER & MARGRETE STEVENS, *BILATERAL INVESTMENT TREATIES* 99-100 (1995).

15. See Alan Larson, Asst. U.S. Secretary of State for Economic, Business and Agricultural Affairs, *Testimony before the House International Regulations Committee, Subcommittee on Int'l Econ. Pol'y and Trade*, Mar. 6, 1998, (visited Jan. 26, 1999) <http://www.state.gov/www/policy_remarks/1998/980306_larson_mai.htm> (on file with author) [hereinafter Larson Testimony]. Between the mid-1980s and March 1998, the United States had negotiated 41 BITs. *Id.*

16. US DEPARTMENT OF STATE, *FACT SHEET: U.S. BILATERAL INVESTMENT TREATY PROGRAM* (Apr. 16, 1997) [hereinafter FACT SHEET].

Nearly all BITs provide protection against expropriation.¹⁷ The majority also cover indirect expropriation,¹⁸ using phrases such as “having effect equivalent to ... expropriation,” “any direct or indirect measure” of expropriation, “any other measure having the same nature or the same effect against investments,” or “all other measures whose effect is to dispossess, directly or indirectly, the investors.”¹⁹ BITs to which the United States is party generally provide protection against “expropriation or nationalization (directly or indirectly through measures tantamount to expropriation or nationalization).”²⁰ According to a study by the Investment Group of the Negotiators of the Free Trade Agreement of the Americas, “[i]n all cases, the language [of BITs] is broad and allows for coverage of so-called ‘creeping’ or ‘indirect’ expropriations, that is, measures having the same effect to expropriation.”²¹

Because BITs seldom define expropriation in any detail, the general rules of international law should inform the interpretation of this term.²² Considering expropriation as included in U.S. BITs, one scholar has stated: “Consistent with article X, paragraph 1 of the U.S. Model BIT, principles of international law, and law under the fifth amendment to the U.S. Constitution, measures taken by competent authorities of either party

17. See DOLER & STEVENS, *supra* note 14, at 98. BITs may use different words to describe the concept of expropriation, such as “dispossession,” “taking,” “deprivation” or “privation.” *Id.*

18. See *id.* at 97, 99.

19. *Id.* at 100-01.

20. FTAA INVESTMENT GROUP, INVESTMENT TREATIES IN THE WESTERN HEMISPHERE: A COMPENDIUM at 19. See also DOLZER & STEVENS, *supra* note 14, at 102 (citing 1992 U.S. model treaty, art. III).

21. FTAA INVESTMENT GROUP, *supra* note 20, at 19.

22. The United States considers that its BITs provide protection against expropriation “in accordance with international law standards.” FACT SHEET, *supra* note 16. A few US BITs have elaborated on the meaning of expropriation, stating that it includes “the levying of taxation, the compulsory sale of all or part of an investment, or the impairment or deprivation of its management, control or economic value.” DOLZER & STEVENS, *supra* note 14, at 102 (quoting U.S.-Zaire BIT (1984), art. III). See also FTAA INVESTMENT GROUP, *supra* note 20, at 19 (quoting US-Haiti BIT). Professors Dolzer and Stevens have noted that such an elaboration “represents possibly the broadest scope in investment treaties with respect to indirect expropriation insofar as the inclusion of measures that cause the ‘impairment ... of [the] economic value’ of an investment equates expropriation with a host of measures which might not otherwise be considered as such under general international law, let alone under liberal systems of domestic law.” DOLZER & STEVENS, *supra* note 14, at 102.

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in the legitimate, nondiscriminatory exercise of its police power, which reduce an investment value, do not constitute expropriation within the meaning of article III [of the Model BIT].²³

B. NAFTA

The international community has come to believe that using BITs to protect investment is “non-transparent and potentially inefficient,” leading to a shift in favor of a multilateral approach to investment protection.²⁴ Consistent with this approach, Chapter 11 of the North American Free Trade Agreement (NAFTA) regulates the treatment by Parties of foreign investors and foreign investments.²⁵

The NAFTA investment chapter establishes two kinds of requirements with respect to foreign investment. First, each country must treat foreign investors or their investments as well as or better than it treats any other investments in that country. Thus, foreign investors and investments must receive the better of²⁶ (a) the treatment provided to a country’s own investors or investments in like circumstances (national treatment)²⁷ and (b) the best treatment provided to the investors or investments of any other nation, whether or not it is a party (most-favored-nation treatment).²⁸ Second, the Agreement prohibits governments from imposing certain requirements on foreign investments. One such provision prohibits certain per-

23. Pamela B. Gann, *The U.S. Bilateral Investment Treaty Program*, 21 STAN. J. INT’L L. 373, 399 n. 120 (1985).

24. See Opschoor, *supra* note 10.

25. North American Free Trade Agreement, December 8 and 17, 1992, Chapter 11, 32 I.L.M. 638 (1993). The Agreement’s definition of “investment” is extremely broad, including an “enterprise”; securities, loans to, or interest in the assets or profits of an enterprise; tangible or intangible real estate or other property acquired for economic benefit; and interests from the commitment of capital or other resources to economic activities. See *id.* art. 1139.

26. See *id.* art. 1104 (requiring parties to provide “the better of the treatment required by Articles 1102 and 1103”).

27. See *id.* art. 1102. States or provinces of a nation must accord treatment at least as favorable as provided to any investor or investment of the country of which they are a part. See *id.* art. 1102(3).

28. NAFTA, *supra* note 25, art. 1103. The national and most-favored-nation treatment requirements apply to the “establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.” *Id.*

formance requirements, such as requiring foreign investors to supply products or services to a specific regional or world market, to export a specified volume of their products or services, to use a certain amount of domestic components, or to transfer technology to an entity in the country's territory.²⁹ Other provisions prohibit imposing nationality requirements on senior managers of an enterprise³⁰ or placing restrictions on transfers relating to investments, including payments made pursuant to arbitration under the investment provisions.³¹

Article 1110 protects against the "expropriation" of foreign investments:

1. No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ("expropriation"), except:

- (a) for a public purpose;
- (b) on a non-discriminatory basis;
- (c) in accordance with due process of law and Article 1105(1);^[32] and
- (d) on payment of compensation in accordance with [subsequent paragraphs specifying valuation of expropriations and form and procedure of payment].³³

When a foreign investor believes that a government has expropriated its investment, Chapter 11 gives the investor a direct right to force the government of the country in which the investment is located into binding arbitration to resolve the

29. *See id.* art. 1106.

30. *See id.* art. 1107(1).

31. NAFTA, *supra* note 25, art. 1109. Such transfers also include profits, dividends, fees and payments, and proceeds of sales. *See id.*

32. Article 1105(1) provides: "Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security."

33. *Id.* art. 1110.

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claim.³⁴ The investor may submit its claim under one of three sets of rules for resolving international investment disputes.³⁵ Arbitration is generally conducted by a three-member tribunal.³⁶ At the request, or with the approval, of the disputing parties, the arbitrators may seek expert assistance concerning environmental, health, safety or other scientific issues of fact.³⁷ Under any of the applicable arbitration rules, the proceedings and findings of the tribunals are confidential and may be made public only if both parties agree.³⁸ It is also important to note that the arbitration rules do not permit participation by or submissions from interested or affected non-parties.³⁹

34. *See id.* arts. 1115-38.

35. *See id.* art. 1120(1). These rules are those established by the International Centre for the Settlement of Investment Disputes (ICSID), Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Mar. 18, 1965, 575 U.N.T.S. 159 (hereinafter "ICSID Convention"), provided that the disputing Party and the Party of the investor are parties to the ICSID Convention (Canada is not); the Additional Facility Rules of ICSID, if either (but not both) the disputing Party or the Party of the investor is a Party to the ICSID Convention; or the Arbitration Rules of the UN Commission on International Trade Law, approved by the UN General Assembly on Dec. 15, 1976. Three of the first four NAFTA chapter 11 disputes were filed with the ICSID, which is apparently pushing to be the "tribunal of choice" for NAFTA challenges. *See AMERICASTRADE*, June 11, 1998, at 4.

36. *See NAFTA*, *supra* note 25, art. 1123. Each party to the arbitration appoints one arbitrator and they must agree on the third. *See id.* If they cannot agree within 90 days, either party may request that the Secretary-General of the ICSID appoint the remaining arbitrator. *See id.*

37. *See id.* art. 1133.

38. *See e.g.*, *Rules of Procedure for Arbitration Proceedings*, ICSID, Rule 32(2) (visited April 8, 1999) <<http://www.internationalaladr.com/tc1151.htm>> (on file with author) ("The tribunal shall decide, with the consent of the parties, which other persons besides the parties...may attend the hearings."); *Rules of Arbitration of the International Chamber of Commerce*, art. 21.3 (visited Dec. 15, 1998) <<http://www.iccwbo.org/html/rulesenglish.htm>> (on file with author) (without approval of arbitral tribunal, "persons not involved in the proceedings shall not be admitted"); *id.* App. I, Statutes of the International Court of Arbitration of the ICC, art. 6 ("The work of the Court is of a confidential nature and must be respected by everyone who participates in that work in whatever capacity."); *id.* App. II, Internal Rules of the International Court of Arbitration of the ICC, art. 1 (sessions of Court open only to members, except upon invitation by Court; documents confidential). The attorney for one of the NAFTA chapter 11 claims brought against Canada defended the confidentiality provisions as preventing long and costly court litigation through an agreement to provide a greater number of internal documents in return for confidentiality. *Inter-Press Service*, Sept. 23, 1998, at 4.

39. *See, e.g.*, *Rules of Arbitration of the International Chamber of Commerce*, *supra* note 38, art. 21.3. In US courts, individuals or organizations with an interest in a case can participate as a "friend of the court" or, if resolution of the case will affect their

The tribunal must decide the claim in accordance with the NAFTA and “applicable rules of international law.”⁴⁰ If the tribunal finds that the Party’s action was “tantamount to nationalization or expropriation,” it may award monetary damages and interest, restitution of property and/or costs of bringing the claim.⁴¹

Once an arbitral award is final, the investor has several options for ensuring that it obtains payment from the country in question. First, Chapter 11 requires each Party to “provide for the enforcement of an award in its territory.”⁴² The investor may also request that its own government espouse its claim before the NAFTA Free Trade Commission, which then must initiate an intergovernmental arbitration to determine whether the failure to comply with the award is inconsistent with the obligations of NAFTA and, if appropriate, to recommend that the Party comply.⁴³ Finally, the investor may seek enforcement under the international arbitration rules recognized in Chapter 11.⁴⁴ One such rule, for example, requires each government to treat arbitration awards

as binding and enforce the pecuniary obligations imposed by that award within its territory as if it were a final judgment of a court in that State. A Contracting State with a federal constitution may enforce such an award in or through its federal courts and may provide that such courts shall treat the award as if it were a final judgment of the courts of a constituent state.⁴⁵

rights or interests strongly enough, they can actually intervene as a party. See FED. R. CIV. P. 24, FED. R. APP. P. 29.

40. NAFTA, *supra* note 25, art. 1131(1).

41. *Id.* art. 1135. The arbitrators may not award punitive damages. See *id.* at 646, art. 1135.3.

42. *Id.* art. 1136.4.

43. *Id.* art. 1136.5.

44. See NAFTA, *supra* note 25, art. 1136.6.

45. ICSID Convention, *supra* note 35, at 194, art. 54(1). This requirement is implemented in 22 U.S.C. § 1650(a), which provides that arbitral awards rendered pursuant to the ICSID Convention

shall create a right arising under a treaty of the United States. The pecuniary obligations imposed by such an award shall be enforced and shall be given the same full faith and credit as if the award were a final judgment of a court of

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NAFTA's investment provisions are subject to several provisions regarding the environment. First, the investment chapter itself includes a provision on "Environmental Measures":

1. Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure^[46] otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns.

2. The Parties recognize that it is inappropriate to encourage investment by relaxing domestic health, safety or environmental measures. Accordingly, a Party should not waive or otherwise derogate from, or offer to waive or otherwise derogate from, such measures as an encouragement for the establishment, acquisition, expansion or retention in its territory of an investment of an investor.⁴⁷

In addition to the investment-specific environmental provisions, several other NAFTA provisions highlight environmental issues. The Preamble states the Parties' intention to achieve NAFTA's goals "in a manner consistent with environmental protection and conservation," to "promote sustainable development," and to "strengthen the development and enforcement of environmental laws and regulations."⁴⁸

Additional protection for environmental measures is made through the incorporation of the general exceptions to the Gen-

general jurisdiction of one of the several States.... The district courts of the United States ... shall have exclusive jurisdiction over actions and proceedings under [these provisions].

22 U.S.C. § 1650(a). See also *LETCO v. Liberia*, 650 F. Supp. 73, 76 (S.D.N.Y. 1986) (court has jurisdiction to enforce award rendered pursuant to ICSID procedures).

46. NAFTA defines "measure" as including "any law, regulation, procedure, requirement or practice." NAFTA, *supra* note 25, art. 201.1.

47. *Id.* art. 1114. If a Party considers that another Party has relaxed measures to attract investment, "it may request consultations with the other Party and the two Parties shall consult with a view to avoiding any such encouragement." *Id.* art. 1114.2.

48. *Id.* pmb1.

eral Agreement on Tariffs and Trade.⁴⁹ Those exceptions provide:

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where similar conditions prevail, or a disguised restriction on international trade, nothing in [the GATT] shall be construed to prevent the adoption or enforcement by any contracting party of measures:

(b) necessary to protect human, animal or plant life or health;

(g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.⁵⁰

Any consideration of the treatment of environmental measures under NAFTA must also take into account the North American Agreement on Environmental Cooperation (NAAEC), the "environmental side agreement" to NAFTA.⁵¹ In the NAAEC, the Parties to NAFTA recognized the need to conserve, protect and enhance the environment in their territories and reaffirmed the importance of "enhanced levels of environmental protection."⁵² Among the environmental objectives of

49. *Id.* art. 2101 ("GATT Article XX and its interpretative notes ... [is] incorporated into and made part of this Agreement."). The investment chapter specifically states that "[i]n the event of any inconsistency between this Chapter and another Chapter, the other Chapter shall prevail to the extent of the inconsistency." *Id.* art. 1112.

50. General Agreement on Tariffs and Trade, Oct. 30, 1947, art. XX, 55 U.N.T.S. 194, 262 [hereinafter GATT]. NAFTA clarifies two points regarding these exceptions that have been challenged under the GATT procedures: that Article XX(b) includes environmental measures and that both living and non-living natural resources fall within Article XX(g). NAFTA, *supra* note 25, art. 2101.1.

51. North American Agreement on Environmental Cooperation (NAAEC), Sept. 8, 9, 12, 14, 1993, Can.-Mex.-U.S., 32 I.L.M. 1480.

52. *Id.* prml. The preamble to the NAAEC also reaffirmed the countries' commitment to the Stockholm Declaration on the Human Environment and the Rio Declaration on Environment and Development, both of which recognize that "environmental protection shall constitute an integral part of the development process and cannot be considered in isolation from it." Rio Declaration, *supra* note 12, princ. 4. *See also*

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the NAAEC are to “foster the protection and improvement of the environment ... for the well-being of present and future generations”; to cooperate to “better conserve, protect and enhance the environment,” and develop and improve environmental laws and regulations; to “enhance compliance with, and enforcement of, environmental laws and regulations”; and to “promote pollution prevention policies and practices.”⁵³

One of the NAAEC’s most important provisions concerning environmental laws and regulations is Article 3:

Recognizing the right of each Party to establish its own levels of domestic environmental protection and environmental development policies and priorities, and to adopt or modify accordingly its environmental laws and regulations, each Party *shall ensure that its laws and regulations provide for high levels of environmental protections and shall strive to continue to improve those laws and regulations.*⁵⁴

As these provisions demonstrate, any interpretation or application of NAFTA’s investment provisions must take into account the importance that the Parties placed on preventing the agreement from interfering with environmental protection.

C. THE MULTILATERAL AGREEMENT ON INVESTMENT (MAI)

Investment protections like those provided by NAFTA, including protection against expropriation, are included in regional agreements in other parts of the world⁵⁵ and may soon become part of a global investment agreement. The European

United Nations Conference on the Human Environment, Stockholm Declaration on the Human Environment, June 16, 1972, princ. 6, U.N. Doc. A/Conf.48/14, *revised by* U.N. Doc. A/Conf.48/14/Corr.1 (1972), 11 I.L.M. 1416 (1972) (“To defend and improve the human environment for present and future generations has become an imperative goal for mankind...”).

53. NAAEC, *supra* note 51, art. 1.

54. *Id.* art. 3 (emphasis added).

55. *See, e.g.*, An Agreement for the Promotion and Protection of Investments, Dec. 15, 1987, ASEAN Nations, 27 I.L.M. 612; European Energy Charter Treaty, *reprinted in* UNCTAD, II INTERNATIONAL INVESTMENT INSTRUMENTS: A COMPENDIUM 539 (1996).

Union and Mexico are discussing a free trade agreement that is likely to include investment protections in some form.⁵⁶ In addition, the Free Trade Agreement of the Americas (FTAA) is likely to include investment provisions.⁵⁷

The first serious proposal to apply investment protections on a global level came from the Organization for Economic Cooperation and Development (OECD), a group of 29 of the world's richest countries.⁵⁸ Since 1995, the OECD has been negotiating the Multilateral Agreement on Investment (MAI), the goal of which was to "create a comprehensive investment discipline, backed up by a dispute settlement mechanism which includes investor to state procedures."⁵⁹ In October 1998, as a result of "significant concerns" regarding the agreement, including "issues of sovereignty, protection of labour rights and environment, culture and other important matters," the OECD indefinitely suspended further negotiations on the agreement.⁶⁰

56. See *Mexico, EU FTA Proposals Clash over Coverage of Investment, Services*, AMERICASTRADE, Nov. 26, 1998, 1.

57. See AMERICASTRADE, Nov. 26, 1998 at 1; AMERICASTRADE, Sept. 17, 1998 at 5. The United States considers the NAFTA investment chapter "comparable to a BIT" and considers its BITs to "complement and support regional initiatives on investment liberalization in the Asia Pacific Economic Cooperation forum (APEC) and the [FTAA] initiative." FACT SHEET, *supra* note 16.

58. The member countries are Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States. OECD countries share "principles of the market economy, pluralist democracy and respect for human rights." OECD, *Membership*, <<http://www.oecd.org/about/general/member-countries.htm>> (on file with author). OECD countries produce two-thirds of the world's goods and services. See *id.* See also *What is OECD*, <<http://www.oecd.org/about/general/index.htm>> (on file with author).

59. Jan Huner, *Environment Regulation and International Agreements: Lessons from the MAI* (paper delivered at the Royal Institute for International Affairs Conference on Trade, Investment and Environment, Oct. 29-30, 1998), <<http://www.island-net.com/~ncfs/maisite/pov-mai3.htm>> (on file with author).

60. OECD *News Release*, (Oct. 23, 1998) <http://www.oecd.org/news_and_events/release/nw98-101a.htm> (on file with author). The OECD had temporarily suspended MAI negotiations in April 1998, intending to resume efforts in November after a period of consultation with representatives of civil society. *Environmentalists Claim Victory as Talks on Multilateral Investment Pact Founder*, 21 INT'L ENV'T REP. No. 22 at 1053 (Oct. 28, 1998). According to the Secretary of the OECD's MAI Negotiating Group, the primary problem with the MAI was that

its negotiators did not expect to have to sell it politically. Most of the MAI-negotiators are (were) investment specialists not used to viewing from a politi-

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Despite the suspension, there remains a consensus among OECD member countries on "the need for and value of a multilateral framework for investment. The goal should still be sought."⁶¹ The OECD's continued interest in the subject is reflected in its conference on Foreign Direct Investment and the Environment, held at The Hague, January 28-29, 1999.⁶² It is thus likely that efforts to develop such a global investment agreement will resume in the near future, possibly under the auspices of the WTO.⁶³ In addition, "investment discussions in UNCTAD, the WTO, APEC and the FTAA are all looking to the MAI as a model for multilateral rules."⁶⁴

In April 1998, partly as a result of criticism that the MAI negotiations had been too secretive,⁶⁵ the OECD released what

cal perspective the concepts that they consider logical and essential parts of an investment discipline.... Least of all [did they expect] to see the MAI portrayed as a threat to environmental protection.

Huner, *supra* note 59. Huner also notes that "the issue of how the MAI relates to multilateral environmental agreements (MEA's) was not discussed" during the early years of MAI negotiations and, with the exception of Washington, was likely "not a subject for debate in [national] capitals either." *Id.* The Chairman of the Negotiating Group made a last-ditch effort to salvage MAI negotiations by proposing a package of environment and labor provisions, but "the Europeans saw too many NAFTA-inspired texts, and the Americans opposed making the not lowering of standards clause binding." *Id.*

61. OECD News Release, *supra* note 60.

62. See *Foreign Direct Investment and the Environment*, <<http://www.oecd.org/daf/env/index.htm>> (on file with author).

63. See 21 INT'L ENV'T REP. No. 22 at 1053, *supra* note 60. Opschoor, *supra* note 10. The April 1998 OECD ministerial declaration stated that the OECD governments "support the current work programme on investment in the WTO and once the work programme has been completed will seek support of all their partners for the next steps towards the creation of investment rules in the WTO." OECD, *Ministerial Statement on the Multilateral Agreement on Investment (MAI)*, Apr. 28, 1998, (visited on Oct. 26, 1998) <http://www.oecd.org/news_and_events/release/nw98-50a.htm> (on file with author).

64. Larson Testimony, *supra* note 15.

65. The Secretary of OECD's MAI Negotiating Group (NG) has explained that [w]hen pressure from NGO's [concerning the secrecy surrounding MAI negotiations] began to rise, the chairman of the NG suggested that NG documents, in particular draft texts, had perhaps better be declassified. This was not approved by a minority of countries. One of the arguments for not releasing texts was that in doing so [the OECD countries] might find ourselves having to negotiate with NGO's about them. This prompted Canada to say that it had already put draft texts on the Internet site of the ministry, and it would continue to do so.

Huner, *supra* note 59.

it called the "MAI Negotiating Text," which was a consolidation of "the text of the agreement considered in the course of the MAI negotiations" to that point,⁶⁶ and an official Commentary to the draft.⁶⁷ Although the text is far from final,⁶⁸ and the schedule and process for further negotiations are unclear, it indicates the basic thrust of discussions to this point.

With a few exceptions, the fundamental provisions of the draft MAI are essentially the same as those of NAFTA.⁶⁹ Thus, the Negotiating Text requires the better of national and most-favored-nation treatment,⁷⁰ and prohibits performance requirements⁷¹ and limitations on transfers.⁷²

With respect to expropriation, the MAI Negotiating Text is essentially identical to the NAFTA provision.⁷³ Like NAFTA,

66. *The MAI Negotiating Text* (as of 24 April 1998) <<http://oecd.org/daf/cmisis/mai/maitem.pdf>> (on file with author) [hereinafter *MAI Negotiating Text*].

67. *Commentary to the MAI Negotiating Text* (as of 24 April 1998) <<http://www.oecd.org/daf/cmisis/mai/MAICOME.PDF>> (on file with author) [hereinafter *MAI Commentary*].

68. The text results "mainly from the work of expert groups and [has] not yet been adopted by the MAI Negotiating Group." *Id.*

69. One such exception is the MAI Negotiating Text's definition of "investment," which is broader than NAFTA's. *MAI Negotiating Text, supra* note 66, at 11, I.2 & n.2. According to the OECD Commentary to the MAI Negotiating Text, the definition is intended to cover "all recognized and evolving forms of investment [and] would include the products of an investment." *MAI Commentary, supra* note 67 (emphasis in the original). The Commentary further indicates support for expanding the definition of investment—via the inclusion of assets controlled "indirectly"—to include investments owned or controlled by non-MAI investors, as long as there is some connection to an MAI investor, as through a subsidiary from an MAI country that directly controls the investment or by virtue of the parent of the investor being from an MAI country. *Id.* at 6. An investment of a domestic investor would even be covered if the investor was owned or controlled by a foreign investor from an MAI member country. *See id.* at 2(d).

70. *MAI Negotiating Text, supra* note 66, at 13, III. The MAI Commentary explains that national treatment is violated by de facto as well as de jure discrimination. *MAI Commentary, supra* note 67, at 8.

71. *MAI Negotiating Text, supra* note 66, at 18, III.

72. *Id.* at 59, IV.4.

73. The Secretary of the MAI Negotiating Group noted that the Ethyl-Canada NAFTA dispute, described *infra*, text accompanying notes 106-134, had caused MAI negotiators to "think twice before copying the expropriation provisions of the NAFTA." Huner, *supra* note 59. Nevertheless, the draft MAI provision was nearly identical to the NAFTA provision:

A Contracting Party shall not expropriate or nationalise directly or indirectly an investment in its territory of an investor of another Contracting Party or take any measure or measures having equivalent effect (hereinafter referred to as "expropriation") except:

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the Negotiating Text does not define “expropriation,” but the Commentary notes that by extending protection to “measures having equivalent effect” to expropriation, the Text was intended to cover “creeping expropriation.”⁷⁴

The MAI Negotiating Text follows the NAFTA example for dispute settlement as well, providing investors the right to initiate binding arbitration concerning claims that government action has violated the Agreement and caused “loss or damage to the investor or its investment.”⁷⁵ Although the Text establishes procedures allowing a nation to challenge another nation’s failure to abide by the provisions of the agreement,⁷⁶ it gives priority to challenges brought against nations by investors.⁷⁷

Like NAFTA, if the three-member arbitral panel that finds that a country has violated the Agreement, it may award monetary compensation for injury or losses suffered by the investor⁷⁸ and restitution in kind (meaning the return of the property in question).⁷⁹ In a state to state arbitration, the panel may also recommend that the losing Party bring its actions into conformity with its obligations under the

- a) for a purpose which is in the public interest,
- b) on a non-discriminatory basis,
- c) in accordance with due process of law, and
- d) accompanied by payment of prompt, adequate and effective compensation....

MAI Negotiating Text, *supra* note 66, at 57, IV.2.2.1.

74. *MAI Commentary*, *supra* note 67, at 30, IV.2.5.

75. *MAI Negotiating Text*, *supra* note 66, at 63, V.D.

76. *Id.* at 63-69, V.A-C.

77. A Contracting Party may not initiate proceedings under this Article for a dispute which its investor has submitted, or consented to submit, to arbitration under [the MAI], unless the other Contracting Party has failed to abide by and comply with the award rendered in that dispute or those proceedings have terminated without resolution by an arbitral tribunal of the investor’s claim.

Id. at 65, V.C.1.b.

78. See *MAI Negotiating Text*, *supra* note 66, at 67, V.C.6.c (state-state disputes, proceedings and awards); *id.* at 75, V.D.16.a (investor-state disputes, final awards). In investor-state arbitration, interest from the time of loss or damage is also available. See *id.*

79. In a state-state arbitration, restitution is available only with the agreement of the losing Party; in an investor-state arbitration, the losing Party need not agree, but has the right to pay monetary compensation instead, if restitution is “not practicable.” *Id.* at 67, V.C.6.c (state-state); *id.* at 75, V.D.16.a (investor-state).

Agreement.⁸⁰ The MAI Negotiating Text provides for enforcement of arbitral awards through domestic law, in the case of investor-state disputes,⁸¹ and through retaliatory sanctions in the case of state-state disputes.⁸²

At least some MAI negotiators wanted the agreement to recognize environmental concerns.⁸³ This gave rise to a proposal for a “three-anchor [environmental] approach”:

The first anchor would be the preamble, which should reaffirm Parties’ commitment to the relevant principles of the Rio Declaration and to the relevant multilateral agreements.^[84] The second anchor would be a provision

80. See *MAI Negotiating Text*, *supra* note 66, at 67, V.C.6.c.ii.

81. *Id.* at 76, V.D.16.c (“An arbitration award shall be final and binding between the parties to the dispute and shall be carried out without delay by the party against whom it is issued, subject to its post-award rights under the arbitral systems utilised.”), V.D.18 (“Each Contracting Party shall provide for the enforcement of the pecuniary obligations imposed by an award rendered pursuant to [the investor-state arbitration provisions].”).

82. See *MAI Negotiating Text*, *supra* note 66 at 69, V.C.9. The Negotiating Text is not very well developed on this point. The draft proposes two alternative provisions for giving enforcement powers to states that have received a favorable award with which the challenged state has not complied. One allows the state to “take measures in response” to the noncompliance. *Id.*, V.C.9.a. The other allows it to “suspend the application to the other Contracting party of obligations under this agreement” other than the obligations relating to general treatment and expropriation. *Id.*, V.C.9.a-b. The Text also proposes giving all of the other parties to the MAI some role in approving such measures and suspending the non-complying party’s right to participate in decisions concerning the Agreement. *Id.* V.C.9.c.

83. According to the Secretary of the Negotiating Group, not all OECD members agreed that the MAI should address the environment. Until the victory of the Labour party in the United Kingdom, the UK took a contrary position. See Huner, *supra* note 59. Other opponents were Australia, New Zealand, Korea and Mexico (“perhaps the strongest critic”). *Id.* In addition, these “anchor” environmental provisions were “poorly received in business circles, particularly in the United States.” *Id.* Even the United States—which, in the Secretary’s opinion, was the only nation with experience (from the NAFTA debates) in the relationship between investment and the environment—did not raise environmental issues until late in the negotiations. *Id.*

84. One draft of the MAI’s preamble reaffirmed the parties’ commitment to sustainable development and expressed their recognition that “investment, as an engine of economic growth, can play a key role in ensuring that growth is sustainable, *when accompanied by appropriate environmental policies to ensure it takes place in an environmentally sound manner.*” OECD, *MAI Draft*, October 6, 1997, <<http://www.oecd.org/daf/cmism/mai/negtext.htm>> (emphasis added) (on file with author). The 1998 Negotiating Text proposed a different version:

[Recognizing that appropriate environmental policies can play a key role in ensuring that economic development, to which investment contributes, is sustainable,] and resolving to [desiring to] implement this agreement [in ac-

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built on NAFTA Article 1114, stating that environmental and social standards as contained in national laws and regulations should not be lowered in order to attract an investment. The main debate here has been whether or not this should be a binding provision. NAFTA 1114 only says that such lowering of standards is "inappropriate." The third anchor was investor performance on environmental protection.⁸⁵

In addition, the United States proposed adding a general environmental exception, essentially identical to NAFTA Article 1114(1).⁸⁶

Finally, the Negotiating Text proposed to recognize the right of each country to establish its own levels of domestic environmental protection and environmental development policies and priorities, and to adopt or modify accordingly its environmental laws and regulations.⁸⁷ The Text proposes to implement this understanding through an interpretive note to the expropriation provision clarifying that the provision does not require compensation for investment losses due to "regulation ... and other normal [governmental] activity in the public interest."⁸⁸

cordance with international environmental law and] in a manner consistent with sustainable development, as reflected in the Rio Declaration on Environment and Development and Agenda 21, [including the protection and preservation of the environment and principles of the polluter pays and the precautionary approach].

MAI Negotiating Text, *supra* note 66, at 7-8 (brackets in original).

85. Huner, *supra* note 59.

86. See *MAI Negotiating Text*, *supra* note 66, at 123. The exception proposed by the United States would have provided: "Nothing in this Agreement shall be construed to prevent a Party from adopting, maintaining or enforcing any measure otherwise consistent with its Agreement that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns." *Id.* In testimony before Congress, Alan Larson, Assistant U.S. Secretary of Economic, Business and Agricultural Affairs, stated that a primary US objective in the MAI is "to ensure that the MAI contributes to the achievement of our goal of fostering stronger global efforts to protect the environment ... and to achieve sustainable development." Larson Testimony, *supra* note 15.

87. *MAI Negotiating Text*, *supra* note 66, at 123.

88. *Id.* at 141. The Assistant U.S. Secretary of State for Economic and Business Affairs noted that these provisions would implement the understanding that "[n]ormal regulatory actions, even when they affect the value of an investment, should not be

IV. CHALLENGES TO ENVIRONMENTAL LAWS AND REGULATIONS UNDER NAFTA

As noted above,⁸⁹ international arbitration proceedings are extremely confidential. In addition to excluding those who may be directly affected by the results of the arbitration, this secrecy makes it very difficult to obtain complete and accurate factual information regarding NAFTA expropriation claims. The cases described in this section are based on information that is publicly available. With one exception (the Ethyl case), none of the parties to the arbitration has made its submissions public. It is therefore possible that these descriptions omit certain relevant factual information or legal claims. Nevertheless, the case descriptions clearly demonstrate the conflict between the NAFTA expropriation provisions and government efforts to protect the environment.⁹⁰

considered as an expropriation requiring compensation." *Quoted in Alan Larson, Environmental, Regulatory Safeguards*, 15 ENVTL. FORUM 46, 51 (1998).

89. See *supra* note 38 and accompanying text.

90. To date, there have been eight claims brought under NAFTA's investment provisions. The cases described in the text are those that raise the issues discussed in this article most clearly and with respect to which the clearest factual information is available. A summary of the other claims follows.

Pope & Talbot v. Canada: Pope & Talbot, Inc., a Delaware-based wood-products company, obtains approximately 75% of its wood from British Columbia. See Pope & Talbot SEC Filing, Form 10-K, *Wood Products Business*, Mar. 31, 1998; see also Pope & Talbot SEC Filing, Form 10-Q, Nov. 13, 1998. The most lucrative portion of the wood products business is lumber production which accounted for \$219,698,000.00 in sales for the company in 1997. See *id.* In 1996, pursuant to the Canada/US Softwood Lumber Agreement, the two nations agreed to establish volume quotas for each company shipping Canadian softwood lumber to the United States. See Pope & Talbot SEC Filing, Form 10-K, *Wood Products Business*, Mar. 31, 1998. In the second year of this regime, Pope & Talbot's quota was decreased from what it had been the previous year. See *id.* Claiming that this reduction was unfair, the company filed a notice of intent to initiate arbitration under NAFTA's chapter 11 on February 17, 1999. Pope & Talbot Press Release, *Pope & Talbot Issues Challenge to Unfair Softwood Quota* (Feb. 17, 1999) <<http://www.poptal.com/news.htm>> (on file with author). If negotiations between Pope & Talbot and Canada do not resolve the dispute, the company may initiate arbitration in May 1999.

DESONA v. Mexico: Desechos Solidos de Naucalpan (DESONA), a US waste management company, claims that the council of the Mexican county of Naucalpan nullified a 15-year waste management concession between the two parties. On December 9, 1996, DESONA notified the government of Mexico of its intent to file a claim through the ICSID Additional Facility Rules and in March 1997 it filed a notice of claim with the ICSID. ICSID has accepted and registered the claim, and the first session of the arbitral tribunal was to be held September 26, 1997. No further information concern-

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A. THE METALCLAD CASE

In 1995, the Mexican federal government authorized Quimica Omega de Mexico, a subsidiary of the US-based Metalclad Corporation, to take over and operate a toxic waste facility in the Mexican state of San Luis Potosi.⁹¹ The facility had a history of contaminating local groundwater. Metalclad reportedly spent \$22 million preparing the facility.⁹²

From before the outset of this project, Metalclad was aware that its "proposed business in Mexico is highly regulated and is subject to Mexican Environmental law."⁹³ This law regulates both the construction and operation of hazardous waste facili-

ing this claim is available. *USTR Update on WTO, NAFTA Dispute Settlement Cases* (visited on May 3, 1999) <<http://www.usia.gov/topical/econ/wto/wtxt0919.htm>> (on file with author). See also West, *AMERICAN LAWYER*, Dec. 1997, available in LEXIS, News Library, Magazine File.

Sun Belt Water Inc. v. Canada: In 1990, six companies, including Snowcap Water, held licenses issued by the government of British Columbia (BC) for the bulk export of what was considered "surplus" water. Public opposition to these exports on conservation grounds led to a temporary moratorium on water exports and, eventually, the BC Water Protection Act, R.S.B.C. Chapt. 484 (1996) (Can.), banned such exports permanently. In 1996, the BC government settled with Snowcap for \$335,000, the amount it had spent creating an infrastructure to export water. In December 1998, Sun Belt, a US corporation that was a partner in a joint venture with Snowcap, brought a claim under NAFTA's Chapter 11 for as much as US\$219 million for lost business opportunities resulting from the ban. Sun Belt's claims are based on violations of the national treatment and minimum standard of treatment provisions. *Sun Belt Filing*, AMERICASTRADE, Dec. 24, 1998, at 13.

Loewen Group v. United States: The Loewen Group, a Canadian funeral services firm, brought a NAFTA investment claim against the United States after it lost a civil contract suit brought by a competing US funeral services company in Mississippi court. The court awarded the US company \$500 million and Loewen, which had filed for bankruptcy, was unable to pay the requisite 125% bond to appeal the case. Loewen brought the NAFTA claim on the basis that the suit against it violated NAFTA's national treatment, minimum treatment and expropriation provisions. AMERICASTRADE, Nov. 26, 1998, at 20.

USA Waste v. Mexico: A US waste management company, USA Waste, brought a NAFTA Chapter 11 claim at the ISCID against Mexico based on the city of Acapulco's failure to pay for street sweeping services provided by USA Waste under a 15-year concession agreement signed in 1995. AMERICASTRADE, June 11, 1998, at 3-4.

91. According to Metalclad, it was "invited" to operate the facility. See *Metalclad Announces It Has Suspended Construction in Mexico*, Metalclad Corp. Press Release, Sept. 30, 1998. See also Carmelo Lodise, *San Miguel's Draining Struggle*, BUSINESS MEXICO, Dec. 1994, available in LEXIS, News Library, Magazine File.

92. See Joel Millman, *Metalclad Suit Is First Against Mexico Under NAFTA Foreign-Investment Rules*, THE WALL STREET JOURNAL, October 14, 1997, at A2.

93. Metalclad SEC Filing, Form 10-KT (Apr. 1, 1997), Item 1(a).

ties, and requires environmental impact studies and permits from the National Institute of Ecology (INE), as well as local and state agencies.⁹⁴ Operation of such facilities and compliance with INE regulations is subject to continual monitoring by the Federal Attorney for the Protection of the Environment.⁹⁵

Environmentalists and local citizens were not satisfied with the environmental impact assessment for the facility, and successfully pressed the local government not to permit its operation.⁹⁶ In late 1996, the Governor of San Luis Potosi deemed the facility to be an environmental hazard to surrounding communities and ordered the Metalclad waste facility shut down.⁹⁷ The Governor's decision was supported by a geological audit performed by environmental impact analysts at the University of San Luis Potosí, who found that the facility was located on an underground alluvial stream and could therefore contaminate the local water supply.⁹⁸ The Governor subsequently declared the site part of a 600,000 acre ecological zone.⁹⁹

On January 2, 1997, Metalclad filed a claim with the ICSID against the Mexican government under the NAFTA investment chapter.¹⁰⁰ The complaint alleges, among other things, that "having been denied the right to operate its constructed and permitted facility, its property has therefore been, as a practical matter, expropriated, entitling the Company to the fair

94. *See id.*

95. *See id.*

96. *See Trying to Give the NACEC Teeth, in LATIN AMERICAN REGIONAL REPORTS: MEXICO AND NAFTA REPORTS 4* (May 9, 1996).

97. Antonia Juhasz, *Update on Metalclad Corporation v. Mexico*, in *GLOBALIZATION AND THE MAI* (Feb. 2, 1998.)

98. *See* Preamble Center for Public Policy, *Update on Metalclad Corporation v. Mexico* (visited on Jan. 28, 1999) <<http://www.islandnet.com/~ncfs/maisite/effect13.htm>> (on file with author).

99. *See id.* *See also* Guadalcázar, *zona ecológica en SLP; descartado, reabrir el confinamiento*, NOTICIERO PECUARIO, 17 Sept. 1997 (visited Feb. 3, 1999) <<http://www.veterin.unam.mx/fmvzunam/17sep97.htm>> (on file with author).

100. *See Metalclad, SEC filing*, Nov. 20, 1998, <<http://www.sec.gov/Archives/edgar/data/13547/0000013547-98-000023.txt>> (on file with author). *See also* Juhasz, *supra* note 97.

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market value of the facility as damages."¹⁰¹ Metalclad asserted that the facility was worth \$90 million.¹⁰²

In July 1997, a three member arbitration tribunal met to address the claim.¹⁰³ On October 13, 1997, Metalclad filed a memorial that included the claim and all the evidence supporting the claim, including expert witness studies. On February 17, 1998, the Mexican government filed a response, to which Metalclad replied on August 21.¹⁰⁴ Mexico responded with a number of procedural objections concerning allegations and evidence that Metalclad should be permitted to submit.¹⁰⁵ On November 13, 1998, the tribunal rejected Mexico's complaints and ordered Mexico to respond on the merits of the case by March 19, 1999.¹⁰⁶

B. THE ETHYL CORPORATION CASE

In April 1997, Canada enacted a law making it a crime to import, or trade between provinces, manganese-based sub-

101. *Metalclad SEC filing*, Apr. 1, 1997; *Metalclad SEC filing*, Nov. 20, 1998, <<http://www.sec.gov/Archives/edgar/data/13547/0000013547-98-000023.txt>> (on file with author) (characterizing its claim as "one likened to expropriation. 'The Company's position is since it is not being allowed to operate a legally authorized project, it has in essence been taken by the Mexican government.'). Metalclad also argued that Mexico violated the national treatment and most-favored-nation treatment requirements and had imposed illegal performance requirements. See Juhasz, *supra* note 97. The national treatment violation is apparently based on the assertion that the refusal to permit Metalclad's facility to operate is intended to protect a Mexican waste disposal company called Rimsa. See Fernando Cesarman, *Buen Periodismo, El Destino de la Basura*, EXCELSIOR: Editorial, 18 Aug. 1997 (visited on Feb. 24, 1999) <<http://excelsior.com.mx/9708/970818/art07.html>>.

102. See *Metalclad SEC filing*, form 10-Q, Nov. 20, 1998, <<http://www.sec.gov/Archives/edgar/data/13547/0000013547-98-000023.txt>> (on file with author); Juhasz, *supra* note 97.

103. Under the arbitration rules, each party has the right to select one panel member; the third is chosen jointly. Metalclad appointed former US Attorney General Benjamin R. Civiletti. See Jim Bryan, *TechStocks.com discussion group, Metalclad Corp. (MTLC)* (June 9, 1997) <<http://www4.techstocks.com/~wsapi/investor/Subject-15440>> (on file with author). The third arbitrator is from Great Britain. See *Metalclad SEC Filing*, Form 10-Q, Nov. 20, 1998.

104. See *Metalclad SEC Filing*, Nov. 20, 1998, <<http://www.sec.gov/Archives/edgar/data/13547/0000013547-98-000023.txt>> (on file with author).

105. See *id.*

106. *Id.* Metalclad "expects to request an oral hearing to be held as soon as possible after Mexico's final filing, following which a decision is expected to be rendered by the Tribunal." *Id.*

stances, including methylcyclopentadienyl manganese tricarbonyl (MMT), a fuel additive designed to prevent automobile engine knocking.¹⁰⁷ Automobile manufacturers had asserted that MMT harms automobile on-board diagnostic systems, which in turn could lead to a failure to detect high levels of pollutant emissions.¹⁰⁸ According to Canada's Environmental Health Directorate, excess exposure to manganese compounds can cause adverse neurological effects, leading to symptoms similar to mild Parkinson's disease.¹⁰⁹

On April 14, 1997, five days after the ban passed the Parliament and eleven days before it received Royal Assent, Ethyl Corporation, a U.S. corporation with a wholly-owned Canadian subsidiary that is the sole Canadian importer, processor and distributor of MMT, filed notice of arbitration pursuant to NAFTA's investment chapter.¹¹⁰ Among other allegations, the notice claimed that the Canadian law constituted an expropriation of Ethyl's business in Canada, subject to the compensation

107. See Manganese-Based Fuel Additives Act (MBFAA), Ch. 11, 1997 S.C. (Can.). I am indebted to David A. Wirth, Professor of Law at Boston College Law School, for his work in uncovering and untangling many of the facts of this claim.

MBFAA gave the Minister of the Environment limited authority to waive the prohibition for uses other than as gasoline additives. *Id.* § 5. According to Ethyl, use as a gasoline additive is "a principal use of MMT," although "MMT is also used by Ethyl Corporation in other fuel products." Ethyl Corp. v. Government of Canada, Notice of Arbitration Under Arbitration Rules of the United Nations Commission on International Trade Law and the North American Free Trade Agreement 6 (Apr. 14, 1997) [hereinafter Notice of Arbitration] (on file with author).

108. For a summary of the scientific evidence concerning these possible effects and a discussion of the treatment of MMT by the US EPA, see Jesus Juanos I Timoneda, *The Legal Dynamics of the Regulation of MMT: Air Quality Standards and the Salt Lake City Airshed*, 17 J. LAND RESOURCES & ENVTL L. 283 (1997), in which the author concludes that there are "numerous, diverse, sometimes conflicting, reasons to support" all positions concerning the use of the additive, but that one variable, "the incidence of MMT's combustion products on the amount of particulate matter in a given airshed," "deserves considerable regulatory attention ... because of its proven harmful effects on health and welfare." *Id.* at 307, 312.

109. See ENVIRONMENTAL HEALTH DIRECTORATE, HEALTH CANADA, RISK ASSESSMENT FOR THE COMBUSTION PRODUCTS OF METHYLCYCLOPENTADIENYL MANGANESE TRICARBONYL (MMT) IN GASOLINE (Dec. 6, 1994). At least some studies suggested a health risk due to breathing exhaust from cars running on gasoline containing MMT. A University of Quebec neurophysiologist stated in April 1996 that tests on laboratory animals suggested that exposure to manganese could speed up the aging process, and that young children "may be particularly at risk" because of the potential for the deterioration of brain tissues. SOUTHAM NEWS, Apr. 20, 1996 (visited on June 11, 1998) reprinted in <<http://www.achilles.net/~jamesh/mmt.htm>>

110. Notice of Arbitration, *supra* note 107.

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requirement of NAFTA's article 1110.¹¹¹ Ethyl sought US \$250 million in compensation for the expropriation of its investment in Canada. This amount included loss of sales and profits in Canada,¹¹² loss of value of Ethyl Canada,¹¹³ loss of "world-wide sales due to other countries relying on" the measures taken by Canada, "the cost of reducing operations in Canada," expenses incurred in "defending itself against allegations made by Canada" and lobbying to defeat the law,¹¹⁴ and its "goodwill both inside and outside Canada."¹¹⁵

Ethyl cited international law in support of its expropriation claim. In particular, Ethyl stated that bilateral investment treaties, "which are substantially similar to the NAFTA's investment protection provisions" have been interpreted as requiring compensation for "indirect expropriation": "Where the effect is similar to what might have occurred under an outright expropriation, the investor would in all likelihood be covered under most BIT provisions."¹¹⁶ According to Ethyl,

An expropriation therefore exists whenever there is a substantial and unreasonable interference with the enjoyment of a property right Article 1110 of the NAFTA does not prevent governmental regulatory actions. It requires governments to compensate investors

111. See *id.* at 3, 10-18. The notice also alleged violations of the national treatment obligations of NAFTA's article 1102, through discriminatory treatment of a US investor. Ethyl noted that the Minister of the Environment had stated that nothing would keep Ethyl from building a MMT production plant in Canada and that "[t]here is no reasonable or plausible explanation why domestically produced MMT is permitted for sale in Canada while imported MMT is not." Ethyl also argued that the ban imposed a performance requirement—in the form of an effective requirement that MMT sold in Canada "have 100% Canadian content"—in violation of NAFTA article 1106. *Id.* at 13.

112. Ethyl noted that "the sale of MMT represents some 50% of Ethyl Canada's total sales revenue." *Id.* at 11.

113. Ethyl threatened that the 50% loss of sales revenue "could cause the parent company to re-evaluate maintaining a Canadian operation." *Id.* at 12.

114. *Id.* at 18.

115. Notice of Arbitration, *supra* note 107, at 6, 15-18. In its Notice of Arbitration, Ethyl claimed that "the Government's statements [concerning the additive] created public distrust" and "animosity" towards MMT. *Id.* at 6, 15.

116. Notice of Arbitration, *supra* note 107, at 10 (quoting DOLZER & STEVENS, *supra* note 14, at 100).

for interference with their property rights as set out in the NAFTA.¹¹⁷

Ethyl argued that the Canadian measure was a discriminatory attempt to protect domestic industry, rather than a legitimate restriction for environmental or health reasons. Ethyl asserted that the Canadian Ministry of Health “has concluded that MMT does not pose a threat to human health and no independent studies have concluded that MMT harms automobile diagnostic systems.”¹¹⁸ According to Ethyl, if the ban had been a health or environmental measure, Canada would have enacted it pursuant to the authority of the Canadian Environmental Protection Act (CEPA), which provides authority for the regulation of the production and manufacture of toxic substances.¹¹⁹ Ethyl claimed that there had not been sufficient scientific support for the government of Canada to prohibit MMT under CEPA or Canadian health laws.¹²⁰ Ethyl supported its discrimination claim by noting that MMT was only one of a number of fuel additives that Canada could have regulated; that Ethyl, a foreign corporation, was the sole manufacturer of MMT; and that the law “will not ban MMT completely, but will make foreign-made MMT inaccessible to consumers in Canada.”¹²¹ For its part, the Government of Canada

117. *Id.* at 11. Ethyl also noted that Canada’s Minister of International Trade had pointed out, in a letter to the Minister of the Environment, “that Canada’s proposed legislation could constitute a measure tantamount to expropriation ... [and] could be inconsistent with Canada’s NAFTA ... investment obligations.” *Id.* at 12 (citing Letter of the Hon. A. Eggleton to the Hon. S. Marchi (February 23, 1996)).

118. *Id.* at 4. See also ENVIRONMENTAL HEALTH DIRECTORATE, *supra* note 109, at 69 (concluding on the basis of exposure assessment that “all analyses indicate that the combustion products of MMT in gasoline do not represent an added health risk to the Canadian population”).

119. Canadian Environmental Protection Act, R.S.C., Ch. 16, §§ 12, 14 (4th Supp. 1985) (Can.) [hereinafter CEPA].

120. Notice of Arbitration, *supra* note 107, at 5, 14-15. CEPA allows the government to regulate toxic substances, including “the total, partial or conditional prohibition of the manufacture, use, processing, sale, offering for sale, import or export of the substance or a product containing the substance.” CEPA §34(1)(i). The Act defines a substance as toxic if it may have a harmful effect on the environment or constitute a danger to human life. *Id.* § 11. The Act provides that, in assessing toxicity, the Minister of Health or of the Environment “may” collect data concerning the nature and effects of the substance. *Id.* §15.

121. Notice of Arbitration, *supra* note 107, at 4. In fact, there were reports that some Canadian gasoline refineries had continued to use MMT that they had stockpiled before the ban took effect. John Urquhart, *Canada Lifts Ban on Ethyl’s Additive; U.S.*

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claimed that it had restricted trade in MMT, as opposed to its production, sale or use, because the Canadian constitution, which shares environmental authority between federal and provincial governments, places production and intraprovincial use of a product beyond the legislative authority of the Canadian parliament.¹²²

With respect to the alleged lack of scientific support for the Canadian law, Ethyl characterized the law as a “performance requirement,”¹²³ with respect to which measures to protect life or health or to conserve exhaustible natural resources are permitted only if they are “necessary.”¹²⁴ Ethyl stated that “[t]he lack of any clear scientific evidence throws into doubt whether [the Canadian MMT measure] is necessary to protect human life or health.”¹²⁵

Ethyl also cited jurisprudence interpreting GATT’s Article XX(b), which permits restrictions on trade where they are “necessary to protect human, animal or plant life or health.”¹²⁶ Ethyl noted that GATT panels have interpreted “necessary” to mean that the measure in question must be “the least trade restrictive measure possible.”¹²⁷ Ethyl argued that an outright

Firm to Terminate Its Legal Fight, WALL STREET JOURNAL, July 21, 1998 reprinted in 1998 WL-WSJ 3502397.

122. See *Proceedings of the Standing Senate Committee on Energy, the Environment and Natural Resources, Issue 12 - Evidence* (Feb. 19, 1997) at 7, <<http://www.parl.gc.ca/english/senate/com-e/enrg-e/12ev-e.htm>> (visited Apr. 7, 1999) (testimony of Mr. Jacques Fremont, Faculty of Law, University of Montreal) (“[U]nder the Canadian Constitution, the provinces have full jurisdiction in relation to the production and the manufacture of products of goods, including gasoline.”); *Debates of Senate (Canada), 2d Sess., 35th Parliament, Vol. 136, Issue 61 (Dec. 12, 1996)*, (visited Apr. 7, 1999) <<http://www.parl.gc.ca/english/senate/deb-e/61db-e.html>> (statement of Sen. Noel A. Kinsella) (“the manufacturing of petroleum and that of automobiles falls under provincial jurisdiction”).

123. Notice of Arbitration, *supra* note 107, at 12-13. Ethyl argued that because the Canadian law banned only import and interprovincial trade in MMT, it could manufacture and sell MMT in Canada only if it built manufacturing and blending facilities in each province. See *id.* at 13. The ban, therefore, required MMT sold in Canada to have 100% Canadian content and required Ethyl Canada to purchase all of its MMT from Canadian producers. See *id.*

124. NAFTA, *supra* note 25, art. 1106.

125. Notice of Arbitration, *supra* note 107, at 14.

126. See GATT, *supra* note 50, art. XX(b).

127. Notice of Arbitration, *supra* note 107, at 14 (citing Restrictions on Importation of and Internal Taxes on Cigarettes, GATT Doc. SD10/R, 37 B.I.S.D. 200 (1989-1990)).

ban on MMT, as opposed to a trade restriction giving domestic producers an advantage over foreign producers, would be less trade restrictive.¹²⁸ For that reason, according to Ethyl, the Canadian law could not be considered “necessary.”¹²⁹

In July 1998, after a Canadian domestic trade panel ruled in favor of several provincial governments that had brought a claim that the ban violated Canada’s Agreement on Internal Trade,¹³⁰ the government of Canada announced that it had settled Ethyl’s NAFTA challenge. The settlement provided for a payment of approximately US \$13 million, including roughly \$4.5 million for legal fees.¹³¹ In addition, the Minister of the Environment, Christine Stewart, issued a letter to Ethyl stating: “Current scientific information fails to demonstrate that MMT impairs the proper functioning of automotive on-board diagnostic systems. Furthermore, there is no new scientific evidence to modify conclusions drawn by Health Canada in 1994 that MMT poses no health risk.”¹³² In a subsequent news conference, Ms. Stewart said she remained concerned about allegations concerning MMT, but stated: “[W]e do not have sufficient scientific evidence at the moment on which to base a

128. *See id.*

129. *Id.*

130. Agreement on Internal Trade, R.S.C. Chapt. 17 (1996) (Can.). The Agreement on Internal Trade (AIT) applies principles of nondiscrimination and elimination of trade obstacles to trade among provincial and other governments. The dispute resolution panel established by the AIT agreed with the governments of Alberta, Québec, Saskatchewan and Nova Scotia that the ban on manganese-based substances was a restriction on the right of movement across provincial boundaries and an obstacle to internal trade, both of which are prohibited by the AIT. REPORT OF THE ARTICLE 1704 PANEL CONCERNING A DISPUTE BETWEEN ALBERTA AND CANADA REGARDING THE MANGANESE-BASED FUEL ADDITIVES ACT (Fil no. 97/98-15-MMT-Po58 June 12, 1998). The panel found that the manganese ban did not satisfy the AIT exception for otherwise legitimate governmental measures because the government had not demonstrated that there existed “such urgency or a risk so widespread as to warrant such comprehensive restrict[ion]s as the Act provides on internal trade.” AMERICASTRADE, July 23, 1998, at 14 (quoting decision of the AIT panel). The AIT panel considering the internal trade ramifications of the law had concluded that the automobile manufacturers’ “evidence as to the impact of MMT on the environment is, at best, inconclusive.” *Id.* at 15. The panel did note that it did not consider the law to be a “disguised restriction” on internal trade. *Id.* at 14.

131. *See* Order Amending the Schedule to the Manganese-Based Fuel Additives Act, SOR/98-393, C. Gaz. 1998.II.2265 (July 20, 1998). *See also* Government of Canada Statement on MMT (July 20, 1998).

132. Quoted in Shawn McCarthy, *Failed Ban Becomes Selling Point for MMT*, THE GLOBE AND MAIL, July 21, 1998 at A3.

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clear case that MMT in gasoline is causing severe problems to either the environment or the health of Canadians.”¹³³ With respect to the effect on automobile emissions systems, Ms. Stewart stated that, in introducing the ban in 1995, the government had relied on evidence from the auto industry that had seemed “quite persuasive,” but that the industry evidence now appeared insufficient.¹³⁴ She also stated that the Canadian government had not banned MMT directly because there was no proof that it was toxic at low levels of exposure.¹³⁵

C. THE SD MYERS CASE

On July 22, 1998, shortly after Canada settled the Ethyl claim, SD Myers, Inc., a U.S. corporation with a facility to dispose of PCB wastes in Ohio, filed a claim against Canada for “not less than” \$10 million, plus fees, costs and interest,¹³⁶ for losses arising out of a 15 month Canadian ban on the export of PCBs, which the company claimed to have been “tantamount to expropriation” of its contracts to treat Canadian PCBs.¹³⁷

133. *Id.* Both the automobile industry and some environmental groups continue to express concern regarding the effects of MMT. The president of the Canadian Motor Vehicle Manufacturers Association stated that the automobile industry had submitted over 40 papers demonstrating MMT’s effect on emission controls. *See id.* In addition, preliminary studies by a neurotoxicologist at the University of Quebec apparently suggest that “even low levels of manganese in the blood can have health effects, particularly in children and the elderly.” Shawn McCarthy, *Threat of NAFTA Case Kills Canada’s MMT Ban*, THE GLOBE AND MAIL, July 20, 1998 (visited on July 21, 1998) reprinted in <<http://www.theglobeandmail.com...9980720/GlobeFront/ummtn.html>>. The author of the study stated: “We know that in large concentrations, airborne manganese does pose a risk to human health. What we don’t know is at what level does it not pose a risk. There remain a lot of questions about manganese and we should know a lot more about it before we use it.” *Id.*

134. Urquhart, *supra* note 121.

135. THE GLOBE AND MAIL, July 21, 1998, *supra* note 132. *See also* THE GLOBE AND MAIL, July 20, 1998, *supra* note 133 (“Former environment ministers Sheila Copps and Sergio Marchi both argued that they couldn’t ban MMT directly because Health Canada had found there was not sufficient evidence that it was toxic at low levels. So they resorted to the trade ban.”).

136. Reports have placed SD Myers’s estimate of its losses as high as \$30 million. *See* Ian Jack, *Feds Face Lawsuit over PCBs: 1995 Ban under Nafta*, FINANCIAL POST, Oct. 30, 1998 at C8; *U.S. Company Seeks Compensation for Losses Due to Canadian PCB Export Ban*, 21 INT’L ENV’T REP. No. 18 at 848 (company claims losses of \$15 million). S.D. Myers’s claim for fees and costs apparently included expenses incurred in the company’s opposition to the Canadian ban.

137. 21 INT’L ENV’T REP. No. 18, *supra* note 135, at 848.

Since 1977, U.S. law has prohibited the manufacture, processing and distribution in commerce of PCBs.¹³⁸ Pursuant to this law, EPA banned the import and export of PCBs in 1980.¹³⁹ Although the law allowed EPA to grant individual one-year exemptions from this prohibition in certain circumstances,¹⁴⁰ it rarely did so.¹⁴¹ Canada first banned the export of PCB wastes in 1990, although at that time it permitted the return of U.S. government-owned PCB wastes to the United States for disposal.¹⁴² In 1992, Canada ratified the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal,¹⁴³ which prohibits countries from exporting hazardous wastes, including PCBs, to nonparties like the United States without ensuring that they will be managed in an environmentally sound manner.¹⁴⁴ Canada implemented these obligations in the Export and Import of Hazardous Waste Regulations.¹⁴⁵ In December 1994, the United States proposed

138. Toxic Substances Control Act, 15 U.S.C. § 2605(e)(3)(A).

139. EPA Final Rule, Disposal of Polychlorinated Biphenyls; Import for Disposal, 61 Fed. Reg. 11096 (Mar. 18, 1996). According to EPA, it had closed the border to PCB transports "primarily because of both limited disposal capacity in the United States and no appropriate disposal capacity in Canada." *Id.* at 11101.

140. 15 U.S.C. §2605(e)(3)(B). The Administrator may only grant such an exemption if there will be no "unreasonable risk of injury to health or environment" and "good faith efforts have been made to develop a chemical substance which does not present an unreasonable risk of injury to health and the environment and which may be substituted for such [PCB]." 15 U.S.C. §2605(e)(3)(B)(i)(ii).

141. EPA Final Rule, Disposal of Polychlorinated Biphenyls; Import for Disposal, 61 Fed. Reg. 11096 (Mar. 18, 1996).

142. *Environmental concerns must be addressed before Canada permits PCB waste exports*, ES&E, May 1996, <<http://www.esemag.com/0596/pcb.html>> (on file with author) (hereinafter "ES&E").

143. Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal, Mar. 22, 1989, UN Doc. UNEP/IG.80/3, 28 I.L.M. 657 (1989) (entered into force May 5, 1992) (hereinafter "Basel Convention").

144. The Basel Convention requires Parties to prohibit the export of hazardous wastes, including PCBs, if they have "reason to believe that the wastes in question will not be managed in an environmentally sound manner." *Id.* art. 4.2(e) (prohibition), Annex 1 (listing PCBs). In addition, Parties may not export PCBs to non-Parties, *id.* art. 4.5, unless they enter into an arrangement or agreement that does not "derogate from the environmentally sound management of hazardous wastes" as required by the Convention. *Id.* art. 11.1. The United States has signed, but not ratified, the Basel Convention.

145. Export and Import of Hazardous Waste Regulations, SOR/92-637, P.C. 1992-2284, Nov. 12, 1992. The regulations prohibit the export of hazardous wastes to countries that are not party to the Basel Convention or the Canada-U.S.A. Agreement on the Transboundary Movement of Hazardous Waste. *Id.* art. 6(c).

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to amend its PCB regulations to allow limited transboundary trade in PCB wastes beginning in mid-1996.¹⁴⁶

In October 1995, the United States granted SD Myers "enforcement discretion" to begin importing Canadian PCBs the following month.¹⁴⁷ The following month, Canada temporarily banned the export of PCBs to the United States because Canada was "uncertain about the final contents of the U.S. regulatory amendments governing PCB waste imports" and "lacked assurance that Canadian PCB wastes, if exported to the U.S., would be managed in an environmentally sound manner."¹⁴⁸ The ban was implemented pursuant to authority under the Canadian Environmental Protection Act to issue "interim orders," which

can be made if a substance deemed toxic under CEPA, in this case PCBs, is not adequately regulated, and immediate action is required to deal with a significant danger to the environment or to human life or health.¹⁴⁹

146. See EPA Final Rule, Disposal of Polychlorinated Biphenyls; Import for Disposal, 61 Fed. Reg. 11096 (Mar. 18, 1996). In particular, instead of requiring persons wishing to import PCBs for disposal to apply for a case-by-case exemption, importers would only have been required to provide EPA notice of the importation of PCBs 45 days prior to the intended importation date. *Id.* at 11097, 11107.

147. ES&E, *supra* note 142.

148. *Id.* Canada's PCB Waste Export Regulations, 1996, explain the concern regarding PCBs:

Polychlorinated biphenyls (PCBs) are very stable substances; they are resistant to chemical and physical degradation. They are also persistent and bioaccumulate in living organisms and are capable of penetrating the food chain. Consequently, PCBs have been listed in Schedule I of the Canadian Environmental Protection Act (CEPA) as toxic. Furthermore, once released into the atmosphere, PCBs can travel extremely long distances. As a result, they are regularly found in the Great Lakes Region and also in remote areas such as the Arctic.

Canadian Dept. of Env't, PCB Waste Export Regulations, 1996, *Regulatory Impact Analysis Statement*, <<http://www.hazmatmag.com/library/PCBRegs96/PCBRegs96e.html>> (on file with author) (hereinafter "Waste Export Regs. Impact Statement").

149. CEPA, *supra* note 119, Chapt. 16, § 15.3 (1985), Interim Orders 35. Once an Interim Order is made, it can only remain in effect if the minister issuing the order "offer[s] to consult with the governments of all affected provinces within twenty-four hours after making the Order to determine whether they are prepared to deal with the significant danger" and "consult[s] with other Ministers of the Crown to determine whether any action can be taken under any other Act of Parliament to deal with the significant danger." *Id.* The Interim Order banning PCB waste exports to the United

In February 1996, the Canadian Ministers of the Environment and Health announced that the ban would remain in place until Canada was assured that PCB wastes exported to the United States would be treated appropriately.¹⁵⁰ Canada's concern regarding PCB treatment was explained in subsequent legislation lifting the ban:

Landfilling does not destroy PCBs, consequently, the potential for future environmental contamination continues. In addition, landfilling requires maintenance and monitoring in perpetuity. If Canadian PCB wastes are allowed to be landfilled in the United States, they could escape into the environment and, because of their capacity to volatilize and to be transported over long distances, they could affect the health of Canadians and Canadian's [*sic*] environment as well as that of other countries. Furthermore, as a party to the Basel Convention, Canada is required to ensure that any exports of hazardous wastes, including PCB wastes, be disposed of in an environmentally sound manner. Since guidelines adopted by Parties of the Basel Convention do not consider landfilling of PCB wastes to be environmentally sound, Canada has an obligation to ensure that Canadian PCB wastes are not exported for landfilling in the United States.¹⁵¹

In March 1996, the United States issued new regulations governing the import of PCB wastes.¹⁵² After reviewing the regulations, Canada rescinded its ban, allowing exports of PCB wastes "for treatment and destruction but not for landfilling," beginning in February 1997.¹⁵³ The Canadian Ministry of the Environment explained that the new regulations would allow PCB waste exports to the United States

States was entitled *Regulations Amending the PCB Waste Export Regulations (Interim Order)*. See *PCB Waste Export Regulations, 1996, Description*, <<http://www.hazmatmag.com/library/PCBRegs96/PCBRegs96e.html>> (on file with author).

150. ES&E, *supra* note 142.

151. Waste Export Regs. Impact Statement, *supra* note 148.

152. EPA Final Rule, Disposal of Polychlorinated Biphenyls; Import for Disposal, 61 Fed. Reg. 11096 (Mar. 18, 1996).

153. Waste Export Regs. Impact Statement, *supra* note 148.

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only if the Department of the Environment has the guarantee that: these wastes will be treated and destroyed in an efficient and environmentally sound manner; and, the U.S. EPA has been informed and has accepted that these PCB wastes enter that country. Therefore, as mentioned in the news release by both Ministers, the Regulations will allow exports of Canadian PCB wastes and these wastes will be allowed only for treatment and destruction and thus ensuring that any export of Canadian PCB wastes will be managed in an environmentally sound manner.¹⁵⁴

In addition to the direct effect of ensuring safe disposal of PCB wastes, Canada noted that lifting the export ban had significant other environmental and economic benefits. These included decreased risk of exposure to PCB wastes due to shorter transport distances for wastes located near disposal facilities in the United States; lowered cost of PCB waste disposal due to increased competitiveness among a larger number of available disposal facilities and shorter transportation distances; and increased destruction of PCBs due to the lowered cost, resulting in less likelihood of exposure and less storage and cleanup expenses.¹⁵⁵ In July 1997, a U.S. Court of Appeals overturned EPA's new import regulations, ruling that EPA was bound by U.S. law to consider individual exemption applications on a case-by-case basis.¹⁵⁶

SD Myers's NAFTA claim is apparently based on contracts that it had with a group of Canadian companies to dispose of their PCB wastes.¹⁵⁷ The company alleged that the ban gave "a monopoly on PCB treatment to an Alberta company."¹⁵⁸

154. *Id.*

155. *Id.*

156. *Sierra Club v. EPA*, 118 F.3d 1324 (9th Cir. 1997).

157. *See InterPress Service*, Sept. 23, 1998, at 4.

158. *Greenwire*, Aug. 24, 1998, at 2 (citing *JOURNAL OF COMMERCE*, 8/24). According to SD Myers's attorney, the Canadian ban "hurt S.D. Myers Inc. simply because it was an American company." *InterPress Service*, Sept. 23, 1998, at 4.

V. INDIRECT EXPROPRIATION UNDER DOMESTIC AND INTERNATIONAL LAW

The question at the heart of this Article is one of international law — specifically, whether international law protects the right of governments to implement environmental measures that affect property interests without becoming obligated to compensate for those effects. Despite the international nature of the question, the Article will first briefly describe U.S., Canadian and Mexican law regarding regulatory takings. It will do so for a number of reasons.

First, whereas relatively few international tribunals have considered whether regulations affecting the value of property give rise to an obligation to compensate, U.S. courts have considered the question in some detail. Canadian courts have also addressed the issue, although less frequently. U.S. law is also likely to have a strong influence on the development of international law in this area, because, as one of the leading capital-exporting states, it “will contend for the transference of the system of property protection in [its] domestic sphere onto the international sphere.”¹⁵⁹ Canada and Mexico have similar motivation, although widely differing ability, to make international law reflect their systems. In addition, domestic laws help to define “general principles of law,” which are one of the sources of international law.¹⁶⁰

Conversely, international law concerning regulatory expropriation could have a strong effect on the ability of the United States to regulate to protect the environment or other important societal concerns. In the famous words of the U.S. Supreme Court, “[i]nternational law is part of our law.”¹⁶¹ More importantly, however, as a party to numerous agreements

159. M. SORNARAJAH, *THE INTERNATIONAL LAW ON FOREIGN INVESTMENT* 294 (1994). Sornarajah notes that “[t]here is evidence of such a transference in the past” and that “[t]he pervasive influence of the American jurisprudence on the taking of property is evident in modern discussions on taking in international law.” *Id.* The United States intends that the expropriation standards in the MAI will be “consistent with U.S. legal principles and practice.” Larson Testimony, *supra* note 15.

160. *See infra* note 241.

161. *The Paquete Habana*, 175 U.S. 677, 700 (1900).

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regulating expropriation, including the NAFTA, and a promoter of the globalization of these rules, the U.S. government and its citizens must be aware of the degree to which international law may support or conflict with U.S. law. If, for example, international law and agreements were to require compensation for a wide variety of environmental regulations — a position already advanced by a number of companies seeking to use the NAFTA to obtain compensation for the impact of laws on their investments — the ability of the United States to protect its environment could be profoundly limited.¹⁶² The same is true for Canada, Mexico and all other countries of the world.

A. REGULATORY TAKINGS UNDER DOMESTIC LAW

The U.S., Canadian and Mexican legal systems provide varying degrees of protection to private property. Nevertheless, as the following descriptions demonstrate, they share a common understanding that the government is not obligated to compensate for the economic impact of most legitimate regulatory action.

1. *Regulatory Takings Under U.S. Law*

The Fifth Amendment to the U.S. Constitution guarantees that private property shall not “be taken for public use without just compensation.”¹⁶³ Until 1922, the Supreme Court had considered that the Constitutional requirement of compensation applied only to direct takings — those in which the government took full title to private property.¹⁶⁴ In *Pennsylvania Coal Co. v. Mahon*, the Court first recognized what have been called “regulatory takings,” stating that “while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking.”¹⁶⁵ The Court has been less than clear,

162. See SORNARAJAH, *supra* note 159, at 299 (“If, each time there is a [regulatory] measure against a foreign investor, he could allege a taking in international law which needs to be compensated, regulatory measures against foreign investors could become impossible.”).

163. U.S. Const. amend. V.

164. See *Lucas v. South Carolina Coastal Council*, 500 U.S. 1003, 1014 (1992).

165. 260 U.S. 393, 415 (1922). The distinction between a direct taking and a regulatory taking is still relevant: “A ‘taking’ may more readily be found when the interfer-

however, in defining what is “too far.” Rather than establishing a definitive test for when a regulation becomes a taking,¹⁶⁶ the Court has determined that the analysis depends on an “ad hoc, factual inquir[y] into the circumstances of each particular case,”¹⁶⁷ and has identified three factors that are particularly significant in undertaking this inquiry.¹⁶⁸ Although these three factors must be applied on a case-by-case basis, one scholar has noted that “it is quite difficult to establish a [regulatory] taking under [the Court’s] ad hoc approach, in part [because of] the sensitivity of the courts to the important purposes of government regulation and the reciprocal advantages of economic regulation.”¹⁶⁹

The first factor in the Supreme Court’s regulatory taking analysis is “the nature of the governmental action.”¹⁷⁰ Regulations that cause the government to “physically invade or permanently appropriate”¹⁷¹ the property in question automatically require compensation “no matter how minute the intrusion, and no matter how weighty the public purpose behind it.”¹⁷² Lesser interference, on the other hand, that “arises from a public program that adjusts the benefits and burdens of economic life economic life to promote the common good ... does not constitute a taking requiring Government compensation.”¹⁷³

ence with property can be characterized as a physical invasion by government ... than when interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good.” *Penn Central v. New York City*, 438 U.S. 104, 124 (1978).

166. See *Lucas*, 505 U.S. at 1015 (Court has “generally eschewed any set formula for determining how far is too far, preferring to engage in essentially ad hoc, factual inquiries” (quotations omitted)).

167. *Concrete Pipe & Prods. of Calif. v. Construction Laborers Pension Trust*, 508 U.S. 602, 643 (1993) (quotation omitted).

168. *Id.*

169. Mark W. Cordes, *Leapfrogging the Constitution: The Rise of State Takings Legislation*, 24 *ECOLOGICAL L.Q.* 187, 203 (1997).

170. *Concrete Pipe*, 508 U.S. at 643.

171. *Id.*; *Connolly v. Trustees of the Operating Engineers Pension Trust*, 475 U.S. 211, at 225 (1986).

172. *Lucas*, 505 U.S. at 1015.

173. *Concrete Pipe*, 508 U.S. at 643. See also *Lucas*, 505 U.S. at 1022 (“[G]overnment may, consistent with the Takings Clause, affect property values by regulation without incurring an obligation to compensate—a reality we nowadays acknowledge explicitly with respect to the full scope of the State’s police power”); *Connolly*, 475 U.S. at 225; *Penn Central*, 438 U.S. at 125 (where the State “reasonably conclude[s] that ‘the

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As the Court has explained, “such restrictions are the burdens we must all bear in exchange for the advantage of living and doing business in a civilized community.”¹⁷⁴

Regulations also must “substantially advance legitimate state interests.”¹⁷⁵ The Supreme Court has recognized as legitimate, and thus not requiring compensation, regulations addressing a host of environmental or human health problems.¹⁷⁶ These have included regulations prohibiting smoke emissions;¹⁷⁷ requiring the construction of roadside flood-control devices;¹⁷⁸ limiting the size of buildings to “avoid unnecessary conversion of open space land to strictly urban areas, thereby protecting against the resultant adverse impacts such as air, noise, and water pollution, ... disturbance of the ecology and the environment, ... and other demonstrated consequences of urban sprawl”;¹⁷⁹ prohibiting the sale of items made from endangered species;¹⁸⁰ regulating the sale and use of pesticides;¹⁸¹ banning the import of baitfish from other states to protect native fish from exogenous parasites;¹⁸² requiring the destruction of diseased trees to protect local orchards;¹⁸³ banning brickyard operations in a residential area because of their adverse impacts on human health;¹⁸⁴ restricting coal mining activities to

health, safety, morals, or general welfare’ would be promoted by prohibiting particular contemplated uses of land,” compensation need not accompany prohibition).

174. *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1007 (1984) (quotation omitted).

175. *Lucas*, 505 U.S. at 1015-17 (quoting *Agins*, 447 U.S. at 260).

176. See *Lucas*, 505 U.S. at 1022 (There exists “a long line of this Court’s cases sustaining against Due Process and Takings Clause challenges the State’s use of its ‘police powers’ to enjoin a property owner from activities akin to public nuisances” (citations omitted)).

177. See *Northwestern Laundry v. Des Moines*, 239 U.S. 486 (1916) (no valid constitutional objection in fact that regulation “may require the discontinuance of the use of property, or subject the occupant to large expense in complying with the terms of the law”).

178. See *Chicago & A.R. Co. v. Tranberger*, 238 U.S. 67 (1915).

179. *Agins*, 447 U.S. at 262 (zoning regulation limiting buildings to single-family dwellings, accessory buildings, and open-spaces uses substantially advanced the cited interests).

180. See *Andrus v. Allard*, 444 U.S. 51, 64-68 (1979) (refusing to require compensation when a ban on the sale of eagle feathers made it impossible for the claimant to sell certain items he had intended to sell).

181. See *Ruckelshaus*, 467 U.S. at 1007.

182. See *Maine v. Taylor*, 477 U.S. 131 (1986).

183. See *Miller v. Schoene*, 276 U.S. 272, 279-80 (1928) (due process challenge).

184. See *Hadacheck v. Sebastian*, 239 U.S. 394, 410-11 (1915).

protect the environment and public welfare;¹⁸⁵ regulating or banning the manufacture or sale of alcoholic beverages to protect “public health, public morals, and the public safety”;¹⁸⁶ and protecting visual access to the ocean.¹⁸⁷

The second factor that the Supreme Court has identified in considering whether a regulatory taking requires compensation is “the severity of the economic impact” of the governmental action.¹⁸⁸ The Court has stated that a regulation will usually constitute a compensable taking if it “denies *all* economically beneficial or productive use” of the property in question.¹⁸⁹ On the other hand, “mere diminution in the value of property, however serious, is insufficient to demonstrate a taking.”¹⁹⁰

185. See *Hodel v. Virginia Surface Mining and Reclamation Ass'n*, 452 U.S. 264, 295 (1981) (statute prohibiting mining near certain locations and regulating conditions under which any mining could be conducted did not constitute a taking because it did not prevent any non-mining uses of land); *Keystone Bituminous Coal Ass'n v. De Benedictis*, 480 U.S. 470, 485 (1987) (statute designed to prevent ground surface from collapsing was warranted in interest of public safety).

186. *Mugler v. Kansas*, 123 U.S. 623, 661-62 (1887). See also *Everard's Breweries v. Day*, 265 U.S. 545, 563 (1924) (law banning sale of certain beverages already existing at time of act); *Jacob Ruppert, Inc. v. Caffey*, 251 U.S. 264, 303 (1920) (same).

187. See *Nollan v. California Coastal Comm'n*, 483 U.S. 825, 828 (1987). Although the Court found the interest advanced to be legitimate, it concluded that conditioning a building permit on the grant of a public easement to provide physical access to the beach did not satisfy the “essential nexus” requirement. *Id.* at 837. The Court has used this requirement where land development permits are conditioned on granting public easements, stating that in such cases there must be an “essential nexus” and a “rough proportionality” between the interest and the conditions imposed by the regulation. See *Dolan v. City of Tigard*, 512 U.S. 374, 385 (1994). When the regulation does not require a public easement on private property, the Court has not applied the essential nexus requirement. See *Clajon Prod. Corp. v. Petera*, 70 F.3d 1566, 1578-79 (1995) (noting that “*Keystone* [480 U.S. at 490]—decided in the same year as *Nollan*—downplayed the need for any nexus requirement in considering the constitutionality of a general regulation and focused on the need for a legitimate police power justification”).

188. *Concrete Pipe*, 508 U.S. at 645.

189. *Lucas*, 505 U.S. at 1015-19 (emphasis added).

190. *Concrete Pipe*, 508 U.S. at 643 (citing *Village of Euclid v. Ambler Realty Co.*, 272 U.S. 365, 384 (1926) (approximately 75% diminution in value); *Hadacheck*, 239 U.S. 394 (finding that a ban on brickyard plant operations was not a taking because it was intended to protect human health even when the ban reduced the value of plaintiff's property from \$2 million to \$100,000 (92.5% diminution))). See also *Lucas*, 505 U.S. at 1019 n.8 (“It is true that in at least *some* cases the landowner with 95% loss will get nothing, while the landowner with total loss will recover in full.”); *Andrus*, 444 U.S. at 66 (although the regulation prevented “the most profitable use of [claimant's] property,” it did not prevent all use); *Haas v. City & County of San Francisco*, 605 F.2d 1117, 1120 (9th Cir. 1979) (diminution in value from \$2 million to \$100,000 not a tak-

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It is important to note that the Court has repeatedly held that it must analyze the impact of a regulation on the property as a whole. "At least where an owner possesses a full 'bundle' of property rights, the destruction of one 'strand' of the bundle is not a taking, because the aggregate must be viewed in its entirety."¹⁹¹ Thus, in *Keystone*, the Court rejected the argument that a regulation prohibiting the removal of more than 50% of the coal beneath certain structures constituted a taking of the unremoved coal.¹⁹²

The final factor identified by the Supreme Court in considering whether a regulation effects a compensable taking is the degree to which the regulation interferes with the claimant's "reasonable investment-backed expectations."¹⁹³ Thus, for example, the owner of property used in an activity already subject to extensive regulation has no reasonable expectation that new or changed regulations will not affect the value of that property.¹⁹⁴ A property owner "necessarily expects the uses of

ing). Even where a regulation has removed all economically beneficial use, the Court has refused to require compensation if the owner had no reasonable investment-backed expectation of being able to make that use of the property. See *infra*, text accompanying notes 193-196.

191. *Andrus*, 444 U.S. at 65-66. In *Concrete Pipe*, the Court stated: "To the extent that any portion of property is taken, that portion is always taken in its entirety; the relevant question, however, is whether the property taken is all, or only a portion of, the parcel in question." 508 U.S. at 644 (citing *Penn Central*, 438 U.S. at 130-32 ("[A] claimant's parcel of property [cannot] first be divided into what was taken and what was left for the purpose of demonstrating the taking of the former to be complete and hence compensable")).

192. *Keystone*, 480 U.S. at 497-98 (1987).

193. *Concrete Pipe*, 508 U.S. at 645 (quotation omitted). This factor is sometimes considered as a threshold question regarding whether the property interest at issue ever included the right to use the property in the manner prohibited by the regulation—if there is no such use interest, the regulation cannot be a taking. See, e.g., *M&J Coal Co. v. United States*, 47 F.3d 1148, 1153-54 (Fed. Cir. 1995). The Supreme Court applied the test in this manner in *Lucas*. See 505 U.S. at 1034-35 (Kennedy, J., concurring) (characterizing majority's consideration of the "nature of the owner's estate" as a test of "whether the deprivation is contrary to reasonable, investment-backed expectations").

194. See, e.g., *Concrete Pipe*, 508 U.S. at 645 ("[L]egislation readjusting rights and burdens is not unlawful solely because it upsets otherwise settled expectations ... even though the effect of the legislation is to impose a new duty or liability based on past acts"; "those who do business in the regulated field cannot object if the legislative scheme is buttressed by subsequent amendments to achieve the legislative end" (quotations omitted; citing numerous cases)); *Ruckelshaus*, 467 U.S. at 1007, 1009 (pesticide sale and use is an area that "has long been the source of public concern and the subject of government regulation"; no reasonable expectation of confidentiality because the

his property to be restricted, from time to time, by various measures newly enacted by the State in legitimate exercise of its police powers.”¹⁹⁵ Moreover, it is reasonable for an investor to expect legislation that imposes an economic burden in the form of liability for past harm caused by the investor, “whether or not the cost was foreseen at the time” the harm was caused.¹⁹⁶

Even a regulation prohibiting *all* economically beneficial use may not require compensation if “the logically antecedent inquiry into the nature of the owner’s estate shows that the proscribed use interests were not part of his title to begin with.”¹⁹⁷ In this respect, the Supreme Court has distinguished between personal and real property. Regarding personal property, the Court has stated that “by reason of the State’s traditionally high degree of control over commercial dealings, [the property owner] ought to be aware of the possibility that new regulation might even render his property economically worthless (at least

chemical industry has historically been “a focus of great public concern and significant government regulation” such that there was a substantial possibility that the Federal Government “would find disclosure to be in the public interest.”)

195. *Lucas*, 505 U.S. at 1028. See also *Goldblatt v. Town of Hemstead*, 369 U.S. 590, 593 (1962) (“A prohibition simply on the use of property for purposes that are declared, by valid legislation, to be injurious to the health, morals, or safety of the community, cannot in any just sense, be deemed a taking or an appropriation of property for the public benefit.”).

196. *Eastern Enterprises v. Apfel*, 118 S. Ct. 2131, 2153 (1998). In *Eastern Enterprises*, the Court held unconstitutional a law requiring a company to pay benefits to retired coal miners and their dependents, despite the fact that the company had not been in the coal business in approximately 30 years. A plurality opinion found the law to violate the Takings Clause because it “single[d] out certain employers to bear a burden that is substantial in amount, based on the employers’ conduct far in the past, and unrelated to any commitment that the employers made or to any injury they caused.” *Id.* at 2153. The plurality distinguished the case from other cases, however, because the coal law was “not calibrated either to [the claimant’s] past actions or to any agreement—implicit or otherwise—by the company,” *id.* at 2152 (citing *Concrete Pipe and Connolly*), and did not “merely impose liability for the effects of disabilities bred in the past [that] is justified as a rational measure to spread the costs of the employees’ disabilities to those who have profited from the fruits of their labor.” *Id.* (quoting *Usury v. Turner Elkhorn*, 428 U.S. 1, 18 (1976)). The plurality further stated that the claimant in *Eastern Enterprises* “might be responsible for employment-related health problems of all former employees whether or not the cost was foreseen at the time of employment,” but noted that the law at issue did not make any such connection. *Id.* at 2153.

197. *Lucas*, 505 U.S. at 1027.

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if the property's only economically productive use is sale or manufacture for sale)."¹⁹⁸

Regarding regulations affecting land, the Court would require compensation when a regulation prohibits all economically beneficial use unless the regulation simply implemented a restriction that already existed in "the background principles of the State's law of property and nuisance."¹⁹⁹ Thus, for example, the Court stated that the owner of a lakebed could be denied a permit to engage in a landfilling operation that would cause flooding in others' land without the denial, giving rise to a right to compensation.²⁰⁰ Nor would the corporate owner of a nuclear generating plant have a right to compensation if the state directed it to "remove all facilities from its land upon discovery that the plant sits astride an earthquake fault."²⁰¹ This special requirement is probably limited to land-use regulations that prohibit *all* economically beneficial use. In light of the Court's consideration of the economic impact of the regulation,²⁰² whether a regulation affecting land implements a preexisting

198. *Id.* at 1027-28.

199. *Id.* at 1029. "A law or decree with such an effect must, in other words, do no more than duplicate the result that could have been achieved in the courts—by adjacent landowners (or other uniquely affected persons) under the State's law of private nuisance, or by the State under its complementary power to abate nuisances that affect the public generally, or otherwise." *Id.*

200. *Id.* at 1030.

201. *Lucas*, 505 U.S. at 1030. The Court explained that:

such regulatory action may well have the effect of eliminating the land's only economically productive use, but it does not proscribe a productive use that was previously permissible under relevant property and nuisance principles. The use of these properties for what are now expressly prohibited purposes was *always* unlawful, and (subject to other constitutional limitations) it was open to the State at any point to make the implication of those background principles of nuisance and property law explicit.

Id. at 1029-30. A federal court of appeals directly addressed the Supreme Court's second hypothetical, rejecting a compensation claim based on the government's failure to issue an operating permit for a plutonium recycling plant, even though the government had actively promoted and induced the claimant's expenditure of over \$200 million to build the plant and had led the claimant to expect the permit before changing course and denying the permit. *Allied-General Nuclear Services v. United States*, 839 F.2d 1572 (Fed. Cir.), *cert. denied*, 488 U.S. 819 (1988). The court explained that "the basic rule that is dispositive here is that as against reasonable state regulation, no one has a legally protected right to use property in a manner that is injurious to the safety of the general public." *Id.* at 1576.

202. *See supra* notes 188-192 and accompanying text.

regulation should be less important if the regulation leaves some economically beneficial use of the property.²⁰³

Applying the analysis required by the Supreme Court, lower courts of the United States have rejected compensation claims arising out of a wide range of laws protecting the environment or human health, including, among many others, laws requiring the clean-up of harmful commercial byproducts²⁰⁴ or other hazardous materials;²⁰⁵ limiting harmful air emissions;²⁰⁶ restricting the sale and transport of endangered species;²⁰⁷ restricting the right to hunt particular animals on private land;²⁰⁸ requiring the destruction of abandoned buildings;²⁰⁹ and prohibiting the exploitation of natural resources on private property for reasons of public health, safety and welfare.²¹⁰

203. As Justice Kennedy stated in his concurring opinion in *Lucas*:

the State should not be prevented from enacting new regulatory initiatives in response to changing conditions, and courts must consider all reasonable expectations whatever their source Coastal property may present such unique concerns for a fragile land system that the State can go further in regulating its development and use than the common law of nuisance might otherwise permit.

Lucas, 505 U.S. at 1035 (Kennedy, J., concurring). Cf. *Miller*, 276 U.S. at 280 (in considering due process challenge to order requiring destruction of diseased trees, Court "need not weigh with nicety the question whether the infected cedars constitute a nuisance according to the common law; or whether they may be so declared by statute. For where, as here, the choice is unavoidable, we cannot say that its exercise, controlled by considerations of social policy which are not unreasonable, involves any denial of due process").

204. See, e.g., *Atlas Corp. v. United States*, 895 F.2d 745 (Fed. Cir. 1990) (law requiring uranium producers to clean up hazardous mill tailings not require compensation, even though the cleanup cost will be greater than the value of the mill and the government had encouraged the companies to produce the uranium).

205. See, e.g., *Kaufman v. City of New York*, 717 F. Supp. 84 (S.D.N.Y. 1989) (law requiring removal of asbestos from office buildings not a taking, despite fact that city had previously approved asbestos for fireproofing); *United States v. Northeastern Pharmaceutical*, 810 F.2d 726 (8th Cir. 1986) (rejecting takings claim based on retroactive application of US Superfund law requiring claimant to pay cleanup costs).

206. See, e.g., *Sierra Club v. EPA*, 540 F.2d 1114, 1139-40 (D.C. Cir. 1976), *vacated and remanded for reconsideration in light of subsequent legislation*, 434 U.S. 809 (1977).

207. See, e.g., *United States v. Kepler*, 531 F.2d 796 (6th Cir. 1976).

208. See, e.g., *Clajon*, 70 F.3d at 1566 (10th Cir. 1995) (limiting hunting licenses to two per landowner, regardless of size of property, not a taking).

209. See, e.g., *Hoeck v. City of Portland*, 57 F.3d 781 (9th Cir. 1995).

210. See, e.g., *MacLeod v. County of Santa Clara*, 749 F.2d 541 (9th Cir. 1984) (denial of timber harvest permit does not deny all economically viable use of property,

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2. *Regulatory Takings Under Canadian Law*

Canadian courts have generally refused to require compensation for the loss of property value caused by a legitimate government regulation unless the regulation actually transfers a benefit from the original owner to the government.²¹¹ This treatment arises out of the Canadian constitutional regime, pursuant to which

the provisional Legislatures ... probably have a general power to expropriate property in the province, simply by virtue of their legislative power over "property and civil rights in the province." The constitutional changes of 1982 put important restraints on the freedom of action of both the federal and provisional governments in the field of civil rights. But, they did not impose rights comparable to those of American constitutional law in favour of the owners of property. The Canadian Charter of Rights, section 7, assures that "everyone has the right to life, liberty and security of the person ...," but it does not go on, as do the Fifth and Fourteenth Amendments of the United States Constitution with respect to the powers of Congress or the States, to assure the right to "property."²¹²

despite claim that harvest is only profitable use); *SUCN Suarez v. Gelabert*, 541 F. Supp. 1253 (D. Puerto Rico 1982) (denial of sand extraction permit not a taking).

211. See PETER W. HOGG, *CONSTITUTIONAL LAW OF CANADA* 28-10 (1997) ("Where a statute is regulatory, not involving a taking of property, the general rule is that no compensation is payable for loss caused by the statute."). See also Michelle Swenarchuk, *Stomping on the Earth: Trade, Trade Law, and Canada's Ecological Footprints*, *BUFF. ENVTL. L.J.* 197, 211 (1998) ("Canadian law maintains the principle that legislatures may legitimately regulate property use in the public interest, without having to pay compensation if the measures are undertaken in good faith and do not involve a change in title.").

212. Donald S. Macdonald, *Sovereignty Revisited: Chapter 11 of NAFTA: What Are the Implications for Sovereignty?*, 24 *CAN.-U.S. L.J.* 281, 282 (1998) (quoting PETER W. HOGG, *CONSTITUTIONAL LAW OF CANADA* 396 (Carwell, Toronto, 2d ed. 1995) (citing Canadian Constitution § 92(13)); Constitution Act of 1982, Canadian Charter of Rights and Freedoms § 7). See also *A&L Investments Ltd. v. Ontario*, [1997] D.L.R.4th 692, 702 ("[T]he jurisprudence that has developed under the Charter [of Rights and Freedoms] has made clear that economic rights as generally encompassed by the term 'property' and the economic right to carry on a business, to earn a particular livelihood, or to engage in a particular professional activity all fall outside the s. 7 guarantee."

Under this scheme, “an aggrieved landowner must be able to demonstrate that not only has property been taken, but that the taking has also benefited the expropriating authority.”²¹³

In a recent case applying this principle, the Ontario Court of Appeal considered a claim that a law voiding previously-issued government orders permitting landlords to increase rents constituted a taking of the landlords’ property rights.²¹⁴ The court first noted that Canadian law applies a presumption pursuant to which “unless the words of the statute clearly so demand, a statute is not to be construed so as to take away the property of a subject without compensation.”²¹⁵ After reviewing several cases, the court concluded that “for the presumption of compensation to apply, ... the legislation must create what is in essence an expropriation of the plaintiff’s property by the state. The state must acquire the property taken from the plaintiff either for its own use or for the purpose of destruction.”²¹⁶ Regarding the claim before it, the court denied the compensation claim, holding that,

[w]hile the property rights of the plaintiffs voided by the [law] may, in one sense, be said to have been taken from the plaintiffs, in no sense can they be said to have been acquired by the Crown....

The [law] is not an act of expropriation by the Crown. Rather, it is an exercise of its regulatory authority.

(Citations omitted). HOGG, *supra* note 211, at 28-11 (“In Canada, ... neither the Constitution Act, 1867 nor the Charter of Rights contains any guarantee of compensation and, in the absence of any such guarantee, legislative power is unlimited. The position was accurately, if dramatically, put by the judge who said that ‘the prohibition “Thou shalt not steal” has no force upon the sovereign body.” (Citations and quotation omitted.))

213. Swenarchuk, *supra* note 211, at 208; *see also id.* (Under Canadian law “the term ‘expropriation’ traditionally refers to a landowner’s loss of use, title or benefit of property and a transfer of the value of use, title or benefit to a public authority.”); *See also* Queen in Right of British Columbia v. Tener [1985] 17 D.L.R.4th 1, 6 (“Expropriation or compulsory taking occurs if the Crown or a public authority acquires from the owner an interest in property”). *See also* A&L Investments, 152 D.L.R.4th 692.

214. A&L Investments, 152 D.L.R.4th at 695-696.

215. *Id.* at 698-699 (quotation omitted).

216. *Id.* at 700 (citing Steer Holdings Ltd. v. Government of Manitoba [1993] 2 W.W.R. 146 (Man. C.A.); Attorney-General v. De Keyser’s Royal Hotel [1920] A.C. 508; Burma Oil Co. Ltd. v. Lord Advocate [1965] A.C. 75 (H.L.)).

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There is no principle of statutory interpretation that would presume that those adversely affected by a statute regulating their affairs are entitled to compensation unless the statute says otherwise. No policy basis is readily apparent for such a rule. Indeed, such a principle would severely hamper the operation of the modern state where most regulatory legislation, however remedial, adversely affects someone. Moreover, if regulatory legislation voiding but not expropriating property rights triggered a presumed right to compensation from the state, the effect would be to give property rights the equivalent of the protection accorded by s. 7 of the Charter despite the clear exclusion of such rights from the Charter of Rights and Freedoms by its drafters. In other words, an individual would have the right not to be deprived of his property by regulatory legislation except with compensation or with an explicit override of that right by legislative language.²¹⁷

Canadian courts have applied these principles to uphold regulations even when the regulations have prohibited all effective use of the property in question. For example, in *Hartel Holdings Co. Ltd. v. Council of the City of Calgary*, the Supreme Court of Canada refused to require compensation when a law freezing development had removed all economically viable use of the claimant's land.²¹⁸ Because the city's actions were "taken pursuant to a legitimate and valid planning purpose, ... the resulting detriment to the appellant is one that

217. *Id.* at 701. The Supreme Court of Canada has suggested that the requirement of transfer to the government removes most regulatory actions from the category of expropriation requiring compensation. In *Tener*, 17 D.L.R.4th at 12, described *infra* text accompanying notes 222 - 226, the Court distinguished zoning regulations and the regulation of activities on lands, which "add nothing to the value of public property," from takings that enhance the value of government assets.

On the other hand, when a regulation does transfer the property in question to the government, Canadian courts have not hesitated to require compensation. For example, in *Manitoba Fisheries Ltd. v. The Queen* [1975] 88 D.L.R.3d 462, the Supreme Court of Canada upheld a compensation claim brought by the owner of a fish marketing corporation that had been put out of business when a Canadian law gave a monopoly in fish marketing to a government corporation. The Court based its conclusion on the fact that the law had transferred the claimant's business to the government. *Id.* at 469-71.

218. [1984] 8 D.L.R.4th 321.

must be endured in the public interest."²¹⁹ Similarly, in *La Ferme Filiber Ltee v. The Queen*,²²⁰ the court refused to require compensation to a claimant who was forced to shut down his trout-hatching enterprise, for which he had held an operating license for five years, because of a law prohibiting the operation of such hatcheries in the area.²²¹ The court's decision was based on the fact that, although the claimant's rights were extinguished, the regulation had not transferred any property interest to the government.²²²

Some Canadian cases have also distinguished between real and personal property, generally giving broad leeway to the government to regulate without incurring an obligation to compensate for the effects of the regulation on the value of personal property.²²³ This distinction is clear in two cases consid-

219. *Id.* at 334. See also *Soo Mill & Lumber Co. v. City of Sault Ste-Marie* [1975] 2 Can. S.C.R. 78, 83 (upholding zoning regulation that "sterilized [the claimant's land] in respect of any effective use," because development freezes not prohibited if enacted in accordance with the purpose of municipal plans or zoning regulations); *Sanbay Developments Ltd. v. City of London* [1975] 45 D.L.R.3d 403 (refusing to invalidate zoning regulation that froze development of claimant's land). Scholars have stated that the principle underlying *Soo Mill*, *Sanbay* and *Hartel Holdings* is that "planning authorities may regulate, restrict or prohibit land use or development without triggering the remedy of compensation for affected landowners, providing that such measures are undertaken in good faith for a proper planning purpose." RICHARD LINDGREN & KAREN CLARK, PROPERTY RIGHTS VS. LAND USE REGULATION: DEBUNKING THE MYTH OF "EXPROPRIATION WITHOUT COMPENSATION" 5-8 (Canadian Env'tl. L. Ass'n 1994) (quoted in Swenarchuk, *supra* note 211, at 210-11). See also Swenarchuk, *supra* note 211, at 208-09 ("Canadian courts have long recognized that land use regulation is not "expropriation," primarily because zoning by-laws [regulations] or other planning instruments do not generally involve a taking or transfer of the full use, title or benefit of property. Therefore, if a landowner's ability to use or develop his or her property is constrained by a properly enacted zoning by-law, the landowner is not entitled to compensation, even if the zoning by-law causes a diminution in property value.").

220. [1997]1 F.C. 128.

221. *Id.* at 128-29.

222. *Id.* at 130 ("An expropriation implies dispossession of the expropriated party and appropriation by the expropriating party; it necessarily requires a transfer of property or rights from one party to the other. There is nothing of that kind here. Defendant has not acquired anything belonging to plaintiff.").

223. See Swenarchuk, *supra* note 211, at 208 ("In Canada, the issue of expropriation generally arises in relation to real estate, not other forms of property"). The distinction between real and personal property has not been absolute. For example, in *Manitoba Fisheries v. The Queen* [1978] 1 S.C.R. 101, the Supreme Court of Canada held that the owner of a pre-existing private fish exporting business had a right to compensation for loss of the business's goodwill after a federal statute put him out of business by giving a government corporation the exclusive right to export fish.

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ering compensation claims arising out of the loss of property resulting from laws designating certain land as public parks.²²⁴ In each case, the claimant held rights related to the exploitation of subsurface minerals within the designated land and the designation prohibited mineral exploration and extraction.²²⁵ In *Queen in Right of British Columbia v. Tener*, the Supreme Court of Canada held that the claimant was entitled to compensation, relying on the fact that the property taken by the regulation, which included the right of access to the claim area, was a real property interest.²²⁶ In *Cream Silver Mines Ltd. v. British Columbia*, however, the court refused to follow the *Tener* decision and denied compensation, stating that although the claimant's mining claim was rendered useless, it was "material" that the interest at issue was not an interest in land.²²⁷

3. *Regulatory Takings Under Mexican Law*

Article 27 of the Mexican Constitution provides:

Ownership of the lands and waters within the boundaries of the national territory is vested originally in the Nation, which has had, and has, the right to transmit title thereof to private persons, thereby constituting private property.

Private property shall not be expropriated except for reasons of public use and subject to payment of indemnity.

224. *Tener*, 17 D.L.R.4th at 5; *Cream Silver Mines Ltd. v. British Columbia* [1993] 99 D.L.R.4th 199, 205.

225. *Tener*, 17 D.L.R.4th at 3, 5; *Cream Silver Mines*, 99 D.L.R.4th at 205.

226. *Tener*, 17 D.L.R.4th at 3 (claimant's grant entitled it to "all [subsurface] minerals ... and the right to the use and possession of the surface of such mineral claim ... for the purpose of winning and getting from and out of such claim the minerals contained therein"). See also *id.* at 6 (grant was interest in land). The Court also noted that the denial of access to the park lands enhanced the value of the government's asset (the park). See *id.* at 12.

227. *Cream Silver*, 99 D.L.R.4th at 202, 205-206 (as opposed to the Crown grant at issue in *Tener*, this is simply a mineral claim; there has never been any absolute right of access to the claim area to obtain the ore, the government has power to refuse to grant right of way, and such claims "have never been capable of registration under the ... system of land regulation").

The Nation shall at all times have the right to impose on private property rights the limitations dictated by the public interest, as well as to regulate, for the collective good, the use of natural resources susceptible to appropriation, to ensure a more equitable distribution of public wealth, to conserve them, to achieve the well-balanced development of the country and the improvement of the living conditions of the rural and urban population.²²⁸

This provision clearly distinguishes between expropriation—which, under Mexican law, consists of “legally taking a thing from its owner, for reasons of public utility, and giving the owner a fair indemnification”²²⁹—and the limitations (*modalidades*) referred to in the third paragraph, which do not require indemnification even though they may affect the value of property.²³⁰ The Mexican Supreme Court of Justice has explained

228. Const. of Mexico, Tit. I, Chap. I, art. 27, in CONSTITUTIONS OF THE COUNTRIES OF THE WORLD (Apr. 1988 & Supp. June 1998).

The Constitution also conditions the right of foreigners to own “lands, waters, and their appurtenances, or to obtain concessions for the exploitation of mines or waters” on the foreigners’ agreement that they will “consider themselves as nationals in respect to such property and bind themselves not to invoke the protection of their governments in matters relating thereto; under penalty, in case of noncompliance with this agreement, of forfeiture of the acquired property to the Nation.” *Id.*, art. 27.I (Supp. June 1998). This provision is a codification of the “Calvo Doctrine” regarding expropriation, which is followed by most Latin American nations. See Justine Daly, *Has Mexico Crossed the Border on State Responsibility for Economic Injury to Aliens? Foreign Investment and the Calvo Clause in Mexico After NAFTA*, 25 ST. MARY L.J. 1147, 1150, 1163-65 (1994). The United States has consistently rejected the Calvo Doctrine as a basis for the treatment of foreign investment. See *id.* at 1166-71.

229. JUAN JOSÉ GONZÁLEZ MARQUEZ, *NUEVO DERECHO AMBIENTAL MEXICANO (INSTRUMENTOS DE POLÍTICA)* 154 (Universidad Autónoma Metropolitana 1997) (translations by author) (quoting Monique Lions, *Expropiación*, in *Instituto de Investigaciones Jurídicas*, *DICCIONARIO JURÍDICO MEXICANO* 1389 (Mexico, Porrúa-UNAM 1992). See also GABINO FRAGA, *DERECHO ADMINISTRATIVO* 375-76 (Mexico 1984) (translations by author) (“in the case of expropriation an individual is deprived of his or her goods inasmuch as this is necessary for the state”).

230. See FRAGA, *supra* note 229, at 375-76 (“Expropriation for reasons of public value is to be distinguished from the limitations that the State may impose on private property for reasons of public interest (Art. 27, para. III, Federal Const.)). In the words of one Mexican legal scholar,

[t]he right to property [under the Mexican Constitution] is not an absolute right, but is a right that serves a social function, and therefore, in Article 27... the Nation is empowered to limit the exercise of that right. [Article 27] signifies that private property is of a derivative character and as a result the nation may impose limitations on it.

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that these latter limitations constitute “a partial extinction of the rights of the owner,” whereas

expropriation amounts to the substitution of the right to use and ownership of the thing for the enjoyment of the indemnity. Regarding the former [limitations], the suppression of the partial authority of the owner occurs without any consideration; regarding the latter, the damage caused is compensated through the payment of the value of the rights lost.²³¹

Limitations that do not require indemnification must be generally applicable, rather than specifically directed at an identified piece of property, and must remove only limited attributes of the owner’s right to the property, rather than transferring to the State ownership of the property.²³² Using these criteria, the Mexican Supreme Court has not required indemnification for the effects of regulations prohibiting a general category of activities in certain types of locations, such as regulations prohibiting the construction of ovens, chimneys or certain other potentially hazardous structures less than a prescribed distance from the property of another.²³³ Another example of property limitations that do not require indemnification are decrees, issued pursuant to the General Law of Ecological Balance, limiting the use of property within natural protected ar-

GONZÁLEZ MARQUEZ, *supra* note 229, at 152-53.

231. [Supreme Court of Justice Report] 1980, Pleno tesis 29, at 543 (quoted in FRAGA, *supra* note 229, at 376-77).

232. González Marquez, *supra* 228, at 156-58 (citing Mexican Supreme Court of Justice, Séptima Época, Primera Parte: Volúmenes 133-38, 155. Amparo en revisión 6408/76. María Fortes de Lamas, 18 Mar. 1980). See also Supreme Court of Justice Report 1980, *supra* note 231 (limitations “suppose a general and permanent restriction on the property right; [expropriation] implies the transfer of the rights over a specific good through the intervention of the state”); FRAGA, *supra* note 229, at 375-76 (“[T]here are differences of form and substance between limitations and expropriation. The former is a measure of general and abstract character that is part of and shapes, but does not transform, the legal regime regarding the general ownership of property in a given time and place. Expropriation, on the other hand, constitutes a measure of individual and specific character whose effects are concentrated on a specific property.”).

233. GONZÁLEZ MARQUEZ, *supra* note 229, at 165-66 (citing unanimous decision of Mexican Supreme Court of Justice, Tomo CXL, at 1918. Amparo civil en revisión 943/48. Díaz de Garza Consuelo, 14 Mar. 1952).

eas.²³⁴ Because these regulations do not remove all of the owner's rights in the property, and are of general application, they do not require compensation.

B. INDIRECT EXPROPRIATION UNDER INTERNATIONAL LAW

International law addresses the takings issue under the rubric of "expropriation" — which is "a compulsory transfer of property rights"²³⁵ — and refers to regulatory takings as "indirect expropriation," "disguised expropriation" or "creeping expropriation."²³⁶ Although a government must generally provide compensation for expropriation,²³⁷ it is "an accepted principle of international law that a State is not liable for economic injury which is a consequence of bona fide 'regulation' within the accepted police power of states."²³⁸ Thus, "anti-trust, consumer protection, securities, environmental protection, land planning and other legislation, are non-compensable takings. These

234. *Id.* at 161-62.

235. *Amoco Int'l Fin. v. Government of the Islamic Republic of Iran*, 27 I.L.M. 1320, 1342-43 (1988). The "paradigm" of direct expropriation consists of "an involuntary transfer of ownership effected immediately by legislation in pursuance of state policy. This results in the vesting of ownership of the property in the state or a state entity created to run the industry that is taken over and the destruction of the rights of ownership of the foreign investors in the industry." SORNARAJAH, *supra* note 159, at 282.

236. SORNARAJAH, *supra* note 159, at 282. One scholar rejects the phrase "creeping expropriation" for fear that it "suggests a deliberate strategy on the part of the state, which may imply a negative moral judgment." Rudolf Dolzer, *Indirect Expropriation of Alien Property*, 1 ICSID REVIEW, FOREIGN INV. L.J. 41, 44 (1986).

237. *See* Restatement (Third) of the Foreign Relations Law of the United States § 712.

238. *Sedco, Inc. v. National Iranian Oil Co.*, Interlocutory Award 9 Iran-U.S. Cl. Trib. Rep. 248, 275 (1985). The Restatement (Third) of the Foreign Relations Law of the United States § 712, cmt. g, states that a State need not provide compensation for loss of property or for other economic disadvantage resulting from bona fide general taxation, regulation, forfeiture for crime, or other action of the kind that is commonly accepted as within the police power of states, if it is not discriminatory and is not designed to cause the alien to abandon the property to the state or sell it at a distress price.

See also id. at reporter's note 6 ("It is often necessary to determine ... whether an action by a state constitutes a taking and requires compensation under international law, or is a police power regulation or tax that does not give rise to an obligation to compensate even though a foreign national suffers loss as a consequence."); SORNARAJAH, *supra* note 159, at 299 (1994) ("Obviously, infringements of property rights in controlling hazardous or environmentally sound use of property ... are regulatory takings that require no compensation"; "It cannot be claimed by the citizens of these states that compensation is due to them when there is such regulatory intervention.").

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regulations are regarded as essential to the efficient functioning of the state."²³⁹

Legal scholars have long affirmed this principle.²⁴⁰ The evidence supporting these scholarly pronouncements has generally consisted of the decisions of international courts and tribunals that have decided claims of expropriation. Although international law generally recognizes judicial decisions as a subsidiary source of international law,²⁴¹ and the principles of

239. SORNARAJAH, *supra* note 159, at 283.

240. See, e.g., G.C. Christie, *What Constitutes a Taking of Property Under International Law*, 38 BRIT. Y.B. INT'L L. 307, 331-32 (1962) ("[T]he operation of a State's tax laws, changes in the value of a State's currency, actions in the interest of the public health and morality, will all serve to justify [*i.e.*, remove from the category of expropriatory or compensable acts] actions which because of their severity would not otherwise be justifiable; subject to the proviso, of course, that the action in question is not what would be commonly called discriminatory [with respect to aliens]."); S. FRIEDMAN, *EXPROPRIATION IN INTERNATIONAL LAW* 1 (1953) ("Indirect expropriation resulting from the normal functioning of public services would not appear to give rise to any great difficulty from the point of view of international law."). See also, SORNARAJAH, *supra* note 159, at 282-83 ("all measures affecting property rights" would not be an acceptable definition of taking in international law "for the simple reason that normal activities of states, such as taxation, affect property rights and cannot be expected to give rise to international concern."); *id.* at 303 ("[T]he generally accepted view is that the exercise of [the power to increase taxation] cannot be regarded as a taking in violation of property rights.").

241. As with any norm of international law, principles concerning expropriation derive from three primary sources. See Statute of the International Court of Justice, June 26, 1945, art. 38, para. 1, 59 Stat. 1033, 1060. The most authoritative sources of international legal obligations for a particular nation are found in international agreements to which that nation is a party and customary international law, which reflects state practice grounded in a belief that the practice is required by law. See *id.*; Restatement (Third) of the Foreign Relations Law of the United States, §§ 102(1)-(4), 103(2) (1987). As noted above, note 22 and accompanying text, international agreements addressing indirect expropriation seldom define precisely what it is or when it gives rise to an obligation to provide compensation. One U.S. government official has stated that international investment agreements "do not generally call into question the sovereign right of governments to regulate as long as regulation does not single out or discriminate against investors based on their nationality." Larson Testimony, *supra* note 15.

A secondary source of international law are "general principles of law common to the countries of the world." ICJ Statute, *supra*, para. 1.d. In this regard, it is worth noting that the constitutions of 19 nations make clear that governmental measures that affect the value of property will not be considered compensable takings where those measures are intended to protect human, animal or plant health, or (regarding taking of land) to conserve soil or other natural resources. See CONSTITUTIONS OF THE COUNTRIES OF THE WORLD (Apr. 1997 & Supps.) (constitutions of Antigua and Barbuda, Bahamas, Barbados, Belize, Botswana, Dominica, Gambia, Grenada, Jamaica, Kenya, Malta, Mauritius, Papa New Guinea, Saint Christopher and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Tuvalu, Zambia, Zimbabwe). Such provisions, along with the consis-

stare decisis does not formally apply to international tribunals,²⁴² the general lack of more authoritative sources addressing the limits of indirect expropriation gives such decisions a special legitimacy.²⁴³

One of the most prolific interpreters of the international law of expropriation has been the Iran-U.S. Claims Tribunal, which was established in 1981 to adjudicate claims by nationals of each country against the government of the other.²⁴⁴ In reviewing the Tribunal's decisions until 1994, one member of the

tent practice of national courts, which, with the exception of US, Canadian and Mexican practice, is beyond the scope of this Article, support the conclusion that international law does not require compensation for the economic effects of environmental regulations.

Judicial decisions and the writings of scholars serve as "subsidiary means for the determination of rules of law." ICJ Statute, *supra*, para. 1.d.

242. For example, the Statute of the International Court of Justice provides: "The decision of the Court has no binding force except between the parties and in respect of that particular case." ICJ Statute, *supra* note 241, art. 59.

243. Modern tribunals deciding expropriation claims have "placed their principal reliance on judicial and arbitral precedents." Patrick M. Norton, *A Law of the Future or a Law of the Past? Modern Tribunals and the International Law of Expropriation*, 85 AM. J. INT'L L. 474, 498 (1991). Norton notes several reasons for this phenomenon, including a "natural predisposition of arbitrators toward the approach of their predecessors" and the legitimacy provided when a case is decided consistently with previous analogous cases. *Id.* at 498-99. Moreover, in the absence of a clear international statement or applicable treaty resolving the question, "such precedents have a tendency to coalesce into a source of legitimacy." *Id.* at 500.

244. Declarations of the Government of the Democratic and Popular Republic of Algeria Concerning Commitments and Settlement of Claims by the United States and Iran with respect to Resolution of the Crisis arising out of the Detention of 52 United States Nationals in Iran, with Undertakings and Escrow Agreement, Jan. 19, 1981, T.I.A.S. (entered into force Jan. 19, 1981). Although the Iran-US Claims Tribunal primarily applies the Treaty of Amity between Iran and the United States, Treaty of Amity, Economic Relations and Consular Rights, Aug. 15, 1955, 284 U.N.T.S. 93 (entered into force June 16, 1957),

[i]t is beyond doubt that international law has been the applicable law in cases where expropriation has been an issue before the Tribunal.... Nevertheless, as regards the questions of expropriation ... there is no indication that the Tribunal conceives the Treaty standards to differ from standards of customary international law. Rather, ... the Tribunal has emphasized, for example, that the Treaty does not add anything to the general rules of international law insofar as concerns the concept of a taking.

Matti Pellonpaa, *Compensable Claims Before the Tribunal: Expropriation Claims*, in THE IRAN-UNITED STATES CLAIMS TRIBUNAL: ITS CONTRIBUTION TO THE LAW OF STATE RESPONSIBILITY 186-87 (Richard B. Lillich & Daniel Barstow Magraw eds., 1997) (citations omitted). See also *Sedco, Inc.*, 9 Iran-U.S. Cl. Trib. Rep. at 273 ("[T]he Treaty of Amity on the particular issue of what constitutes a taking incorporates the rules of customary international law.").

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Tribunal, George Aldrich, described the Tribunal's understanding that, under international law, "[l]iability does not arise from actions that are nondiscriminatory and are within the commonly accepted taxation and police powers of states."²⁴⁵ Numerous other tribunals have reached the same conclusion.²⁴⁶

International tribunals have seldom, if ever, addressed whether environmental regulations affecting foreign-owned property give rise to a right to compensation. However, an examination of cases addressing indirect expropriation claims arising out of regulations promoting other government interests demonstrates that international law would not support an expropriation claim arising out of legitimate environmental regulations.

International tribunals have not agreed on a definitive test establishing when indirect expropriation gives rise to a right to compensation. Although these tribunals have not agreed to a list of factors relevant to the question, they frequently refer to factors similar to those described by the U.S. Supreme Court.

For example, international tribunals have considered whether government actions leading to indirect expropriation are "reasonable."²⁴⁷ In one such case, the Iran-U.S. Claims Tri-

245. George H. Aldrich, *What Constitutes a Compensable Taking of Property? The Decisions of the Iran-United States Claims Tribunal*, 88 AM. J. INT'L L. 585, 609 (1994) [hereinafter Aldrich I]. See also GEORGE H. ALDRICH, *THE JURISPRUDENCE OF THE IRAN-UNITED STATES CLAIMS TRIBUNAL* 217 (1996) (same) [hereinafter ALDRICH II]. See, e.g., *Sedco, Inc.*, 9 Iran-U.S. Cl. Trib. Rep.; *Too v. Greater Modesto Insurance Assocs.*, 23 Iran-U.S. Cl. Trib. Rep. 378 (1989).

246. See, e.g., *Kugele v. Polish State*, 6 Ann. Dig. Int'l L. 69 (1931-32) (Upper Silesian Arb. Trib. 1930) (series of license fees that forced claimant to close brewery did not constitute compensable taking); *Brewer, Moller & Co. Case (Ger. v. Ven.)*, 10 R. Int'l Arb. Awards 423 (1903) (taxes legally levied and without discrimination cannot be recovered); *Liselotte Hauer v. Land Rheinland-Pflaz*, 1979 E.C.R. 3727 (considering, *inter alia*, "principles of international law," finding no expropriation when EEC regulations prohibited claimant from planting a certain type of grapevine because the regulations promoted the general welfare). See also *West v. Multibanco Comermex, S.A.*, 807 F.2d 820, 831 (9th Cir. 1987), *cert. denied*, 482 U.S. 906 (1987) ([U]nder international law, "[v]alid expropriations must always serve a public purpose; that public purpose in some cases may be so strong as to render lawful what otherwise might constitute a 'taking'; finding no taking because requiring foreign funds to be surrendered in exchange for local (less valuable) fund was a legitimate exercise of the police power.).

247. See *supra* notes 163-170 and accompanying text.

bunal considered an expropriation claim arising out of the refusal of a government bank to honor the claimant's checks because of a law establishing certain authentication requirements.²⁴⁸ The Tribunal refused to find an expropriation because it did not find the bank's actions to amount to "unreasonable interference" with the claimant's property.²⁴⁹ Other cases have concluded that government regulations were reasonable when they imposed taxes,²⁵⁰ prohibited planting new grapes to regulate wine production,²⁵¹ and regulated the production of alcohol through license fees.²⁵²

Like the U.S. Supreme Court, international law requires something more than a simple governmental declaration that a particular interference with an alien's enjoyment of his or her

248. *Harza Engineering Co. v. Iran*, 1 Iran-U.S. Cl. Trib. Rep. 499, 504 (1981-82). Because of its finding, the Tribunal found it unnecessary to determine "how unreasonable the interference must be to constitute a taking of property." *Id.*

249. *Id.* at 505. See also *Mark Dallal v. Iran*, Award No. 53-149-1 (10 June 1983), reprinted in 3 Iran-U.S. Cl. Trib. Rep. 10 (refusing compensation for bank's refusal to honor checks because no indication that banks had acted unreasonably). These decisions follow general international legal practice, which considers financial regulation to be among the legitimate police powers of government. See *Pellonpaa*, *supra* note 244, at 253 (noting that the Iran-US Claims Tribunal's treatment of cases involving financial regulations "has not been decisively different" from "previous international legal practice, [in which] exchange control regulations and other restrictions on the transfer of funds abroad have been accepted to a very significant degree").

250. See *Too*, 23 Iran-U.S. Cl. Trib. Rep. at 387 (refusing to require compensation for government seizure of claimant's liquor license for failure to pay taxes due because "a State is not responsible for loss of property or for other economic disadvantage resulting from bona fide general taxation or any other action that is commonly accepted as within the police power of States, provided it is not discriminatory and is not designed to cause the alien to abandon the property to the State or to sell it at a distress price."); *Brewer, Moller & Co.*, 10 R. Int'l Arb. Awards at 423 (taxes legally levied and without discrimination cannot be recovered).

251. *Hauer*, 1979 E.C.R. at 3745-49. Although the court in *Hauer* applied European law, the relevant protection of property rights depends on principles of international law. See *id.* at 3745 (applying Article I of Protocol to European Convention for the Protection of Human Rights, which protects property rights "subject to the conditions provided for ... by the general principles of international law").

252. See, e.g., *Kugele*, 6 Ann. Dig. at 69 (series of license fees that forced claimant to close brewery did not constitute compensable taking). In *Kugele*, the tribunal stated that

there is an essential difference between the maintenance of a certain rate of profit in an undertaking and the legal and factual possibility of continuing the undertaking. The trader may feel compelled to close his business because of the new tax.... But this does not mean that he has lost the right to engage in the trade.

Id. at 69 (citing 3 SCHIDSGERICHT FÜR OBERSCHLESISIEN at 24).

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property is justified by the so-called 'police power,' "[b]ut, if the reasons given are valid and bear some plausible relationship to the action taken, no attempt may be made to search deeper to see whether the State was activated by some illicit motive."²⁵³ Thus, the European Court of Justice considered "whether there exists a reasonable relationship between the measures provided for by the regulation [a prohibition on planting new grapes] and the aim pursued by the Community in this case [to regulate wine production]."²⁵⁴

International decisions also recognize that the severity of the economic impact caused by an indirect expropriation is relevant to determining whether compensation is required.²⁵⁵ International tribunals have refused to require compensation when the expropriation did not remove all economic value from the property. As explained by one scholar considering the jurisprudence of the Iran-U.S. Claims Tribunal,

before measures restricting the rights of owners to use and dispose of their property will be considered to amount to expropriation it must be apparent that the governmental actions have so completely deprived the owners of their property rights that the rights are rendered nugatory. Such findings are more readily made where the government has the avowed intention of socialising the economy and thereby depriving private owners of their property rights. * * * [T]he principal test as to whether actions falling short of a formal taking of title constitute a taking is whether or not the action fundamentally restricts the right of the owner to

253. Christie, *supra* note 240, at 338.

254. Hauer, 1979 E.C.R. at 3747.

255. This principle may be a "general principle of law," recognized as a source of international law. See *supra* note 241. One scholar reviewing "representative" legal systems concluded that

a comparison of domestic law leaves no doubt that the prohibition of economically optimal use of property in itself may not be equated with an indirect expropriation.... A survey of the relevant domestic laws indicates that [the point at which the regulation of property assumes the quality of an indirect expropriation] lies where the property in question, after introduction of the measure concerned, can no longer be put to reasonable economic use.

Dolzer, *supra* note 236, at 62.

manage or dispose of the property, or if the property has been rendered virtually valueless. Governmental actions which limit the owner's right in relation to his property but which do not significantly affect the aforementioned fundamental rights generally do not amount to expropriation of the property entitling the owner to compensation.²⁵⁶

This principle has been applied by the Iran-U.S. Claims Tribunal to decide an expropriation claim arising out of Iranian exchange restrictions that prohibited the Iranian Central Bank from converting claimant's money into a currency that could be transferred out of the country.²⁵⁷ When the claimant sought compensation, the Tribunal concluded that Iran had not expropriated the funds, because the "account remain[ed] in existence and available, in [Iranian currency], at [the claimant's] disposal."²⁵⁸ Similarly, the Tribunal refused to find an expropriation when Iranian law prohibited the exportation of certain property but the claimant maintained the option to sell the property in Iran.²⁵⁹

256. WAYNE MAPP, *THE IRAN-US CLAIMS TRIBUNAL: THE FIRST 10 YEARS* 152, 155 (1993). In *Starrett Housing Corp. v. Iran*, 4 Iran-U.S. Cl. Trib. Rep. 122, 154 (1983), the Tribunal stated:

[I]t is recognized in international law that measures taken by a State can interfere with property rights to such an extent that these rights are rendered so useless that they must be deemed to have been expropriated, even though the State does not purpose to have expropriated them and the legal title to the property formally remains with the original owner.

257. See *Sea-Land Service, Inc. v. Iran*, 6 Cl. Trib. Rep. 149 (1984-II) cited in *Peltonpaa*, *supra* note 244, at 253.

258. *Id.* at 167 (citing *Harza Engineering Co.*, 1 Iran-U.S. Cl. Trib. Rep. 499, in which "the Tribunal held that the refusal of [the bank] to honour four cheques drawn on the Claimant's account could have been motivated by reasons of legitimate banking practice, and did not constitute an interference with the Claimant's right to deal with the account as a whole"). The *Sea-Land* Tribunal found "insufficient evidence that [the bank] intentionally obstructed the progress of the [transfer] application, or that it interfered unlawfully in any way with [claimant's] use of its account." *Id.*

259. *Seismographic Service Corp. v. National Iranian Oil Co.*, 22 Iran-U.S. Cl. Trib. Rep. 3, 78-81 (1989-II). See also *Sedco, Inc.*, 9 Iran-U.S. Cl. Trib. Rep. at 275 ("When an action ... results in an outright transfer of title rather than incidental economic injury, ... a taking must be presumed to have occurred."). Other international tribunals have reached the same conclusion. See, e.g., *Mitzi Schoo*, Decision No. CZ-279 (1960), U.S. FOREIGN CLAIMS SETTLEMENT COMMISSION, FOURTEENTH SEMI-ANNUAL REPORT (1961), at 180 (hereinafter *FOURTEENTH SEMI-ANNUAL REPORT*).

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Other tribunals have applied similar reasoning. The European Court of Human Rights, interpreting a claim under a European human rights instrument providing for the right of “peaceful enjoyment of ... possessions,” did not find indirect expropriation to have occurred as a result of land use regulations that affected the claimant’s property because,

although the right [of peaceful enjoyment of possessions] lost some of its substance, it did not disappear The Court observe[s] in this connection that the [claimants] could continue to utilise their possessions and that, although it became more difficult to sell properties [as a result of the regulations], the possibility of selling subsisted.²⁶⁰

Likewise, the U.S. Foreign Claims Settlement Commission rejected a compensation claim based on the government’s refusal to grant an export license for the claimant’s jewelry.²⁶¹

Another component in considering the severity of the impact on property is the duration of the regulation causing the im-

As under U.S. law, however, an action that renders the property entirely worthless may require compensation, even if the action was justifiable. For example, in *Phelps Dodge Corp. v. Iran*, 10 Iran-U.S. Cl. Trib. Rep. 121, 129-130, 25 ILM 619, 625 (1986), the Iran-U.S. Claims Tribunal considered a claim arising out of Iran’s replacement of the managers of the claimant’s company with government representatives pursuant to a regulation designed to prevent the closure of factories, ensure payments due to workers and protect debts owed to the Government. The Tribunal found an expropriation even though it “fully underst[ood]” the reasons for the regulations. *Id.* According to one member of the *Phelps Dodge* panel, the Tribunal’s award of compensation despite the arguable legitimacy of the measures at issue “was doubtless influenced by its perception that the deprivations were likely to be permanent, even when termed ‘provisional’” and that the measure gave the government full control over the property. *See Aldrich I, supra* note 245, at 590.

260. *Sporrong and Lonnroth v. Sweden*, (1982) Eur. Ct. H. R. A/52 available in LEXIS, Intlaw Library, ECCASE file. *See also West v. Multibanco Comermex, S.A.*, 807 F.2d 820, 831 (9th Cir. 1987), *cert. denied*, 482 U.S. 906 (1987) (no taking under international law where legitimate exchange controls reduced value of claimant’s funds).

261. Erna Spielberg, Decision No. CZ-2 466 at 146-47 (1961), FOURTEENTH SEMI-ANNUAL REPORT, *supra* note 259, at 146 (refusal to grant export license for jewelry not a taking). Using analogous reasoning, the Iran-U.S. Claims Tribunal has refused to require compensation for loss of value of a minority shareholder’s interest in a company after the government expropriated the holdings of a majority shareholder because the minority shares retained value. *See, e.g., Ataollah Golpira v. Iran*, 2 Iran-U.S. Cl. Trib. Rep. 171 (1983).

pact. Thus, Iran-U.S. Claims Tribunal decisions appear to indicate that “[o]ne or two isolated instances of interference ... do not suffice [for a compensable taking]; proof appears to be required that the blocking is of a more comprehensive nature.”²⁶² Similarly, when the European Court of Justice denied a compensation claim arising out of the grape restriction, it did so in part because the regulatory action was to be valid for only two or three years.²⁶³

International decisions have also noted that whether the foreign property owner could reasonably have expected the particular impact on her property is relevant to whether a government regulation gives rise to a right to compensation. For example, in *Starrett Housing v. Iran*, for example, the Iran-U.S. Claims Tribunal refused to find an indirect expropriation based on the inability of the claimant to complete a construction project due to strikes, work stoppages, the collapse of the Iranian banking system and other obstacles that were the result of the Iranian revolution.²⁶⁴ The Tribunal noted that

investors in Iran, like investors in all other countries, have to assume a risk that the country might experience strikes, lock-outs, disturbances, changes of the economic and political system and even revolution. That any of these risks materialized does not necessarily mean that property rights affected by such events can be deemed to

262. Pellonpaa, *supra* note 244, at 252 (describing *Harza Engineering* case). One Tribunal member has concluded that

[p]rovisional or temporary assumption of control of an alien's property by State action gives rise to liability whenever the deprivation is not merely "ephemeral" in the sense that (a) no reasonable prospect exists that control will be returned; or (b) that any losses that may ensue during the period of control are not compensable to the property owner; or (c) that the control has continued for a substantial period of time (perhaps several years) in circumstances where the property owner has not behaved in a manner clearly inconsistent with a claim of deprivation.

ALDRICH II, *supra* note 245, at 217.

263. *Hauer*, 1979 E.C.R. at 3749. The US Foreign Claims Settlement Court has also rejected compensation claims when national administration of property has been only temporary. See, e.g., Public Law 85-604 Panel Opinion No. 6, Part I, ELEVENTH SEMIANNUAL REPORT (1959), at 28-29; FOURTEENTH SEMIANNUAL REPORT, at 134-35.

264. *Starrett Housing Corp.*, 4 Iran-U.S. Cl. Trib. Rep. At 156 (1983), 23 I.L.M. at 1117.

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have been taken. A revolution as such does not entitle investors to compensation under international law.²⁶⁵

The same reasoning applies to the possibility of encountering legitimate government regulations:

[I]t could be argued that the foreign investor entered the state voluntarily, knowing the risk of ... regulatory laws being applied against him, and that he should bear the risk of such adverse changes as any citizen of the state would. It should not be the function of the international law to insulate the foreign investor from the regulatory regime of the host state's laws.²⁶⁶

This discussion demonstrates that international law does not require compensation for the economic impact of regulations that are a legitimate exercise of government police power. This rule holds particularly true when the regulation leaves the affected property with some value and is one that could reasonably be expected given the nature of the regulated activity. Although no international tribunal has yet applied this rule to environmental regulations, the following discussion will demonstrate that it applies with particular force in such cases.

265. *Id.* See also *Sedco, Inc.*, 9 Iran-U.S. Cl. Trib. Rep. at 275 (When property is forfeited as the result of a crime, no taking has occurred because "the person(s) affected do not rightfully possess title to the property in question.").

266. SORNARAJAH, *supra* note 159, at 300. As evidence that this principle is generally recognized and thus supports an international norm, Professor Dolzer notes that the various domestic orders uniformly indicate, in principle, that no compensation is due when the measure is necessary in order to protect the public from a danger arising from the property; the police power in its various forms generally overrides property rights, even though certain definitional issues have plagued courts and commentators in this area. When the measure is not based on the police power and infringes upon existing use, the state normally will enter into conflict with legitimate ... investment backed expectations based on property rights[, which] will typically violate the guarantee of private property in the absence of compensation.

Dolzer, *supra* note 236, at 62.

VI. UNDER NAFTA AND INTERNATIONAL LAW,
ENVIRONMENTAL MEASURES ARE A LEGITIMATE
EXERCISE OF POLICE POWER THAT SHOULD NOT
NORMALLY GIVE RISE TO A RIGHT TO COMPENSATION

NAFTA does not define what constitutes "expropriation" or a "measure tantamount to ... expropriation." The terms must therefore be interpreted consistently with international law and in light of their context.²⁶⁷ As demonstrated above, it is "an accepted principle of international law that a State is not liable for economic injury which is a consequence of bona fide 'regulation' within the accepted police power of states."²⁶⁸ To the best of my knowledge, however, no international tribunal has yet considered whether this principle applies to environmental regulations, although scholars have assumed that it does²⁶⁹ and the United States claims to agree.²⁷⁰

267. Article 31 of the Vienna Convention on the Law of Treaties, U.N. Doc. A/CONF. 39/27 (1969), 8 I.L.M. 679 (1969), provides that interpretation of a treaty is to take into account "any relevant rules of international law applicable in the relations between the parties." The NAFTA parties apparently intended the expropriation provision to implement international law. In responding to questions from Congress, US Trade Representative Kantor stated that NAFTA's expropriation provision would mean that Mexico (and presumably Canada and the United States as well) "will now be governed by common international law in respect of any nationalizations or expropriations of foreign investments." *North American Free-Trade Agreement (Nafta) And Supplemental Agreements To The Nafta: Hearing Before The Committee On Ways And Means And Its Subcommittee On Trade*, 103rd Cong., 1st Sess., (Sept. 14, 15, 21, 23, 1993) (statement from Micky Kantor, U.S. Trade Representative) (in *Arnold & Porter Legislative History*: P.L. 103-182 at 90).

268. *Sedco, Inc.*, 9 Iran U.S. Iran Cl. Trib. At 275. See generally *supra* Part V.

269. See, e.g., SORNARAJAH, *supra* note 159.

270. Assistant U.S. Secretary of State for Economic, Business, and Agricultural Affairs Alan P. Larson noted the concern that, in its current form, the expropriation provision of the MAI, which is substantially similar to that of NAFTA,

could be misinterpreted to go beyond international (and U.S. "takings") law.

There is consensus among negotiators that any ambiguity on this point must be eliminated. *Normal regulatory actions, even when they affect the value of an investment, should not be considered as an expropriation requiring compensation....* There is emerging consensus that the MAI must include meaningful commitments on both labor and environment. We all agree that the MAI must not and will not undermine the ability of governments to regulate for protection of health, safety and the environment.

Larson, *supra* note 88, at 51 (in light of the ongoing MAI negotiations, the article was not to "be construed as providing formal or final administration positions on specific outstanding issues"). In testimony before Congress, Larson reiterated that

the U.S. delegation has argued that the provision of this proposed agreement simply cannot interfere with normal, non-discriminatory regulatory activities

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A review of the international cases described above shows that environmental regulations should be among those legitimate regulations that do not normally give rise to an obligation to compensate for devaluation of property. International tribunals have recognized a range of government regulations as legitimate exercise of the police power that do not require compensation. These include tax regulations, regulations governing the transfer and exchange of currency, licensing fees for the production of alcoholic beverages, restrictions to protect wine production, and export restrictions.²⁷¹ Given the undeniable impact of human activities on environmental health, and the equally obvious relationship between environmental health and human welfare, it is clear that regulations to protect the environment are at least as legitimate as regulations to address any of these other governmental concerns.

Furthermore, the nature of environmental protection indicates that environmental regulations should be accorded particular protection from compensation claims. Such regulations are an important method of internalizing environmental costs, which is an essential component of environmental protection and "a general principle of international law."²⁷² As the OECD has explained, internalizing environmental costs depends in large part on requiring the *polluter* to "bear the expenses of carrying out [pollution prevention] measures decided by public authorities to ensure that the environment is in an acceptable state."²⁷³ Requiring the government to provide compensation for the economic impact of environmental regulations does exactly the opposite, shifting the cost of complying with environmental measures, and thereby the cost of environmental harm, onto the general public. Such a shift constitutes a significant obstacle to environmental protection. For these reasons, the

in such areas as health, safety and the environment. In particular, we want to ensure that the expropriation article of the MAI cannot be used inappropriately to challenge regulatory decisions.

Larson Testimony, *supra* note 15.

271. See *supra* notes 250-258.

272. International Convention on Oil Pollution Preparedness, Response and Cooperation, Nov. 30, 1990, pmbl., 30 I.L.M. 733, 735-736. See generally *supra* notes 11-12 and accompanying text.

273. OECD Guiding Principles, *supra* note 11, at par. 4.

polluter pays principle and the multitude of international agreements for the protection of the environment require that governments generally be free to implement environmental regulations without having to pay to do so.

Environmental measures also have special legitimacy in the NAFTA regime. Under international law, treaty provisions are to be interpreted in light of their context.²⁷⁴ The context of the NAFTA expropriation provisions includes the strong emphasis that both NAFTA and NAAEC give to environmental protection. Both agreements strongly promote preserving the right of each government to protect the environment, ensuring that governments maintain and enforce environmental measures, and facilitating the strengthening of laws and regulations to protect the environment.²⁷⁵ In the context of NAFTA, therefore, environmental measures are legitimate and the expropriation provision should not be interpreted to interfere with the ability of governments to implement such measures.

In addition, NAFTA's investment provisions themselves specifically address environmental protection. Those provisions discourage countries from waiving or derogating from environmental measures to attract or retain foreign investment,²⁷⁶ and protect the right of each government to adopt, maintain or enforce measures that it considers "appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns."²⁷⁷ Requiring compensation for the economic impact of environmental regulations conflicts with these provisions by making it costly for governments to enforce or strengthen existing environmental measures or to adopt new ones.

274. According to the Vienna Convention on the Law of Treaties, *supra* note 267, art. 31, the terms of a treaty are to be interpreted "in their context," which includes "any agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty." The NAAEC thus constitutes part of the context in which NAFTA terms are to be interpreted. If a global investment agreement were to be based on the MAI Negotiating Text, the same context of environmental protection would apply there. *See supra* notes 66-68 and accompanying text.

275. *See supra* note 241-266 and accompanying text.

276. NAFTA, *supra* note 25, art. 1114.2.

277. *See supra* note 47 and accompanying text.

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For all these reasons, there can be no doubt that environmental regulations are a legitimate exercise of governmental power that should not normally give rise to a government obligation to compensate for resulting economic losses. Moreover, to require compensation would be inconsistent with generally accepted international law concerning environmental protection, as well as with NAFTA's particular concern that its provisions not interfere with the ability of governments to protect the environment.

Ethyl Corporation's expropriation claim raised a different legitimacy issue. Ethyl based its claim in part on an argument that Canada's ban was not really an environmental measure. Ethyl argued that "[t]he lack of any clear scientific evidence throws into doubt whether [the Canadian MMT measure] is necessary to protect human life or health,"²⁷⁸ and claimed that the measure was unjustified "since there is no consensus of scientific opinion on the effects of MMT."²⁷⁹ Similar arguments may be expected in support of other NAFTA expropriation claims. Such challenges to the scientific basis for an environmental measure raise important issues that directly affect the right and ability of governments to protect against the risk of environmental harm.

When a government promotes a measure as protecting against a risk to the environment, it is reasonable to require that the risk be real, not simply a disguise for a measure intended to achieve another purpose such as expropriation or protecting domestic production. This is the scheme established by the general exceptions to NAFTA and GATT,²⁸⁰ which recognizes that certain concerns are important enough to justify in-

278. Notice of Arbitration, *supra* note 107, at 14. Ethyl based its claim in large part on its characterization of the Canadian ban as a performance requirement. See *supra* note 111 and accompanying text. Although it is beyond the scope of this article to analyze this characterization, that argument appears to strain the language of the performance requirement provision. Ethyl's claim may have been motivated by a desire to avoid the general exceptions to the NAFTA, which permit measures "related to" the conservation of exhaustible natural resources, by applying the exceptions to the performance requirement provision, which limit the exception to measures "necessary for" such conservation. See *supra* notes 126-127 and accompanying text.

279. Notice of Arbitration, *supra* note 107, at 14.

280. See *supra* note 50.

terfering with the free flow of trade, as long as they are not really a disguise for measures intended to achieve illegitimate goals, such as protecting domestic industry. To distinguish between legitimate environmental measures and disguised illegitimate measures, it is reasonable to require that the existence of the risk to the environment be scientifically supported. It is essential, however, that the need for scientific support not become a requirement that the government demonstrate that its measure is supported by "most," "best" or "most widely accepted" scientific evidence. Such a requirement is contrary to the precautionary principle and inconsistent with the nature of science. More importantly, it would seriously interfere with the ability of governments to protect against risks of environmental harm.

Any regime that truly allows for protection against the risk of environmental harm must recognize the precautionary principle, which is based on the premise that science does not always provide the information or insights necessary to take protective action effectively or in a timely manner, and that undesirable and potentially irreversible effects may result if action is not taken until science does provide such insights.²⁸¹ Pursu-

281. The precautionary principle is included in the Rio Declaration on Environment and Development, which is explicitly reaffirmed in NAFTA's preamble. NAFTA, *supra* note 25, at 297. The Rio Declaration provides the following definition of the principle:

Where there are threats of serious or irreversible damage, lack of full scientific certainty shall not be used as a reason for postponing cost-effective measures to prevent environmental degradation.

Rio Declaration, *supra* note 12, princ. 15. Other agreements recognizing the principle include the Convention on Biological Diversity, June 5, 1992, pmbl., 30 I.L.M. 818; the *Framework Convention on Climate Change*, U.N. Doc. A/AC.237/18 (Part II)/Add.1 (1992), 31 I.L.M. 849 ("The Parties should take precautionary measures to anticipate, prevent or minimize the causes of climate change and mitigate its adverse effects. Where there are threats of serious or irreversible damage, lack of full scientific certainty should not be used as a reason for postponing such measures"); the *Ministerial Declaration of the Second World Climate Conference*, Nov. 7, 1990, 1 Y.B. INT'L ENVTL. L. 473 (1990) (ministers and representatives of 137 countries agree to "protect the ozone layer by taking precautionary measures to control ... emission of substances that deplete it"); the *Second International Conference on the Protection of the North Sea, Ministerial Declaration 1* (1987) (ministers of the EEC and eight countries agree that the North Sea ecosystem should be protected through the reduction of pollution "even where there is no scientific evidence to prove a causal link between emissions and effects ('the principle of precautionary action')"); and the *World Charter for Nature*, G.A. Res. 37/7, U.N. GAOR, 37th Sess., Supp. No. 51, U.N. Doc. A/Res/37/7 (1982), 22

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ant to this principle, countries have the right to regulate activities that may be harmful to the environment even if the scientific evidence concerning the connection between the activity and the harm is inadequate or inconclusive—that is, even if scientists do not agree or cannot explain exactly whether, how or to what degree the harm is caused.²⁸² This principle has been part of domestic and international law for several decades and has become a “broadly accepted basis for international action.”²⁸³

The precautionary principle does not ignore science or remove scientific inquiry from the effort to identify legitimate governmental measures. However, the principle reflects a rec-

I.L.M. 455 (1983) (“Activities which are likely to pose a significant risk to nature shall be preceded by an exhaustive examination; their proponents shall demonstrate that expected benefits outweigh potential damage to nature, and where potential adverse effects are not fully understood, the activities should not proceed.”). See also E. Hey, *The Precautionary Principle in Environmental Policy and Law: Institutionalizing Caution*, 4 GEO. INT’L ENVTL. L. REV. 303, 308-09 (1992).

282. In understanding the importance of the precautionary principle, it is helpful to remember that the fact that scientific evidence is not conclusive does not mean that it is not probative. For example, human health regulations have long been based on studies exposing animals to high doses of potentially harmful substances, even when there was no conclusive evidence that the regulated substances cause the same harm in humans that they do in animals. These regulations are based on the reasonable assumption that effects on animals are probative evidence—not conclusive proof—of potential effects in humans. See NATIONAL CANCER INSTITUTE, EVERYTHING DOESN’T CAUSE CANCER (NIH Pub. No. 90-2039, March, 1990) (“Of the several hundred ... chemicals that cause cancer in animals, however, it is not known how many are also human carcinogens. Nevertheless, materials that cause cancer in one type of animal usually are found to cause cancer in others.... For these and other reasons, we should expect animal carcinogens to be capable of causing cancer in humans.”). Likewise, studies showing harm at high doses are at least evidence of the possibility of—or potential for—harm at low doses. Although they may not prove that harm will occur, they support the conclusion that there is a risk.

283. Philippe Sands, *The Greening of International Law: Emerging Principles and Rules*, 1 GLOBAL LEGAL STUDIES J. 293, 301 (1994). See also PHILIPPE SANDS, PRINCIPLES OF INTERNATIONAL ENVIRONMENTAL LAW 208-12 (1995) (precautionary principle has received widespread support; a “good argument” can be made that it reflects customary international law); INTERPRETING THE PRECAUTIONARY PRINCIPLE 262 (Tim O’Riordan & James Cameron eds., 1994). In his dissenting opinion in the 1995 French nuclear testing case, Judge Weeramantry of the International Court of Justice noted the importance of the precautionary principle in light of the irreversibility of some environmental damage and stated that the precautionary principle is gaining increasing support as part of the international law of the environment. Request for an Examination of the Situation in Accordance With Paragraph 63 of the Court’s Judgment of 20 December 1974 in the Nuclear Tests (New Zealand v. France) Case, 1995 ICJ Reports 288, 342 (Weeramantry, J., dissenting).

ognition that scientific certainty is rare and that advancements in scientific knowledge—including knowledge of previously unknown risks—nearly always begin as controversial theories held by a minority of the scientific community. If governments must base environmental measures on the scientific conclusions accepted as “best” by the majority of scientists or supported by the “weight” of available scientific evidence, they will be unable to take precautionary measures to protect against risks suggested by new, and frequently controversial, evidence.

The NAAEC recognizes the right of each Party “to establish its own levels of domestic [environmental] protection”²⁸⁴ and the importance of achieving “enhanced levels of environmental protection.”²⁸⁵ Determining the appropriate level of protection in the face of a given risk is a fundamentally political decision that only a government that is accountable to those affected by the decision can make legitimately. When a nation identifies a potential risk to health or the environment, it must decide whether and to what extent to take steps to protect against that risk. While science plays an important role in identifying the existence of a risk, the decision concerning the appropriate response to that risk also requires political decisions such as weighing how much the citizens of the country fear the particular risk and how much, if at all, they value the benefits that the risky activity provides. This balancing of potentially competing concerns goes to the heart of what governments do — determine appropriate actions based on the fears and values of citizens.

Similarly, the ability to enhance environmental protection is meaningless unless governments are permitted a full range of responses to legitimate environmental risks. Such responses must include the right to impose stricter standards to prevent harm that is certain to occur, as well as the right to implement

284. NAAEC, *supra* note 51, art. 3.

285. *Id.* pmb1.

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measures to protect against possible risks revealed by new or controversial scientific evidence.²⁸⁶

For these reasons, governments implementing an environmental measure must retain the ability to make judgments concerning conflicting evidence or different scientific principles, as well as how and when to respond to a legitimate environmental risk. It is therefore inappropriate for an outside body that is not accountable to a country's residents, such as an arbitral tribunal, to attempt to weigh competing scientific claims to determine whether there is "enough" risk to justify the measure in question, or whether the measure is supported by the "correct" or "best" or "most accepted" science.

In light of these considerations, therefore, an arbitral tribunal considering an expropriation claim arising out of a purported environmental measure should limit its inquiry to determining whether the science underlying the risk determination has the minimal attributes of scientific inquiry — that is, whether the evidence of risk has been derived through the application of legitimate scientific methods and procedures, and is probative of a potential for adverse effects.²⁸⁷ This is true even if the evidence is controversial or inconclusive. Once an arbitral tribunal has confirmed that the evidence is scientific and

286. This point can be illustrated by the following example. Suppose two people are preparing to leave their homes to go to the office in the morning and each checks several weather forecasts before doing so to determine whether to take precautions against getting wet from rain. Assume further that these people are seeking to achieve different levels of protection: one is willing to suffer a little wetness but would prefer not to get extremely wet; the other considers it extremely important to avoid getting wet (*i.e.*, has chosen a higher level of protection). Four out of five forecasts indicate that it is most likely not going to rain during the day, but the fifth, using a new and controversial forecasting method, indicates that it is likely to rain. The person who is willing to get a little wet is likely to take fewer precautions against rain on the chance that the new forecasting method is not as reliable as the method used by the other four forecasts. The person with the higher level of protection is more likely to consider the possibility that the new method may be accurate and take precautions against rain. Forcing the second person to act on the basis of the majority of the evidence effectively lowers the level of protection that she is permitted to choose.

That is not to say, however, that science has no role in this scenario. To be a legitimate basis for protective measures, the new forecasting method must be based on a minimally scientific inquiry concerning the weather, instead of on unscientific methods, such as astrological predictions.

287. This is an appropriate role for the expert assistance NAFTA makes available to arbitral tribunals. NAFTA, *supra* note 25, art. 1133.

probative, it should accept the legitimate environmental basis for the measure. Such an analysis will ensure that environmental measures are not disguised expropriations or protectionist measures without interfering with the ability of governments to take precautionary measures or their right to apply the political judgments inherent in setting their appropriate levels of protection against risk.²⁸⁸

The SD Myers claim raises a different issue concerning the legitimacy of environmental measures. The Canadian PCB export ban was based on Canada's obligations under the Basel Convention.²⁸⁹ The Basel Convention forms part of the international law that applies in interpreting NAFTA's expropriation provisions.²⁹⁰ Environmental measures addressing risks recognized in a widely adopted international agreement shall be presumed to be legitimate and should not normally give rise to an obligation to compensate for their economic impact on investment. Moreover, requiring governments to pay compensation to implement such measures interferes with efforts to address global environmental problems through international consensus.

International law thus recognizes the right of governments to regulate to promote legitimate governmental objectives

288. These principles would support the right of the governments of Canada and Mexico to maintain the measures at issue in the Ethyl and Metalclad cases. Scientific studies have apparently shown that airborne manganese poses a risk to human health. *See supra* notes 109 and 133. If these studies are the result of the application of legitimate scientific methods, they should be sufficient to support the environmental legitimacy of Canada's ban. Likewise, the study indicating that operation of Metalclad's waste facility poses a risk to human health and the environment (again assuming that the study is legitimately scientific) weighs against Metalclad's compensation claim. Even the existence of scientific studies to the contrary should not prohibit the government from taking precautionary measures to protect these serious interests.

289. *See supra* notes 142-144.

290. Article 104 of NAFTA provides that the obligations of several international environmental agreements are to prevail over any inconsistent obligations in NAFTA. These agreements are the Basel Convention; the Convention on International Trade in Endangered Species (CITES); the Montreal Protocol on Substances that Deplete the Ozone Layer; the Agreement Between the Government of Canada and the Government of the United States Concerning the Transboundary Movement of Hazardous Waste; and the Agreement Between the United States and Mexico on Cooperation for the protection and Improvement of the Environment in the Border Area. NAFTA, *supra* note 25, art. 104.

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without incurring an obligation to provide compensation for every impact of those regulations on the value of property.²⁹¹ The discussion of international law in Section V also indicates that international tribunals have recognized additional factors that support governments' right to regulate without having to provide compensation.

The most important such factor is the degree to which the regulation affects the value of the investment.²⁹² As noted above, international law considers an indirect expropriation to require compensation if it renders property "virtually valueless."²⁹³ In other words, as Ethyl explained in its NAFTA claim, international law requires compensation "where the effect [of the regulation] is similar to what might have occurred under an outright expropriation."²⁹⁴ Thus, a regulation is not "tantamount to expropriation" if it leaves some value in the investment in question.²⁹⁵

291. See *supra* Part V.

292. See *supra* notes 255 - 263 and accompanying text.

293. See *supra* note 256 and accompanying text. This criterion is supported by the statement of the Iran-US Claims Tribunal quoted by Ethyl in its Notice of Arbitration: "[M]easures taken by a State can interfere with property rights to such an extent that these rights are rendered so useless that they must be deemed to have been expropriated." Notice of Arbitrations, *supra* note 107, at 10 (quoting *Starrett Housing Corp.*, 4 Iran-US Cl. Trib. Rep. at 154) (emphasis added)).

294. See *supra* notes 116-117 and accompanying text.

295. This factor is relevant to the claims of both Metalclad and Ethyl. It does not appear that Metalclad is asserting that the government actually took its property, but rather that the refusal of the operating permit and the environmental zoning regulation affected the economic value of the waste treatment facility. Likewise, Ethyl admits that the sale of MMT constitutes only half the revenue of Ethyl Canada. See *supra* note 112. Canada's law thus did not deprive Ethyl of all economic benefit of its investment. Therefore, even under Ethyl's own interpretation of international law, Ethyl's claim was unsupported.

Ethyl attempted to strengthen its claim by arguing that the loss of 50% of its revenues would cause the parent corporation to reevaluate whether to continue operations in Canada. See *supra* note 113. International tribunals have long recognized that this fact is completely irrelevant to the compensation determination. See, e.g., *Kugele*, 6 Ann. Dig. At 69. Ethyl also padded its claim with allegations of negative effects on its "worldwide sales." This approach hugely multiplies the disincentive to achieving the goals of strengthening environmental protection. Claims like Ethyl's would make governments unwilling ever to take measures to protect against newly-identified risks, because to do so would make them potentially liable for harm to sales and reputation in any country that has not already implemented measures. This is clearly inconsistent with the goals of NAFTA to maintain and strengthen environmentally protective measures. See *supra* notes 46-54 and accompanying text.

Another factor that is relevant under international law is whether regulations affecting the investment were foreseeable.²⁹⁶ This factor weighs against requiring compensation in the case of most environmental laws, including those at issue in the NAFTA cases described above.²⁹⁷ Harm to the environment is universally recognized as an extremely serious issue and, as such, is a common subject of government regulation. NAFTA's emphasis on maintaining and strengthening environmental protection gives notice of the three governments' intention to implement environmental measures. It can hardly be considered a surprise when they do so.

VII. CONCLUSION

The NAFTA claims described in this Article demonstrate the need for clarification of the NAFTA expropriation provision as it applies to environmental measures. International law has long supported the right of governments to implement legitimate measures in the exercise of their police powers without incurring an obligation to compensate if such measures diminish the value of foreign investments. General principles of environmental law and protection, as well as the specific emphasis that NAFTA places on environmental protection, make clear that this right applies with particular force with respect to legitimate regulations protecting the environment. For these reasons, the parties to NAFTA and negotiators of other regional or global investment agreements should make explicitly clear that protection against expropriation does not include a right to compensation for diminished value resulting from the effects of legitimate environmental regulations.

296. See *supra* notes 264-266 and accompanying text.

297. When Metalclad undertook to upgrade and operate the hazardous waste facility, it was well aware that its activities were subject to regulation. In addition to being aware that its activities were subject to regulation in Mexico, see *supra* note 93 and accompanying text, Metalclad should have been aware that similar activities are regulated in the United States. Nor can Ethyl claim surprise that the government promulgated new regulations concerning the production and sale of gasoline additives, because these activities have long been the subject of government regulation, both in Canada and the United States. The long-standing laws regulating PCB use and disposal in both the United States and Canada, as well as the existence of the Basel Convention, gave SD Myers ample notice that its activities were subject to regulation.

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To truly enable governments to protect the environment, it is essential to make explicit the following points:

- Legitimate environmental measures do not create a right to compensation for any decrease in the value of a foreign investment affected by the measures
- Legitimate environmental measures include measures implemented pursuant to the precautionary principle
- Governments must have the right to establish their own level of protection against risks of environmental harm
- Any test of the legitimacy of environmental measures must not require the government to prove that a risk of harm is supported by the “best,” “most” or “most widely accepted” science; it is sufficient if the application of legitimate scientific methods and procedures demonstrates a potential for adverse environmental effects.

Creating a right to compensation for an environmental law’s economic impacts on foreign investors would severely chill the ability of governments to protect the environment. Such a regime would be akin to a legally enforced protection racket—the government would be forced to pay those who would harm the environment to stop or limit their harmful activities.

Fortunately, international law does not support such a scheme. Rather, it recognizes that legitimate governmental regulations do not normally give rise to a right to compensation, and that environmental protection is an important subject of government action, even when foreign investors must bear an economic burden as a result of that action. It is crucial that governments negotiating new trade or investment agreements recognize these principles and explicitly ensure that such agreements do not create new obstacles to the ability of governments to protect the environment through legitimate environmental laws and regulations.