

HOUSE OF COMMONS STANDING COMMITTEE ON INTERNATIONAL TRADE

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Thank you Mr Chairman, members of the Committee, for the invitation to speak to you today on the Canada-EU Comprehensive Economic and Trade Agreement. This is a major trade and investment treaty initiative that, if completed, will have important implications for all governments in Canada and for the Canadian public.

I will speak today only to the Chapter on Investment, not because the rest is not important, but simply because that is where my expertise lies, based on 15 years of experience in the area and having worked with over 75 governments on investment treaty-related issues.

Unfortunately, official texts have not been released, just summaries by the Canadian Government and the EU Commission. However, as I indicated in my letter accepting the invitation to speak that I will do the best I can based on the summaries and on leaked texts that have been circulating from time to time. Of course it would be much better if we could all have a fully informed, transparent discussion based on the full draft text rather than having to rely on leaks and self-selected summaries by each government. Details matter, and they are largely absent from the summaries. We look forward to being able to have such a discussion before the treaty is finalized.

In the meantime, one such leaked text began circulating last week and I received it a couple of days ago, of course in English only, the language of the negotiations. It closely parallels the previous leaks that have been confirmed as valid documents, and reflects text agreed, and sometimes not agreed on, to mid November. Consequently, I will speak to this text as well as the others.

The final written submissions will address six technical issues. But I will give my conclusion first: **In my opinion, the Investment Chapter, if it continues on what appears to be its present course, will provide foreign investors into Canada with the most investor-friendly set of corporate rights ever drafted by the Canadian government into a treaty.**

The consequence of this increase in investor rights coupled with a robust investor-

to-state dispute settlement mechanism under the agreement will be a growing substantive scope for many more investors to challenge more government measures based on higher levels of corporate rights, including future human health and environmental measures at the federal and provincial levels.

I say foreign investors here, and not just European investors because all foreign investors in Canada with coverage of any investment treaty will be able to benefit from the new agreement due to the Most Favoured Nation (MFN) provision in those other treaties. So this is a big deal Mr. Chairman, a very big deal in my view.

Each point discussed below is then followed by the current draft text of the Investment Chapter as of November 2013, based on the leaked document.

### **Point 1: The MFN provision in this draft agreement is fully open and backward looking**

A Most Favoured Nation (MFN) provision under investment law allows an investor into Canada to have the same level of rights as the highest level of rights any investor in Canada has. The current draft text is fully open so that the provisions of prior investment treaties concluded by Canada can be adopted by foreign investors under this treaty in the event of any disputes.

The present draft CETA text provides carefully worded language on many provisions. In several cases this is designed to limit the potential scope of interpretation of the rights of investors and thus protect government regulatory space, the right to regulate.

However, the MFN provision allows investors to reach back in time to use provisions in older treaties that were not so carefully drafted. This wipes out the benefit of the new drafting by giving the investor the right to apply the older provisions in any arbitrations against the government.

Mr. Chairman, it is worth noting that this ability to reach back into older texts was precluded by language in the 2004 Canadian Model FIPPA that allowed the MFN provision to apply only on a forward looking basis, not backwards in time, precisely to prevent the undoing of the more modern language in the Model FIPPA on the substantive obligations of the government. The present draft text quite precisely reverses the 2004 Model FIPPA in this very important way and allows investors to cherry pick the highest level of rights from all the treaties in effect at the time of a dispute.

**Reference Article of 21 November draft Investment text:**  
***Article X.8: Most-Favoured-Nation Treatment***

*4. For greater certainty, the “treatment” referred to in Paragraph 1 and 2 does not include investor-to-state dispute settlement procedures provided for in other international investment treaties and other trade agreements.*

## **Point 2: The Fair and Equitable Treatment provision will become the most open ever concluded**

Experience with the over 600 investor-state arbitrations under investment treaties shows that the fair and equitable treatment (FET) provision is the most frequently, and the most successfully, used provision by investors. So it is a truly important provision.

It was noted earlier that several of the more carefully drafted provisions are designed to protect government regulatory space. The draft of this crucial article, however, appears designed to do the opposite, to broaden the rights of investors and create more uncertainty as to the scope of government regulatory space. The current text is the most open-ended text a Canadian government will have ever drafted if concluded as it now appears to stand. This is because the text comes in three main parts. Lets call them boxes here.

The first box has a defined list of factors that would constitute a breach of the provision by a state. This is fine. The list generally reflects the issues most analysts would associate with the concept of FET under international law. It is what most would have looked to, and it is defined and limited.

The second box is actually in paragraph 5, and addresses a specific concept called the legitimate expectations of the investor. It too has been widely referred to before, and it too is specifically defined and limited here. These two boxes together have generally been seen as the total scope of FET in most cases.

But the third box is defined to exist “in addition” to these first two. This third box refers to what customary international law says constitutes a breach of FET, other than or in addition to what is in the other two boxes. However, it does not set any scope for this, it does not set any thresholds relating to the degree of government misconduct (significant, serious, egregious), or the tests to apply in terms of how to determine whether an asserted type of government act is actually part of customary international law. The problem is all of these questions are subject to very much contradictory rulings in existing arbitral decisions. The text gives no guidance which direction to go in or which arbitral decisions to follow, other than saying it exists and it is for the Tribunals to set the tests for deciding what goes in it, and the size of the box.

Because the first list combined with the concept of legitimate expectations was seen by many as the proper scope of FET, this approach rejects that oft-held view and says no, the list and legitimate expectations is not the full scope but we are not saying what the full scope is: you the lawyers go figure out what it is in arbitrations. It is a high risk, open invitation to the international arbitration lawyers, investors and tribunals (composed of the same lawyers for the most part) to figure it out, instead of the governments clarifying what they mean. This makes it the most incalculable provision on FET I have seen in the last ten years of modern drafting of the provision. In sum, on the single most used provision in investment arbitrations, the text now is decidedly unpredictable for governments.

**Reference Article of 21 November draft Investment text:**

**Article X.9: Treatment of Investors and of Covered Investments**

1. Each Party shall accord in its territory to investors and to covered investments of the other Party fair and equitable treatment and full protection and security in accordance with paragraphs 2 to 7.

2. A Party breaches the obligation of fair and equitable treatment referenced in paragraph 1 where a measure or series of measures constitutes:

a. Denial of justice in criminal, civil or administrative proceedings;

b. Fundamental breach of due process, including a fundamental breach of transparency, in judicial and administrative proceedings.

c. Manifest arbitrariness;

d. Targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief;

e. Abusive treatment of investors, such as coercion, duress and harassment; or

f. A breach of any further elements of the fair and equitable treatment obligation adopted by the Parties in accordance with paragraph 4 of this Article.

3. In addition to paragraph 2, a breach of fair and equitable treatment may also arise from any other treatment of covered investments or investors which is contrary to the fair and equitable treatment obligation recognized in the general practice of States accepted as law.

4. In accordance with X [*exact reference to be determined regarding the procedure*], the Parties shall every X years [*or regularly*], or upon request of a Party, review the content of the obligation to provide fair and equitable treatment.

5. When applying the above fair and equitable treatment obligation, a tribunal may take into account whether a Party made a specific representation to an investor to induce a covered investment, that created a legitimate expectation, and upon which the investor relied in

deciding to make or maintain the covered investment, but that the Party subsequently frustrated.

### **Point 3: Possible umbrella clause still on the table**

An umbrella clause is a clause that states simply, as the EU is proposing:

“Each Party shall observe any specific written obligation it has entered into with regard to an investor of the other Party or an investment of such an investor.”

(EU proposed language in the Reference text, Article 9 of 21 November draft Investment text)

It is short, but powerful: this provision would elevate every written undertaking or obligation by a government towards an investor to an international law undertaking or obligation, subject to review by an international tribunal.

It would allow an investor, at its sole discretion, to oust the role of the domestic courts in addressing disputes related to domestic law instruments in their proper context of Canadian law, and instead move the dispute to an international tribunal. This has been done in multiple other arbitrations to date.

Few if any existing Canadian treaties have this clause, but its inclusion now would make it available to all foreign investors in Canada covered by any treaty, again due to the MFN provisions in those treaties. It is a very powerful clause that transforms and potentially replaces the relationship between an investor and the domestic law of the state it operates in.

### **Point 4: The exceptions to national treatment are being made much more difficult to develop**

The inclusion of exceptions to National Treatment and MFN is a normal part of the drafting process. The NAFTA, for example, has over 100 pages of such exceptions. Under the CETA, these exceptions are to be done only by a complete listing of all the existing measures that do not conform to the obligations in the CETA, including at the provincial level. This reverses the practice of simply grandfathering all such provincial measures, a practice that started with the NAFTA in order to reduce the burden on the provinces. By now requiring a full listing of such non-conforming measures in each province and territory, CETA will place a very high burden on the provinces to comply with this. Any error, due to accompanying provisions in the text, are for all practical purposes irreversible, meaning that even a measure that exists when an investment was made can be challenged by an investor if the province leaves it out of its list by accident.

**Reference Article of 21 November draft Investment text:**

**Article X.14: Reservations and Exceptions**

1. Articles X- (National Treatment), X- (Most-Favoured-Nation Treatment), X- (Market Access), X- (Senior Management and Boards of Directors) and X- (Performance Requirements) do not apply to:

(a) an existing non-conforming measure that is maintained by:

(i) the European Union, as set out in its Schedule to Annex I;

(ii) a national government [of a Party], as set out in its Schedule to Annex I;

(iii) a provincial, territorial, or regional government [of a Party], as set out in its Schedule to Annex I; or

(iv) a local government of a Party.

(b) the continuation or prompt renewal of any non-conforming measure referred to in subparagraph (a); or

(c) an amendment to any non-conforming measure referred to in subparagraph (a) to the extent that the amendment does not decrease the conformity of the measure, as it existed immediately before the amendment, with Articles X- (National Treatment), X- (Most-Favoured-Nation Treatment), X- (Market Access), X- (Senior Management and Boards of Directors) and X- (Performance Requirements).

2. Articles X- (National Treatment), X- (Most-Favoured-Nation Treatment), X- (Market Access), X- (Senior Management and Board of Directors) and X- (Performance Requirements) do not apply to measures that a Party adopts or maintains with respect to sectors, subsectors or activities, as set out in its Schedule to Annex II.

**Point 5: Art. XX type Exceptions clause does not save any of this**

Several government have argued that regulatory space is protected by including a more broadly worded general exception for certain type of government measures relating to the environment and human health. However, in my view, the presence of such a general exception clause, which is along the lines of the well known Art. XX of the GATT, does not save any of the above problems. Instead, it imports a strict test of necessity from the WTO, a text that has always been interpreted very restrictively against governments. Moreover, the WTO necessity test applies in the context of traded products, which is very different than the context of how products are made of services delivered. It also allows three arbitrators to decide what is necessary for, in this case Canada or a province, if Canada ever seeks to use this exception, with no appeal possible of their decision as there would be in the WTO Appellate Body process.

There is no history of the use of this type of exception in the very different context of investment as opposed to trade law, and no obvious pathway fro how it might be used. Rather, it reflects an assumption that what is good for trade law will work in investment law. In my view it is a misappropriation from the regulation of trade in

goods to the regulation of investments, which are two very different things in nature and scope.

**Reference Article of 21 November draft Investment text:**

**Article X: General exceptions**

1. For purpose of the Investment Chapter:

(a) a Party may adopt or enforce a measure necessary:

(i) [EU: to protect public security or public morals or to maintain public order<sup>2</sup>];

(ii) to protect human, animal or plant life or health,

(iii) to ensure compliance with domestic law that is not inconsistent with this Agreement, [EU: including those relating to:

a) the prevention of deceptive and fraudulent practices or to deal with the effects of a default on contracts;

b) the protection of the privacy of individuals in relation to the processing and dissemination of personal data and the protection of confidentiality of individual records and accounts;

c) safety];

(iv) [EU: to protect national treasures of artistic, historic or archaeological value];

(v) for the conservation of living or non-living exhaustible natural resources, [EU: if such measures are applied in conjunction with restrictions on domestic investors];

or

[EU: (vi) inconsistent with Articles 3 (National Treatment) and 4 (Most-Favoured-Nation Treatment), provided that the difference in treatment is aimed at ensuring the effective or equitable imposition or collection of direct taxes in respect of economic activities, investors or services suppliers of the other Party.]

*[Parties to check for the need of paragraph (vi) in relation to coverage in the Article on Taxation.]*

(b) provided that the measure referred to in subparagraph (a) is not:

(i) applied in a manner that constitutes arbitrary or unjustifiable discrimination between investments or between investors [EU: where like conditions prevail], or

(ii) a disguised restriction on international [CAN: trade] or investment.

<sup>2</sup> The public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society

**Point 6. The right to regulate clause clearly restricts the right to regulate, it does not expand it**

The right to regulate clause is also often referred to as showing the sensitivity of the investment chapter to the needs of government. Here, it is intended to be in the preamble to the whole of the CETA, and is not in the Investment chapter per se.

The government's technical summary tells us that the agreed language is that it will indeed reaffirm the parties' right to regulate, but "***in a manner consistent with the Agreement.***"

This is the language from NAFTA Article 1114(1) and means, as a matter of settled law, that the agreement prevails over the right to regulate, and all exercises of the right to regulate, at both the federal and provincial levels, must conform to the agreement. Contrary to what is often implied by referring to a right to regulate provision, it in fact prioritizes conformity with the treaty obligations over the right to regulate. This is absolutely beyond legal doubt, as seen in the history of the NAFTA itself.

**Reference texts:**

**- TECHNICAL SUMMARY OF FINAL NEGOTIATED OUTCOMES**

**Preamble**

Sets out a number of aspirational (non-binding) statements for CETA, including statements

- reaffirming the parties' right to regulate (in a manner consistent with the Agreement)

**- NAFTA: Article 1114: Environmental Measures**

1. Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure 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.

**Conclusions**

Given all this Mr. Chairman, as a matter of law based on the summaries and known legal texts, it is my view that the CETA as currently worded and explained:

1. will give foreign investors into Canada more international law rights than ever before, and in a more open-ended way than ever before;
2. will do so quite knowingly and deliberately; and
3. that this will inevitably lead to increases in the number of arbitrations against Canada, for both federal and provincial measures, with resulting pressures not to regulate in key areas such as the environment, human health, anti-tobacco practices, etc.