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I. INTRODUCTION

Chapter 11 of the North American Free Trade Agreement (NAFTA) benignly named the "Investment Chapter," is a theater for some of the most advanced issues of 21st century international law and adjudication. The Chapter gives private parties the right to challenge national policies that burden their ability to do business freely.[1] It empowers arbitral tribunals to assess damages against the governments of NAFTA parties. The adjudicators, as this Article illustrates, render opinions with a constitutional flavor in that they assess the validity of domestic norms against larger principles of international economic law.[2] In a drastic move away from classical century international law that is reminiscent of the system of judicial remedies ushered into the European Union,[3] the Investment Chapter binds governments by empowering panels to render damage awards against national governments that are enforceable in national courts.

As is the case with the World Trade Organization (WTO), we are witnessing in the scholarship and popular commentary the formation of a familiar divide between competing claims that advance the core arguments for or against Chapter 11 but, although sophisticated and nuanced, tend not

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[1] *See* North American Free Trade Agreement, Dec. 8-17, 1992, U.S.-Can.-Mex., ch. 11, 32 I.L.M. 605, 639 (1992) [hereinafter NAFTA].

[2] *See id*; *see also infra* note 18 and accompanying text.

[3] *See* Weiler, *infra*, note 18; NAFTA's Investment Chapter *infra* note 27.

to have much common ground.[4] Familiar voices from affiliates of what may be termed the anti-globalization movement rail against NAFTA's Chapter 11. These voices argue that neoclassical economic principles are now embodied in a dangerous and powerful legal weapon.[5] Unlike the WTO, which at least has the ability to confine itself to state-to-state disputes, they argue, the Investment Chapter allows private business interests to challenge health, labor, taxation, procurement, and other policies that are mainstays of democratic lawmaking in the democratic nation-state as we know it.[6] These self-interested economic forces, critics fear, may find a sympathetic ear in international NAFTA panels which may favor *laissez faire* norms that tend to facilitate the cross-border flow of capital.[7] In turn, the critics also argue that these NAFTA panels lack the hallmarks of legitimacy that characterize courts in our modern democracies.[8] They claim that decisions need not be justified, appeals are not allowed except on highly limited grounds, the process lacks transparency, and yet NAFTA panels have the power to invalidate democratically adopted rules.[9] Those suspicious of Chapter 11, then, claim that at a minimum the Treaty is fundamentally flawed because it gives individuals the right to extract from national governments payment for damages arising out of a breach of international economic law, thereby creating the functional equivalent of judicial review of domestic law under ambiguous international norms applied by illegitimate tribunals.

In response, supporters of Chapter 11 argue that the cross-border creation of capital and economic opportunity is essential to international economic development.[10] They assert that the free flow of cross-border investment is conditioned on the presence of antidiscrimination jurisprudence and a modicum of protection that approximates standards in the investor's home jurisdiction.[11] By accomplishing this goal, Chapter 11

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[4] *Compare* Guillermo Aguilar Alvarez & William W. Park, *The New Face of Investment Arbitration: NAFTA Chapter 11*, 28 YALE J. INT'L L. 365 (2003), *and* Charles H. Brower, II, *NAFTA's Investment Chapter: Initial Thoughts About Second-Generation Rights*, 36 VAND. J. TRANSNAT'L L. 1533 (2003), *with* PUBLIC CITIZEN, NAFTA CHAPTER 11 INVESTOR-TO-STATE CASES: BANKRUPTING DEMOCRACY (Sept. 2001), *available at* http://www.citizen.org/documents/ACF186.PDF (last visited Jan. 5, 2005).

[5] *See, e.g.*, PUBLIC CITIZEN, *supra* note 4.

[6] *Id.*

[7] *Id.*

[8] *See, e.g., NAFTA's Powerful Little Secret; Obscure Tribunals Settle Disputes, but Go Too Far, Critics Say*, N.Y. TIMES, Mar. 11, 2001, *available at* 2001 WLNR 3421720.

[9] *Id.*

[10] Alvarez & Park, *supra* note 4.

[11] Since the 1980's, there has been an astonishing increase in the number of bilateral or trilateral investment treaties. It is unclear whether these treaties are merely symbolic, *i.e.* signaling a country's philosophical approach toward foreign investment, or true facilitators of foreign direct investment. Regardless of the answer to this empirical question, the

clears the way for a freer flow of capital across borders, which will channel benefits to the host economies even if their ability to regulate the allocation of those benefits is somewhat limited by international norms.[12] In other words, treaties such as Chapter 11 arguably protect less developed countries from their own misplaced protectionist urges, much like good governance principles enshrined in the WTO norms tend to prevent domestic interests from imposing self-destructive protective barriers to trade.[13] As further explained below, the core provisions of Chapter 11 prevent the host jurisdiction from imposing measures traditionally followed in developing countries. Thus, the international law embodied in NAFTA establishes minimum levels of protection against takings without compensation at fair market value, discriminatory treatment, and arbitrary government action, thereby clearing the way for the creation of capital and economic activity.[14] The argument concludes that the enforcement of these regulations in the NAFTA panels is necessary to protect against the risk that domestic judges will refuse to recognize the norms' validity.

In sum, proponents argue, the Chapter merely reflects international custom regarding the economic security for foreigners, and actually helps and promotes economic activity in developing countries. Furthermore, they argue the legitimacy challenge to the Treaty is not warranted. Who, then, is afraid of Chapter 11, and why?

Criticism of the Treaty spans the political, academic, lobbying and juridical spectrum.[15] The root cause of the crisis, I argue, is the combination of the ambiguity inherent in the Treaty, its potential to invalidate sensitive domestic norms if the ambiguous language of the Treaty is not properly interpreted, the power given to arbitrators to engage in the functional equivalent of judicial review of democratically enacted

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existence of over one thousand treaties, and the potential use of Chapter 11 as a model for the investment chapter of the Free Trade of the Areas Agreement, show that the answer to the questions raised by this Article are not merely academic. Kenneth J. Vandevelde, *The Economics of Bilateral Investment Treaties*, 41 HARV. INT'L L.J. 469, 469-470 (2000).

[12] *See* Charles N. Brower & John Tepe, *The Charter of Economic Rights and Duties of States: A Reflection or Rejection of International Law?* 9 INT'L LAW 295 (1975).

[13] *See* J.H.H. WEILER & SUNGJOON CHO, INTERNATIONAL AND REGIONAL TRADE LAW: THE LAW OF THE WORLD TRADE ORGANIZATION (2004) *available at* www.jeanmonnetprogram.org/wto/PDF-files/WTO_2004_UnitI.pdf (last visited Jan. 5, 2005). *See also* Brett Williams, *The Influence and Lack of Influence of Principles in the Negotiations for China's Access to the World Trade Organization,* 33 GEO. WASH. INT'L L. REV. 791, 839-40 (2001) (arguing that the WTO treaties not only regulate relations between states but also regulate relations between citizens within states and act as counterweights to groups that lobby the government to adopt policies that are inequitable and welfare decreasing).

[14] See *infra* notes 42 through 57.

[15] For a discussion of how the critics of Chapter 11 may be found across the American political, judicial, academic, and advocacy spectrum, *see, e.g.,* PUBLIC CITIZEN, *supra* note 4.

norms, and the classic conflict between *laissez faire* norms and domestic regulation that infuse the debate over Chapter 11. This conflict may rise to the level of an "existential crisis"—if interpreted too broadly without due regard for its context and objective, Chapter 11 may bring general claims for violations of international law within the ambit of private party dispute resolution.[16]

As the European integration experience has demonstrated, and as is addressed later in this Article, even if most domestic measures survive international scrutiny, the very possibility that an international tribunal might engage in "constitutional" review of domestic norms (forcing the defendant government to litigate) will create legitimacy concerns. Chapter 11, in turn, is a prime candidate for a severe crisis of legitimacy; it involves substantive norms that may be construed to override domestic law in several crucial areas, all the while establishing a "judicial-constitutional" system akin to that which obtains in Europe, but without the sophisticated judicial and institutional system of the European Union and the intricate dialogue between the various European actors.[17]

To resolve these concerns, I put forth in prior writings proposals for the interpretation of Chapter 11 within a common law framework, while articulating some broad norms that should guide NAFTA Chapter 11 panels when engaging in the review of the legality of validly enacted domestic norms under the aegis of supranational standards.[18] I defined a "spectrum of integration;" one that would establish doctrinal principles applicable to various free trade and other integrated areas, and provided parameters for the jurisprudential direction of these proposed common law trade tribunals.[19] I argued that we may understand Chapter 11, based on its place along the spectrum of integration, to incorporate two fundamental

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[16] Ari Afilalo, *Towards a Common Law of International Investment: How NAFTA Chapter 11 Panels Should Solve Their Legitimacy Crisis*, 17 GEO. INT'L ENVTL. L. REV. 51 (2004) [hereinafter Legitimacy Crisis].

[17] The classical exposition of the transformation of Europe from an aggregation of sovereign nation-states into an integrated area bearing constitutional hallmarks of a "Federation" or other unitary entity may be found in Joseph H.H. Weiler, *The Transformation of Europe, reprinted in* JOSEPH H.H. WEILER, THE CONSTITUTION OF EUROPE: "DO THE NEW CLOTHES HAVE AN EMPEROR? AND OTHER ESSAYS ON EUROPEAN INTEGRATION (Cambridge Univ. Press 1999). One of the important themes in the narrative recounted by Professor Weiler is the elimination of the Member States' ability to "selectively exit" the supranational system to protect their domestic interests. The removal of selective exit was a byproduct of the establishment of national courts empowered (and that proved willing) to apply European law and enforce it against their own governments. As I elaborate further in this Article, the removal of selective exit is also one of the features of the Investment Chapter of NAFTA.

[18] Legitimacy Crisis, *supra* note 16.

[19] *Id.*

principles: a ban on discrimination and a ban on arbitrary behavior.[20] I concluded that, if properly limited to focusing on rooting out these two kinds of prohibited conduct, the Chapter would achieve its intended goal without threatening domestic values.[21] If so interpreted, I believe, the Chapter 11 arbiters may stake a claim to place of distinction in international law and in the debate over constitutionalization: their work would breathe further life into the common law of international trade concept described by Professor Weiler, by developing and applying legal norms that, while borrowing from other areas of international trade law, would properly circumscribe NAFTA to its legitimate place in the spectrum of integration.[22]

In this article, I analyze two recent decisions of NAFTA Chapter 11 panels in cases that implicated highly sensitive domestic interests: *The Loewen Group and Raymond L. Loewen v. United States,* [23] and *Mondev International Ltd. v. United States*.[24] My goal is to demonstrate, through these cases, that the NAFTA panels reached the correct result but failed to articulate a methodological approach and criteria that may be used to guide subsequent panels in applying the Treaty and resolving its ambiguity and potential legitimacy problems. In addition to the discrimination and arbitrariness guideposts, I will show that the panels should have expressly articulated prudential principles for circumscribing the scope of Chapter 11, bringing it in line with the purpose of the system. I will also argue that the panels *de facto* rejected a rigid and formalistic approach in favor of a pragmatic approach that takes into account the political reality of constituent states' view of trade obligations. The panels indicated their willingness to move towards jurisprudence that takes into account the political and social reality of their domestic interlocutors, and their reaction to the perceived intrusion of trade norms on domestic subject matter. This move, however, was largely unspoken, and I will argue that the acceptance of the Chapter by domestic constituencies will depend on its interpreters' future willingness to articulate their methodological interpretation explicitly, thereby resolving the Treaty's crisis of legitimacy. Thus, my argument is that Chapter 11's ambiguity problem could in fact be resolved if the treaty's scope is limited and its decisions are guided by a growing

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[20] *Id.* at 44, 47.

[21] *Id.* In this Article, I review only the national treatment and international law provisions of the Treaty.

[22] *See* THE EU, THE WTO, AND NAFTA: TOWARDS A COMMON LAW OF INTERNATIONAL TRADE 1-4, 201-31 (J.H.H. Weiler, ed., Oxford Univ. Press 2000) [hereinafter TOWARDS A COMMON LAW].

[23] International Centre for Settlement of Investor Disputes, Case No. ARB(AF)/98/3. The Loewen Group, Inc. v. United States, Final Award, ICSID Case No. ARB/(AF)/98/3 ¶ 87 (June 26, 2003), *available at* http://www.state.gov/ documents/organization/22094.pdf.

[24] Mondev Int'l Ltd. v. United States, Final Award, ICSID Case No. ARB(AF)/99/2, (Oct. 11, 2002) *at* http://www.state.gov/documents/organization/14442.pdf.

body of "common law" of international trade, but that the panels should explicitly articulate their methodological approach.

This article proceeds in three parts. Section II outlines Chapter 11's history and the norms enshrined in the Treaty to the extent necessary for the reader to understand the thrust of the article's argument without having to refer to outside sources. Section III summarizes the two cases that are the subject of this article with a view to demonstrating how Chapter 11's three pillars—international law, national treatment, and takings—implicate the policy concerns described in this introduction. Section IV offers a potential solution to these difficulties, arguing that the panels should explicitly articulate and start applying principles of common law of international trade that are in accord with the object and purpose of the Treaty. Professor Weiler's observation that the legal frameworks of various international bodies are becoming more and more interconnected guides our understanding of the boundary between investment law under Chapter 11 and other areas of law such as WTO trade law or separate bodies of international law.[25] I will argue that principles of international trade law that are articulated by the WTO can, if properly transplanted into the context of investment law, supply new rules by which Chapter 11 panels may legitimately adjudicate cases.[26] The benefit will be two-fold. First, by interpreting Chapter 11 properly, Chapter 11 will serve its original object and purpose of providing neutral, minimally protective rules of investment law, thereby facilitating foreign direct investment, without unduly infringing on national sovereignty. Second, Chapter 11 would provide a jurisprudential and methodological model for construing international investment rules that are born out of the battles of the 20th century, in the business context of the 21st century, and it would further and continue the common law of trade enterprise.

II. HISTORY AND STRUCTURE

A. Background

The history of Chapter 11 has been recounted elsewhere, and need not be entirely restated here again.[27] Suffice it to say, for purposes of this Article, that the United States, Canada and Mexico had, before NAFTA, fundamentally divergent views of the contours of the customary

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[25] TOWARDS A COMMON LAW, *supra* note 22, at 1-4.

[26] *Cf.* Legitimacy Crisis, *supra* note 16.

[27] *See, e.g.*, CHARLES A. JONES, THE NORTH-SOUTH DIALOGUE: A BRIEF HISTORY 72-73 (1983); Ari Afilalo, *Constitutionalization Through the Back Door: A European Perspective on NAFTA's Investment Chapter*, 34 N.Y.U. J. INT'L L. & POL. 1, 13-19 (2001) [hereinafter NAFTA's Investment Chapter]; Eduardo Jimenez de Arechaga, *State Responsibility for the Nationalization of Foreign Owned Property*, 11 N.Y.U. J. INT'L L. & POL. 179 (1978).

international law of investment.[28] The United States, at bottom, advocated a formally neutral set of principles that would ban discriminatory measures and provide protection against takings without just compensation and other government action viewed as arbitrary.[29] This position was challenged by Mexico, which argued instead that less developed nations should be granted preferential treatment.[30] Mexico's position reflected the post-colonial critique that more *laissez faire* principles would entrench the unjust enrichment of the "North"—a loose appellation for the industrialized countries of Europe and for the United States—that resulted from years of colonization.[31]

When the most contentious provisions of Chapter 11 were finally agreed upon, their acceptance by Mexico signaled a decisive victory for the United States—the Chapter's most ardent backer.[32] Furthermore, Chapter 11 was supposed to presage an analogous investment chapter in the Free Trade of the Americas Agreement (FTAA).[33]

The predictive significance of Chapter 11 stems not only from its contents, but also from the players whose agreements it came to embody. Mexico had traditionally acted as a leading advocate of the traditional

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[28] The disparities in economic strength between Mexico and the United States (and Canada) was cause for concern in the "North" as well as the "South." In the United States, the 1992 election campaign featured the famous "Great Sucking Sound" comment from Ross Perot, which captured the fear that the lower Mexican labor standards and wages would "suck" American jobs down to Mexico (hence the "Sound"). This concern was shared by the American labor unions, and it led President Clinton to negotiate the NAFTA "side agreement on labor," which on paper compelled Mexico to enforce what turned out to be substantively protective labor norms that the government simply ignored. *See* William F. Pascoe, *Deja Vu All Over Again? Collective Bargaining and NAFTA: Can Mexican and United States National Unions Foster Growth under the NAALC?*, 19 ARIZ. J. INT'L & COMP. L. 741 (2002). From the Mexican standpoint, the concerns about NAFTA centered on its opening up borders for Northern employers to take advantage of cheaper labor, and repatriate profit and know-how home without leaving behind tools of meaningful development needed by the Mexican economy. *See* Jose E. Alvarez, *Critical Theory and the North American Free Trade Agreement's Chapter 11*, 28 U. MIAMI INTER-AM. L. REV. 303, 304 (1997).

[29] *See* Jose E. Alvarez, *supra* note 28; Gloria L. Sandrino, *The NAFTA Investment Chapter and Foreign Direct Investment in Mexico: A Third World Perspective*, 27 VAND. J. TRANSNAT'L L. 259 (1994); *see also* RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 712 (1987); Kevin Banks, *Can Regulation Be Expropriation?*, 5 NAFTA: L. & BUS. REV. AM. 499 (1999).

[30] Sandrino, *supra* note 29; *see also, e.g.*, SAMIR AMIN, ACCUMULATION ON A WORLD SCALE: A CRITIQUE OF THE THEORY OF UNDERDEVELOPMENT 382 (Brian Pearce trans., Monthly Review Press 1974).

[31] World-systems analysis and dependency theory are two such examples of this revisionist approach. *See, e.g,.* 3 IMMANUEL WALLERSTEIN, THE MODERN WORLD-SYSTEM: THE SECOND ERA OF GREAT EXPANSION OF THE CAPITALIST WORLD-ECONOMY 1730-1840S (1989).

[32] *See* NAFTA's Investment Chapter, *supra* note 27, at 19.

[33] Sandrino, *supra* note 29; *see also* Jose E. Alvarez, *supra* note 28.

developing countries' position on custom. The United States, for its part, firmly advocated the conflicting views of custom advocated by the North (summarized below). Mexico and like-minded countries argued that when political control over colonies was discontinued, it would also be necessary to take affirmative measures (including discriminatory action) to end economic subjugation by the colonizers' companies (which were viewed as economic agents of Northern domination) and to give the colonized nations the opportunity to achieve meaningful development.[34] The United States, for its part, pushed for the national treatment and protective rules that were ultimately embodied in Chapter 11.[35] When Mexico accepted the United States' view that colonization did not justify discrimination, arbitrary measures or takings, the international investment community predicted that future bilateral or regional investment treaties would follow suit.[36] In particular, it was thought that Chapter 11 would be the road map for the FTAA, and would protect investments throughout this future free trade area—"from Alaska to Tierra del Fuego."[37]

B. Structure of Chapter 11

NAFTA's "Investment Chapter," as written, set forth investment standards pertaining to three essential substantive topics (i.e. three "pillars" or "disciplines"): customary international law, national treatment, and takings.[38] It also established its own arbitral panels to hear disputes arising under any of the three subject areas.[39] The next subsections briefly review each of the pillars of Chapter 11. The Article then moves on to outlining its dispute resolution system, with a view to providing the background necessary for the ensuing discussion.

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[34] *See generally* Sandrino, *supra* note 29; *see also* PETER J. BURNELL, ECONOMIC NATIONALISM IN THE THIRD WORLD 243-44 (Westview Press, 1996).

[35] *See* Ari Afilalo, *Not in My Backyard: Power and Protectionism in U.S. Trade Policy*, 34 N.Y.U. J. INT'L L. & POL. 749 (2002) [hereinafter Not In My Backyard].

[36] Sandrino, *supra* note 29.

[37] This motto first appeared at a Free Trade of the Americas summit. The allusion refers to free customs zones and their potential impact on member economies. *See, e.g.*, Jon M. Tate, *Sweeping Protectionism Under the Rug: Neoprotectionist Measures among Mercosur Countries in a Time of Trade-liberalization*, 27 GA. J. INT'L & COMP. L. 389 (1999).

[38] I use these terms, borrowed from the European Union and WTO terminology, interchangeably to refer to the main provisions of Chapter 11. It is common knowledge that, aside from creating a unique dispute resolution framework, the essential provisions of Chapter 11 include the three disciplines of national treatment, takings and minimum standards of protection under international law. *See, e.g,* Daniel M. Price, *17th Annual Symposium, Investment, Sovereignty, and Justice: Arbitration Under NAFTA Chapter 11: Some Observations on Chapter Eleven of NAFTA*, 23 HASTINGS INT'L & COMP. L. REV. 421 (2000) (offering a brief overview of NAFTA by one of its chief negotiators for the United States).

[39] NAFTA, *supra* note 1, at ch. 11.

1. International Law

Article 1105 is the international law pillar of Chapter 11. Under this Article, the governments of all member nations must afford a level of protection to foreign investors that complies with minimal requirements of customary international law: "[e]ach 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."[40] The lynchpin principle behind Article 1105 is the protection of business operations outside the investor's jurisdiction from arbitrary government action.[41] Arbitrariness may come in various forms. For example, a shakeup in the government of a given country may result in attempts to cancel government contracts entered into by the previous ruling group.[42] A jurisdiction may fail to provide access to a justice system that satisfies minimum requirements, or that denies basic rights to foreign economic interests.[43] Article 1105 attempts to establish the minimum level of economic security that is thought to be a condition precedent to investment flowing into a particular jurisdiction.[44]

This international law pillar squarely rejected the view customarily adopted by Mexico. Mexico's objection to the U.S.-backed version was twofold. First, Mexico noted that substantive legal rights and, specifically, concepts like "arbitrariness," are not universal but particular; their applications are determined by the cultural, political or socioeconomic contexts in which they are found. Secondly, Mexico maintained, developing economies must be flexible in their policy assessments; changes

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[40] NAFTA, *supra* note 1, at art. 1105.

[41] RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 712 (1987); NAFTA Free Trade Commission, *Notes of Interpretation of Certain Chapter 11 Provisions* (July 31, 2001) *available at* http://www.dfait-maeci.gc.ca\tna-nac\nafta-intrpr-e.asp [hereinafter NAFTA Notes of Interpretation]. For example, a contract that the government cancels for no explicable reason outside of its desire to advantage domestic competitors, will probably be in breach of Article 1105. Initially, however, there was some question as to whether or not the treaty norms themselves could be considered part of "international law," which would essentially render the proviso moot. To avoid this problem, the FTC specifically declared international law to mean "customary" international law only. I will return to this point in Part II.

[42] *See* Legitimacy Crisis, *supra* note 16, at 57.

[43] *See generally* Renee Lettow Lerner, *International Pressure to Harmonize: The U.S. Civil Justice System in an Era of Global Trade,* 2001 B.Y.U. L. REV. 229, 233 (stating "NAFTA encompasses a substantive doctrine that capital-exporting countries have invoked against less-developed countries: the prohibition of denial of justice"). *See also,* RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 712 (1987); Brower & Tepe, *supra* note 12; Concerning the Chorzow Factory (F.R.G. v. Pol.), 1928 P.C.I.J. (ser. A) No. 17 (Sept. 13).

[44] *See, e.g.*, JEFFREY L. DUNOFF ET AL., INTERNATIONAL LAW: NORMS, ACTORS, PROCESS 71, 811 (2002).

of circumstances should be allowed to mitigate the enforcement of prior trade agreements if the country's economic welfare is at stake. To insist otherwise perpetuates the exploitive practices of ages past.[45] Again, Chapter 11 embodied the formally neutral view of arbitrariness espoused by the United States and other developed countries, thereby rejecting the contextual arguments traditionally advanced by developing countries.

2. National Treatment

Similar considerations attended Chapter 11's adoption of a national treatment standard. Article 1102 is designed to prevent domestic governments from requiring foreign investors to confer benefits to the domestic economy beyond those extended in the ordinary course of their business, from imposing more burdens on foreign economic interests than on domestic concerns, and from excluding foreigners from certain sectors of the domestic economy.[46] The Article states, "[e]ach Party shall accord to investors of another Party *treatment no less favorable than that it accords, in like circumstances, to its own investors* with respect to the establishment, acquisition, expansion, management, conduct, operation and sale or other disposition of investments."[47] This is another straightforward rejection of the position advocated by Mexico, which (again) had traditionally espoused the view that formal discriminatory measures were necessary to redress historical imbalances.

This formal equality standard was also enshrined in Article 1102's companion, Article 1106. This Article prohibits the imposition of "performance requirements." These measures were traditionally applied by less developed countries to compel foreign companies to confer benefits to the domestic economy beyond those transferred in the ordinary course of business. Performance requirements included the achievement of a given level or percentage of domestic content, the use of local goods or services, or the transfer of technology or other know-how.[48] Article 1102 reflects the position of the United States that the incentive to invest in areas with comparative advantage would disappear if the price-tag for doing so entailed "nation-building" in the economic realm.[49]

In contrast, Mexico and like minded countries had traditionally adhered to the position that formal discrimination might be justified as a

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[45] *See* Burns H. Weston, *The Charter of Economic Rights and Duties of States and the Deprivation of Foreign Owned Wealth*, 75 AM. J. INT'L. L. 437 (1981); *see also* Schwebel, *The Story of the UN's Declaration on Permanent Sovereignty over Natural Resources*, 49 A.B.A. J. 463 (1963); Alvarez, *supra* note 28.

[46] See Legitimacy Crisis, *supra* note 16, at 60-61.

[47] NAFTA, *supra* note 1, at art. 1102 (emphasis added).

[48] *Id.* at art. 1106.

[49] *See* Brower, *supra* note 4.

means of redressing historical wrongs. Under this view, developing countries could adopt measures such as the "performance requirements" so as to aid domestic development in ways more meaningful than if the foreign undertakings operated in the ordinary course of business under the same rules that applied to domestic concerns. The forced use of domestic suppliers or the transfer of capital or intellectual property to the local economy would, under this view, provide the domestic economy a lift that would partially compensate for the harm caused by colonization and other forms of perceived subjugation. Again, Article 1102 squarely rejected Mexico's view that these measures were necessary to generate economic self-determination as a necessary companion to decolonization and political independence.[50]

3. Takings

Finally, Chapter 11 addressed the complex issue of expropriation in its section on takings. Article 1110 adopts a position similar to that embodied in the Fifth Amendment of the U.S. Constitution: "[n]o 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 except: a) for a public purpose; b) on a non-discriminatory basis;. . .and d) on payment of compensation . . . equivalent to the fair market value of the expropriated investment immediately before the expropriation took place."[51] The Article further mandates prompt payment in full in cases where a taking has occurred.[52] These stipulations put Chapter 11's definition of expropriation on equal footing with the doctrine of eminent domain as embodied in U.S. case law on substantive due process. Without such requirements, the United States feared cross-border capital flow would be significantly impeded.[53]

Here again, Mexico championed the view that developing countries ought to be exempt from these takings provisions in order to correct historical disadvantage.[54] Proponents of this position claimed that a developing nation should only be required to pay what is "appropriate" under the circumstances.[55] This meant that seizure of investment property

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[50] *Id.*

[51] NAFTA, *supra* note 1, at art. 1110.

[52] *Id.*

[53] *See* Legitimacy Crisis, *supra* note 16; Vandevelde, *supra* note 11.

[54] *See* Sandrino, *supra* note 29 at 271-72.

[55] *Id.* at 218-19; *see also* Burns H. Weston, *Constructive Takings under International Law: A Modest Foray into the Problem of 'Creeping Expropriation,'* 16 VA. J. INT'L L. 103 (1975). To illustrate how divergent initial views on this issue were, consider the United States' further challenge to "creeping expropriation." This concept encompassed, among other things, the arbitrary use of state power to deprive a property owner of all uses of her

should be tolerated upon payment of compensation reasonable in light of the social and economic condition of the relevant country; needless to say, the United States rejected arguments of this type, and the United States' position was fully embraced by Chapter 11.[56]

4. Standing and Dispute Resolution

In addition to the three substantive matters just discussed, Chapter 11 also deals with the essential questions of jurisdiction and dispute resolution. Chapter 11 casts a broad net in its definition of "investors" and "investments." Almost any individual conducting any kind of business in a member country is covered under the chapter's provisions.[57] A non-exhaustive list of protected enterprises includes corporations, joint ventures, partnerships, and limited liability companies.[58] Further, many forms of assets and asset ownership fall within the purview of Chapter 11.[59] Recognizing that structural and capital arrangements are not uniform, the drafters' intent was to prevent member governments from circumventing provisions of NAFTA because of legal technicalities or investors' choice of business form.[60] As a result what may be understood as the scope of personal jurisdiction under the Chapter is expansive.[61]

Chapter 11 panels hear disputes arising under Chapter 11's substantive requirements, and are intended to give plaintiffs a supranational remedy—free of domestic interference—for NAFTA violations.[62] Again, it was the United States that successfully lobbied for the supremacy of international tribunals.[63] Prior to acquiescing, Mexico was steadfast in its adherence to the "Calvo Doctrine," which protects the jurisdiction of national courts.[64] Named after the Argentinean scholar who coined it, the doctrine essentially holds that economic and political self-determination is not complete unless

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property, forcing a sale at much less than fair market value. For example, a developing country might, without legitimate grounds, deny a permit necessary to keep a factory in operation. Technically, the factory would not be "taken," but its owner would lose the power to operate it. The government would then make an offer of purchase at a price much lower than its fair market value; in effect, amounting to uncompensated nationalization.

[56] *See* NAFTA's Investment Chapter, *supra* note 27, at 14-15.

[57] *See* Legitimacy Crisis, *supra* note 16, at nn. 54-61

[58] NAFTA, *supra* note 1, at arts. 1139 & 201.

[59] *Id.* 605, art. 1139.

[60] Legitimacy Crisis, *supra* note 16, at 61-62.

[61] *See* Price, *supra* note 38.

[62] Gregory M. Starner, *Taking a Constitutional Look: NAFTA Chapter 11 as an Extension of Member States' Constitutional Protection of Property*, 33 LAW & POL'Y INT'L BUS. 405, 413 (2002), *citing* MEX. CONST. ch. I, art. 27, *reprinted in* XII CONSTITUTIONS OF THE COUNTRIES OF THE WORLD (Albert P. Blaustein & Gilbert H. Flanz, eds., 1998).

[63] *See* NAFTA's Investment Chapter, *supra* note 27, at 16-17.

[64] *See* CHARLES M. CALVO, LE DROIT INTERNATIONAL 348 (5th ed. 1896).

national judges, applying national law, have the exclusive right to apply the domestic law.[65] It is a rejection of the Western position that supranational norms, applied by supranational arbiters, should govern international investment.[66] In Chapter 11, the United States, skeptical that nations with a traditional philosophical tendency to ignore private property rights so as to redress historical injustice could adequately protect cross-border capital, prevailed in its efforts and achieved an agreement that many thought would sound the death toll of the Calvo Doctrine.[67]

Chapter 11 created dispute resolution tribunals that operate under the aegis of either the World Bank or the United Nations. In either forum, a defendant government must pay the aggrieved investor compensatory damages when a substantive breach has occurred.[68] The system further specifies that the *central* government of any such defendant is held vicariously liable for the acts of subordinate branches: regional, provincial, municipal, state or local.[69] In other words, a breach of Chapter 11 by the State of Mississippi is actionable against the government of the United States, which would be required to compensate the private investor for any damages causally related to the breach. This measure, of course, raises the stakes, and thus, the degree of accountability.[70]

The awards rendered by Chapter 11 panels are enforceable by national courts. Under the rules applicable to awards rendered by the Investor for the Settlement of Investor Disputes (ICSID), a national court may refuse to enforce the award if it is tainted by procedural irregularities (i.e., lack of integrity in the arbitration "process").[71] The review rules applicable to awards rendered by panels operating under the aegis of the U.N. tribunals, the standard of review also allows courts to take public policy into account.[72]

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[65] *Id.*

[66] *See, e.g,* David E. Graham, *The Calvo Clause: Its Current Status as a Contractual Renunciation of Diplomatic Protection*, 6 TEX. INT'L L.J. 289-90 (1971); *see also* Manuel R. Garcia-Mora, *The Calvo Clause in Latin American Constitutions and International Law,* 33 MARQ. L. REV. 205, 219 (1950). The Calvo Doctrine, which makes the competence of Mexico's national courts absolute, has longstanding resonance in Mexican jurisprudence and appears in the national constitution.

[67] *See* NAFTA's Investment Chapter, *supra* note 27, at 17.

[68] *Id.* at 12.

[69] In the case of the United States of course, the federal government is liable.

[70] *See* NAFTA's Investment Chapter, *supra* note 27, at 19; *see also* Naomi Gal-Or, *Private Party Direct Access: A Comparison of the NAFTA and EU Disciplines*, 21 B.C. INT'L & COMP. L. REV. 1 (1998); Charles Brower, *Investor-State Disputes Under NAFTA: The Empire Strikes Back*, 40 COLUM. J. TRANSNAT'L L. 43 (2001).

[71] This standard of review is reminiscent of the one applied by federal courts in domestic commercial arbitration.

[72] Brower, *supra* note 70, at 49.

III. THE CASES

In this Section, I describe the background of the *Mondev* and *Loewen* cases and provide an analysis of each.[73] I will then explain in Section V how each case raises the problems of meaning, ambiguity and legitimacy. I will then argue that, although the result reached by the panels is correct, they failed to articulate a methodology that accords with international legal principles of interpretation and to engage explicitly in a common law development of the relevant principles that would properly circumscribe Chapter 11 in light of this object and purpose. This jurisprudential failure of the panels will undermine the usefulness of their opinions as guideposts for future decision-making. The background review of the cases set forth in this Section is necessary to understand the problems analyzed later.

The issue in *Mondev v. U.S.* would have normally been a generic tortious interference with contract claim if it had been confined to a dispute between private parties, or if the plaintiff had not been Canadian. Instead, it gave rise to an international challenge against an important provision of American tort law and civil procedure.

Mondev, a Canadian development corporation, accused the Boston Redevelopment Association (BRA) of obstructing its performance of an option contract.[74] Mondev's Massachusetts-based subsidiary entered into an agreement with the BRA and the City of Boston that gave Mondev the right and option to purchase a property at a given phase of the contract.[75] The contract further specified the date by which the option would expire if not exercised, provided that both parties worked in good faith to close acquisition of the property.[76] Mondev claimed that its failure to make good on the option in a timely fashion was due to the BRA's deliberate attempts to forestall purchase of the redevelopment property.[77]

In 1994, Mondev brought suit in a Massachusetts court against the City of Boston and the BRA.[78] The jury found that both defendants had not acted in good faith and were therefore liable for damages.[79] The judge, however, set aside the verdict because the state legislature had specifically

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[73] Mondev Int'l Ltd. v. United States, Final Award, ICSID Case No. ARB(AF)/99/2, (Oct. 11, 2002) *at* http://www.state.gov/documents/organization/14442.pdf (last visited Aug. 4, 2004); The Loewen Group, Inc. v. United States, Final Award, ICSID Case No. ARB/(AF)/98/3 ¶ 87 (June 26, 2003), *available at* http://www.state.gov/documents/organization/22094.pdf.

[74] *See Mondev*, ICSID Case No. ARB(AF)/99/2.

[75] *Id.* ¶ 38.

[76] *Id.*

[77] *Id.* ¶ 1.

[78] *Id.* ¶ 39.

[79] *Id.* ¶ 40.

granted immunity from lawsuit to municipal agencies.[80] The Massachusetts Supreme Judicial Court affirmed on appeal, and ordered all claims against the City of Boston and its agents to be dismissed.[81] Mondev subsequently filed for a rehearing before the Massachusetts high court, and then petitioned the U.S. Supreme Court for certiorari; the Canadian corporation was unsuccessful on both counts.[82]

Having exhausted its remedies under U.S. law, Mondev looked into possible NAFTA Chapter 11 claims. *Mondev* argued that Article 1105 (the international law prong of Chapter 11) was applicable, on the grounds (among other arguments) that the Supreme Judicial Court's unwillingness to waive appellees' grant of statutory immunity was a violation of NAFTA's international law pillar.[83] It filed for arbitration before a NAFTA panel.[84] The panel engaged at length in a discussion of the issues at hand, but ultimately it also ruled against Mondev.[85] In reaching its decision, the panel held that "investments of investors under NAFTA are entitled, under the customary international law which the NAFTA Parties interpret Article 1105(1) to comprehend, to fair and equitable treatment and to full protection and security," without specifying the core conceptual components of such a body of customary international law. [86] The panel then engaged in a review, under the amorphous principles which it found to provide the applicable guidance, of each factual basis adduced by Mondev in support of its complaint.[87] After dismissing Mondev's challenges to the legal analysis of the Supreme Judicial Court, the panel addressed the crux of the complaint: the denial of an otherwise proper claim by a domestic court on statutory immunity grounds.[88]

The panel stated, in dictum, that government, at any level, could not categorically deny private litigants the opportunity to be compensated for wrongdoing.[89] Regardless, the panel found that Massachusetts had acted within the discretion afforded by international law.[90] Statutory immunity, the panel reasoned, might be appropriate for a variety of reasons—e.g. conserving government resources that might be expended defending

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[80] *Mondev*, ICSID Case No. ARB(AF)/99/2.

[81] *Id.* ¶ 1.

[82] *Id.*

[83] *Id.* ¶¶ 93-156.

[84] *Id.* ¶ 1.

[85] *Id.* ¶ 157.

[86] *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶ 125.

[87] *Id.* ¶¶ 126-56.

[88] *Id.* ¶¶ 139-56.

[89] *Id.* ¶ 151 ("In the Tribunal's opinion, circumstances can be envisaged where the conferral of a general immunity from suit for conduct of a public authority affecting a NAFTA investment could amount to a breach of Article 1105(1) of NAFTA.").

[90] *Id.* ¶ 156.

frivolous lawsuits—and in the case at hand, the government had justifiable grounds for granting immunity to its agencies.[91]

Furthermore, in a move whose significance is described below, the NAFTA panel reiterated the necessity of showing a high degree of deference to national courts, and refused to usurp their authority by acting as an "international appellate court."[92] In the course of reviewing Mondev's challenge to the legal analysis of the Supreme Judicial Court, the panel stated that only cases involving blatant abuse of judicial discretion supported a contrary finding by NAFTA.[93] Furthermore, in a common law system, as in the United States, deviations from precedent cannot be offered as per se evidence that the verdict is an illegitimate one.[94]

The *Loewen* opinion likewise relied substantially on Article 1105, and it also addressed the plaintiff's argument under Article 1102. In *The Loewen Group, Inc. v. U.S.*, the NAFTA complainant challenged a sensitive set of U.S. procedures and practices; specifically punitive damages, unfettered jury verdicts, and the use of biases and xenophobic stereotypes in trials that allegedly resulted in an unfair and disproportionate verdict.[95] Loewen, a Canadian funeral home conglomerate, challenged the outcome of a Mississippi state trial that had ordered the company to pay $500,000,000 to a group of class-action plaintiffs for various claims under contract law.[96] When Loewen initiated NAFTA proceedings for violations of Article 1105, Article 1102 and Article 1110, there arose a fear that a ruling against the United States would chip away at the cornerstone of the U.S. civil litigation and erode domestic sovereignty over matters of justice.[97]

The original trial was a colorful one.[98] A brilliant lawyer, Willie Gary, tried the case in Hinds County, Mississippi. The son of African-American migrant workers, Gary fought his way to become a highly successful trial lawyer, and a larger than life character reminiscent of a John Grisham

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[91] *Id.*

[92] *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶ 126.

[93] *Id.* ¶¶ 127, 133.

[94] Mondev also asserted secondary claims, questioning the integrity of the trial judge's evidentiary rulings. NAFTA ruled in favor of the United States on these matters as well this seems "slanted" a little too much. *Id.*

[95] The Loewen Group, Inc. v. United States, Final Award, ICSID Case No. ARB/(AF)/98/3 ¶ 87 (June 26, 2003), *available at* http://www.state.gov/documents/organization/22094.pdf., at ¶ 87.

[96] *Id.* ¶¶ 3-4.

[97] Alvarez & Park, *supra* note 4, at 381-83; Adam Liptkak, *Review of U.S. Rulings by Nafta Tribunals Stirs Worries*, N.Y. TIMES, Apr. 18, 2004, *available at* 2004 WLNR 4553718; *The End of Sovereignty,* CONN. LAW TRIB., May 17, 2004, at 21.

[98] Charlotte Ku, *Emerging Worldwide Strategies In Internationalizing Legal Education,* 18 DICK. J. INT'L L. 493, 507 (2000) (citing Jonathan Harr, *The Burial*, THE NEW YORKER, Nov. 1, 1999, at 70).

hero.[99] In this case, Gary argued that the Canadian "carpetbagger" destroyed local competition, making inordinate profits off the backs of Mississippi's dead in the process. Though a reasonable verdict in the plaintiffs' favor would have cost no more than $10,000,000, Gary's courtroom tactics were clearly intended to inflame the jurors' xenophobic and class based tendencies.[100] Seeing how a proper rite of passage to the afterworld is serious business in Mississippi, the jury awarded damages (including punitive damages) 5,000% greater than it ought to have—sending Loewen a crystal-clear message.[101]

Defeated and angered by what it perceived as a failure of justice because of outrageous courtroom conduct, Loewen initiated proceedings against the U.S. government under Chapter 11.[102] Loewen argued that the U.S. government, vicariously liable for the actions of Mississippi juries, had violated each and every pillar of Chapter 11.[103] Loewen claimed that it was given discriminatory treatment as a foreigner, in violation of the national treatment norm.[104] It argued that the trial was so botched as to amount to a denial of justice under customary international law and a violation of Article 1105.[105] Lastly, Loewen asserted that the verdict constituted a taking of its property without compensation at fair market value in breach of Article 1110 because the court and the jurors essentially expropriated his money through an unwarranted verdict.[106] These claims were premised in large part on the argument that the punitive damages assessed in the case violated international law, that procedural irregularities vitiated the administration of justice in the case, that the trial judge was partial, and that the Mississippi Supreme Court refused to reduce the appeals bonds requirement that was a condition to its review of the case on account of a politically motivated desire to let an illegal verdict stand.[107] Meanwhile,

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[99] See Legitimacy Crisis, *supra* note 16, at 65.

[100] *Loewen*, ICSID Case No. ARB/(AF)/98/3, ¶¶ 68-70. As stated by the Panel:

> When the trial is viewed as a whole right through from the voir dire to counsel's closing address, it can be seen that the O'Keefe case was presented by counsel against an appeal to home town sentiment, favoring the local party against an outsider. To that appeal was added the element of the powerful foreign multi-national corporation seeking to crush the small independent competitor who had fought for his country in World War II. Describing "Loewen" as a Canadian was simply to identify him as an outsider.

Id. ¶ 70.

[101] *See id.* ¶¶ 3-4, 39(3), 80, 92-93, 104, 106-14.

[102] *Id.* ¶¶ 4, 8.

[103] *Id.* ¶¶ 39-40.

[104] *Id.* ¶ 39.

[105] *Id.*

[106] *Loewen*, ICISD Case No. ARB/(AF)/98/3.

[107] *Id.* ¶¶ 39, 48.

having gone through the proper appeals channels in state, Loewen agreed to settle for $150,000,000, under threat of seizure of its assets to satisfy the larger verdict.[108]

When the NAFTA tribunal finally issued its decision, it sided with Loewen on the merits.[109] In dicta, the tribunal stated that the trial judge had completely abdicated his responsibilities to ensure the defendant basic due process and to rein in Willie Gary.[110] It agreed with the petitioner in its assessment of the record: procedural gaffs had tainted the award of punitive damages, which in any event were so disproportionate to actual damages as to raise serious questions of fairness.[111] However, the panel then dismissed the case on the grounds that Loewen should not have brought its NAFTA claims when it chose to before exhausting all possible remedies under U.S. law (petitioning the U.S. Supreme Court for *certiorari*).[112]

The tribunal's decision, in my judgment, shows an internal tension. On the one hand, the panel clearly believed that Loewen was denied justice. At the same time the tribunal must have been acutely aware of the onslaught in store for NAFTA Chapter 11 were it to rule against the United States.[113] The critics feared that the panel would elevate trade and investment norms above the right of access to courts, protection of weaker parties vis-à-vis unbounded corporate interests, contingency fee arrangements enabling plaintiffs to retain talented but expensive attorneys, award of punitive damages in deterrence of egregious conduct and basic civil procedure within a federal system.[114] *Potential* conflict involving any

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[108] The lawsuit had proved to be a real thorn in Loewen's side, contributing to the precipitous drop in its stock value. It was widely – and correctly – supposed that reaching settlement would help reverse that effect.

[109] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶¶ 53-70. While the panel's grounds for dismissing the claims were technically procedural, the panel engaged nonetheless in a review of the case on the merits and found for the United States.

[110] *Id.* ¶ 87.

[111] *Id.* ¶ 122.

[112] The NAFTA tribunal's dismissal made it unnecessary to consider other claims asserted by Loewen. Those included a claim that Mississippi denied national treatment to Loewen because its courts singled out the Canadian defendants for discriminatory treatment. In addition, Loewen argued that the botched trial had "expropriated," de facto, the settlement amount from the defendants. These claims stemmed from the primary grievance that the United States' often-criticized tort system gave rise to an unusually wayward monetary judgment in the case at hand. On this point, as explained above, the tribunal squarely endorsed the defendant's position. Unfortunately, however, Loewen's failure to file for cert in a timely fashion, as well as its executed settlement with the Mississippi plaintiffs, precluded any future claims or issues from being brought in American courts—an incurable defect, as it turns out, in its NAFTA proceedings.

[113] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶ 1 (opening opinion with statement that "this is an important and extremely difficult case.")

[114] *See* Francisco S. Nogales, *The NAFTA Environmental Framework, Chapter 11 Investment Provisions, and the Environment*, 8 ANN. SURV. INT'L & COMP. L. 97, 139

one of these basic components was at the heart of their concern, with good reason.[115] The implications of such potential conflict are discussed in the following section, where I also argue that the Loewen panel should have engaged in a common law articulation of jurisprudential concerns that would insulate the Chapter from the adverse reaction that would have resulted from a ruling against the United States.

IV. MEANING, AMBIGUITY AND LEGITIMACY

This Section discusses each of the pillars of Chapter 11 as illustrated by the *Mondev* and *Loewen* cases. It exposes how these cases involved the symptoms of the crisis of legitimacy that afflicts Chapter 11, which are rooted in the ambiguity of the meaning of the Treaty. In each instance, the supranational norm put pressure on a domestic choice in a sensitive area of the law. In *Loewen*, the debate over tort reform taking place in U.S. legislatures or election campaigns encountered the relatively widespread hostility of other systems of law to allow the jury to award punitive damages or to countenance contingency fees and other characteristics of the U.S. judicial system as it currently stands.[116] In *Mondev*, the international panel was asked to intervene in a domestic court's administration of a statutory directive protecting public resources. In both instances, the ambiguous meaning of the Treaty allowed for a review of the domestic norm, resulting in a potential crisis of legitimacy.

A. The Problem of Meaning and Ambiguity in Defining Customary International Law, National Treatment and International Takings Law, and Its Impact on National Sovereignty

1. Article 1105

The ambiguity issues related to Article 1105 are illustrated by the *Mondev* and *Loewen* proceedings. Article 1105, as its history indicates, embodies the United States-backed principles of customary international law that provide minimal levels of protection to foreigners.[117] The lynchpin of the substantive rights protected by Article 1105 is the right to be free from arbitrary government action. As will be discussed later, in the *Loewen* and *Mondev* cases, the salient questions related to whether judicial and statutory practices affecting access to justice constituted arbitrary denials of

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(2002). *See, e.g.* PUBLIC CITIZEN, *supra* note 4.

[115] See my discussion of *Torfaen Borough, infra* notes 193-197 and accompanying text.

[116] For a recent debate on tort reform, *see* Press Release, White House, President Discusses Lawsuit Abuse at White House Economy Conference (Dec. 15, 2004), *available at* 2004 WL 61639873 [hereinafter White House Conference].

[117] NAFTA, *supra* note 1, at art. 1105.

justice.[118]

The language of Article 1105, however, like its companion pillars, is laden with interpretative ambiguities.[119] Article 1105 is indiscriminate in its reference to "international law."[120] Read broadly, the Article might extend jurisdiction to NAFTA panels any time business interests are affected by a government measure that violates international law. The Free Trade Commission's Interpretative Notes clarified that international law must qualify as customary international law, and that a treaty provision would not be actionable under Chapter 11.[121] Presumably, however, a provision of a treaty that has become a norm of customary international law could be the basis for a cause of action. Also, as *Mondev* and *Loewen* demonstrate, Chapter 11 panels may not even consider themselves bound by the FTC's construction.[122] In all events, the amorphous language of Article 1105 opens the door to challenging any national measure that affects economic interest and that may violate international law.

Loewen and *Mondev* illustrate these arguments. In *Loewen*, the crux of the plaintiff's challenge was that the Mississippi tort system allowed the use of stereotypes and xenophobic tactics to obtain disproportionate punitive damages, thereby violating international law on minimum standards of justice.[123] Loewen had to attack the Mississippi Supreme Court's denial of its petition to reduce the appeals bond, in order to have a clear government action to challenge. However, its grievance was essentially with the Mississippi trial. Loewen adduced an affidavit from a former president of the International Court of Justice to argue that the imposition of punitive damages in the case was a violation of international law.[124] Loewen's NAFTA pleadings were replete with anecdotal evidence of the failure of the Mississippi trial court to adhere to due process, and its allowing highly prejudicial evidence for the sole purpose of inflaming the jury against the defendant.[125]

By way of example, the trial judge allowed the plaintiffs to call in Mike Espy, a former Congressman from the Mississippi Delta and Agriculture Secretary under President Clinton, to testify that O'Keefe (a white plaintiff) was a good friend of the African American community.[126]

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[118] *See infra* notes 140-48.

[119] The potential breadth of the language led to the drafting of the FTC's Interpretive Notes. *See* NAFTA Notes of Interpretation, *supra* note 41.

[120] NAFTA, *supra* note 1, at art. 1105.

[121] NAFTA Notes of Interpretation, *supra* note 41.

[122] *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶¶ 94-127.

[123] *Loewen*, ICSID Case No. ARB/(AF)/98/3, ¶¶ 68-70.

[124] *See* Affidavit of Sir Robert Jennings, on file with author.

[125] *Id.*

[126] *Loewen*, ICISD Case No. ARB/(AF)/98/3.

Espy's testimony was part of a three-prong strategy clearly intended to appeal to the predominantly African American jury.[127] In addition to Espy's testimony, other statements made and evidence introduced at trial included repeated negative references to the "Canadians" as alien corporate interests bent on taking advantage of the good people of Mississippi in their very hour of sorrow.[128] Willie Gary went as far as to compare the Japanese attack on Pearl Harbor to the Canadian "descent upon Mississippi" and to distribute flyers in town that featured the Canadian flag side by side with the Japanese one.[129] The "corporate monster" theme was sounded effectively throughout the trial, with repeated references to meeting held by a cigar smoking Loewen on a fancy yacht, with which the humble and down to earth Mr. O'Keefe had a difficult time adjusting.[130]

The meaning and ambiguity problem arises because the mere reference to "international law," albeit customary, does nothing to distinguish between the international law that is actionable under Article 1105 and that which is not. *Loewen* involved the tension between international custom and a distinctly U.S. practice—the award of punitive damages to deter wrongful behavior through a system of contingent fee lawyers with some latitude to appeal to the prejudices of a virtually all-powerful jury. International practice does not necessarily conform to the U.S. practice of awarding punitive damages, and the international law ambiguity as to what is permissible in the way of punitive damages gave Loewen an opening to bring a private action to challenge the Mississippi proceedings.[131] Without a guidepost for deciding which international law displaces domestic norms, Article 1105 becomes a mere conduit for incorporating norms of international law (as the panel might understand them) into the domestic legal system.

The related legitimacy problem arises because the international arm attempts to reach deep within a debate that is national in nature and touches on sensitive domestic chords. Judicial practices and tort reform have hovered over Congress, state legislatures, federal and state courts and (of late) the presidential campaign.[132] The debate pits familiar opponents on

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[127] *Id.* ¶¶ 60-62, 72. This strategy consisted of encouraging discrimination based on race, class and nationality.

[128] *Id.* ¶¶ 32, 39.

[129] *Id.*

[130] *See id.* ¶ 68.

[131] *See* Shelby D. Green, *Specific Relief for Ancient Deprivation of Property*, 36 AKRON L. REV. 245 (2003); Michael Reisman & Monica Hakimi, *Illusion and Reality in the Compensation of Vicitims of International Terrorism*, 54 ALA. L. REV. 561 (2003); *cf.* Phillip I. Blumberg, *American Law in a Time of Global Interdependence: Asserting Human Rights Against Multinational Corporations Under United States Law*, 50 AM. J. COMP. L. 493, 504-06 (2002).

[132] White House Conference, *supra* note 116; Lewis H. Lapham, *Tentacles of Rage: The*

the American scenes against one other. Plaintiff's lawyers and consumer advocates are fighting ostensibly to promote corporate accountability through the threat of a lawsuit. Business interests counter that the consumer will ultimately suffer the cost of lawsuits that are often thought to be frivolous, and that economic growth requires that the contingency fee system be reined in. As Professor Daniela Caruso has explained in the European context, the private law system is highly resistant to interference by an international body or set of norms in its administration by judges and like officers.[133] In turn, as will be further explained below, how to conduct litigation, who should have access to justice, and how our system of law should be handled are domestic sovereign matters that, when scrutinized under international raise, raise legitimacy concerns in that all of these issues are essential components of the private law system.

Similar issues arose in the *Mondev* cases, albeit in a different context. There, the issue related to statutory immunity.[134] Again, as *Mondev* demonstrates, international law has a say on how far a State may go in depriving a plaintiff of access to justice.[135] The Massachusetts practice, however, was challenged under open ended language of Article 1105, and the case illustrates that without additional interpretative tools Article 1005 may graft international law (as interpreted by the panel) into domestic law in a wholesale fashion.[136] In turn, as in *Loewen*, the international rules affected highly sensitive issues of domestic private law and of governmental immunity from suit, which essentially deal with the extent to which the taxpayer should pay for errors made by the government.[137] As further explained below, the very fact that these issues would be litigated before an international arbitral tribunal raised serious questions of legitimacy.

Republican Propaganda Mill, a Brief History, HARPER'S MAG., Sept. 1, 2004, at 31; Stephanie Mencimer, *False Alarm: How the Media Helps the Insurance Industry and the GOP Promote the Myth of America's "Lawsuit Crisis,"* WASH. MONTHLY, Oct. 1, 2004, at 18.

[133] Daniela Caruso, *The Missing View of the Cathedral: The Private Law Paradigm of European Legal Integration*, 3 EUR. L.J. 3 (1997).

[134] *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶¶ 139-56.

[135] Sean Murphy, *Contemporary Practice of the United States Relating To International Law, State Responsibility, and Liability: The Denial of Justice Standard in International Law*, 97 AM. J. INT'L L. 438 (2003); Thomas H. Lee, *Making Sense of the Eleventh Amendment: International Law and State Sovereignty*, 96 NW. U. L. REV. 1027, 1096-97 (2002); *cf.* Roger H. Taylor, Note, *Pinochet, Confusion, and Justice: The Denial of Immunity in U.S. Courts to Alleged Torturers Who Are Former Heads of State*, 24 T. JEFFERSON L. REV. 101 (2001) (discussing principles of head of state immunity that are applicable to statutory immunity).

[136] *Compare* NAFTA, *supra* note 1, at art. 1105, *with* NAFTA Notes of Interpretation, *supra* note 41.

[137] *Loewen*, ICISD Case No. ARB/(AF)/98/3.

2. Article 1102

Article 1102 presents similar problems of interpretation. Article 1102 refers to "national treatment" with respect to investment, and it does not distinguish between investment cases and those under the WTO that address more sensitive issues of international trade law, such as how to deal with regulatory disparities among various jurisdictions (especially among developed and developing countries).[138] This textual ambiguity stems from the impossibility of distinguishing between traders and investors. By definition, trade is carried out by enterprises and their owners, the "investors" that Chapter 11 has in mind. When it requires states to afford national treatment to these investors, Chapter 11 is in effect replicating textually the WTO's national treatment norm. Hence, as is the case with respect to the international law pillar of the Chapter, Article 1102 has the potential to swallow and bring within the ambit of private party litigation greater issues of international law that traditionally are resolved either diplomatically or through infrequent, selective state-to-state dispute resolution, such as cases brought before the WTO Dispute Settlement Body.[139]

The problem is compounded because the WTO itself is laden with ambiguity. The upshot is that Chapter 11 could become the forum for private parties to litigate issues that are bound to bedevil the WTO for the foreseeable future. These issues relate principally to the disparities in the regulatory environments that exist in the various countries engaged in cross-border trade. Should a regulation that disproportionately burdens foreign companies be struck down even if it is not intended to discriminate against foreigners? Should a developing country be allowed to trade on its lesser protection of environmental, labor, consumer or health rights, or may a developed country justifiably impose trade sanctions intended to level the playing field? If a developing country may use lesser levels of regulation to attract business, is there any floor that an international tribunal should articulate in the absence of international consensus? Under Chapter 11, as written, these questions could become the subject of private party litigation, and NAFTA plaintiffs seeking damages, rather than states in infrequent proceedings, would be litigating WTO issues at the NAFTA level, with a resulting legitimacy problem.[140]

3. Takings

The same problem of meaning, ambiguity and legitimacy arises in the area of Chapter 11's takings law. By failing to define what is a "measure

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[138] Legitimacy Crisis, *supra* note 16, at 82-85.
[139] *Id.*
[140] *Id.*

tantamount to an expropriation," Chapter 11 leaves litigants free to argue that a broad array of government actions amount to what we call regulatory takings.[141] Under United States Supreme Court jurisprudence, decades of precedential evolution can guide a decision in any given takings case.[142] The Court will carefully assess the investment-backed expectations of the plaintiff, and will weigh those against an evaluation of the measure at issue that draws from deeply rooted legal and regulatory practices.[143] An international panel operating with the guidance and judicial sensitivity accrued over decades of jurisprudence, on the other hand, may be left with nothing beyond vague and malleable words to judge whether an entrenched domestic practice violates international law.

At bottom, the *Loewen* cases involved attacks that had no legitimate basis in the law of regulatory takings under the U.S. judicial practice.[144] Loewen challenged punitive damages and unfettered jury verdicts, arguing that the jury essentially "took" his property by imposing unnecessarily high punitive damages.[145] This strained reading of what a "measure tantamount to an expropriation" involves illustrates the potential for a broad interpretation of the amorphous language of Article 1105.[146]

The next subsection argues that in the *Loewen* and *Mondev* cases the Chapter 11 panel cases could have engaged explicitly in a proper evaluation of the object and purpose of the system.[147] In both cases, the panel ultimately demonstrated an understanding of the relevant Chapter 11 concepts—deference to the rulings of national courts and consideration for prudential principles limiting interference with state sovereignty—but it failed to ground its rulings on an explicit articulation of the principles at work.[148]

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[141] *Id.* at 84-88.

[142] *See* Michael A. Heller & James E. Krier, *Deterrence and Distribution in the Law of Takings*, 112 HARV. L. REV. 997 (1999).

[143] *See, eg.,* Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982) (characterizing a cable installer's right of entry as a permanent albeit partial physical occupation, and therefore a taking); Frank Michelman, *Takings*, 88 COLUM. L. REV. 1600 (1987).

[144] *Compare Loretto*, 458 U.S. 419, *and* Michelman, *supra* note 143, *with Loewen*, ICSID Case No. ARB/(AF)/98/3, ¶ 44.

[145] *See Loewen*, ICSID Case No. ARB/(AF)/98/3, ¶ 44.

[146] NAFTA, *supra* note 1, at art. 1105.

[147] Of course, according to customary international law, as expressed in Article 31 of the Vienna Convention on the Law of Treaties of 23 May 1969, a treaty must be interpreted in good faith in accordance with the ordinary meaning to be given to its terms in their context and in the light of its object and purpose. *See, e..g,* Legal Consequences of the Construction of a Wall in the Occupied Palestinian Territory, 43 I.L.M. 1009, ¶ 94 (ICJ 2004).

[148] *Loewen*, ¶¶ 208-40; *Mondev,* ICSID Case No. ARB(AF)/99/2.

B. Arbitrariness, Anti-Discrimination and National Takings Law: the Fundamental Common Law Principles of Chapter 11.

This subsection reviews each of the common law principles that should guide Chapter 11 panels in interpreting the treaty, and explains how the *Mondev* and the *Loewen* decisions might be explained as furthering and applying these principles to limit the Chapter to its proper scope. In addition, it discusses the prudential concerns that the *Mondev* and *Loewen* panels followed to limit Chapter 11 to supplement the common law principles described above, but that they filed to explicitly articulate.

Start with the notion of arbitrariness.[149] At issue in *Mondev* was the extent to which a government may immunize official actors from liability.[150] As with punitive damages, immunity carries the potential for arbitrariness. By definition, the body that receives immunity has violated the law and, except for its special status, would be liable to the plaintiff. However, considerations separate from grounds for liability make the defendant immune from prosecution.[151] These considerations include, usually, logistical and practical concerns for the proper functioning of government, as well as the need for certain actors to operate free from legal constraints.[152] For example, a firefighter requires a certain degree of immunity from civil liability.[153] The firefighter is engaged in a highly dangerous activity, where accusations of negligence or neglect of duty may easily be brought forth in hindsight. If fire departments could be subjected to negligence lawsuits without an additional layer of protection, they would likely be dragged into endless litigation that could potentially bankrupt their treasuries (probably in legal fees alone). Firefighters in the field, therefore, might be deterred from doing their jobs to the best of their judgment. In order to avoid this state of affairs, a legislative body might immunize a fire department against all negligence-based lawsuits, or shelter it from liability altogether for performance of its public duties.[154]

The *Mondev* panel properly recognized the limits of Chapter 11 with respect to a legislative grant of immunity.[155] It created an arbitrary floor, for which governments must be held accountable if they fall below.[156] The

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[149] Legitimacy Crisis, *supra* note 16, at 46-49. Arbitrariness should be the lynchpin of Chapter 11's international law analysis because, by definition, it involves no countervailing, important governmental interest.

[150] *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶¶ 139-156.

[151] *See, e.g.*, Jean W. v. Commonwealth, 610 N.E.2d 305 (Mass. 1993) (discussing immunity rationale).

[152] *See, e.g.*, Eyssi v. City of Lawrence, 618 N.E.2d 1358 (Mass. 1993).

[153] *See id.* at 197-98.

[154] *Id.*

[155] *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶¶ 140-50.

[156] *Id.* ¶¶ 151-54.

panel limited its findings to the facts of that case.[157] Clearly it intended to put governments on notice that future dispositions of the immunity issue might not go as well if the regulating authority did not respect the NAFTA ban on arbitrary government action. Much as a constitutional court controls government action by requiring that a reasonable relationship exists between the means and objective, the Chapter 11 panel protected the foreign investors' interests by requiring that a valid reason exist for the grant of statutory immunity.[158] However, because the grant of immunity fell short of arbitrary action, the panel properly refrained from interfering with the legislature's judgment.[159] It did not express any view as to the desirability of immunity in a given setting; as long as there was a particularized, reasonable ground for the legislation, the panel would not interfere with domestic jurisdiction.[160]

This ruling makes eminent sense when evaluated in light of an understanding of the object and purpose of Article 1105 as banning arbitrary treatment. In today's financial world, arbitrariness is one of the most powerful deterrents to investment. Certainty and predictability are core elements of the cross-border investor's panoply. By insisting on a legitimate governmental purpose, the NAFTA panel upheld the investment protective goals of the Chapter, all the while respecting national sovereignty over an important domestic norm. However, the panel should have expressly grounded its ruling on this view of customary international law of investment. By including a standard that is amenable to being applied and interpreted in future cases, such as arbitrariness, the panel would have infused some meaning into the notion of "international law" and resolved the legitimacy crisis that arises from the ambiguous meaning of the text.

In *Loewen*, the tribunal properly rejected challenges based on Article 1102 and Article 1110, but then had to turn to prudential considerations in finally rejecting Loewen's claim under international law.[161] First consider national treatment and takings, and let us understand why the panel was right to reject Loewen's claims on these counts. With respect to Loewen's national treatment claim under Article 1102, the crux of Loewen's argument was that the corporation was selected for discriminatory treatment because it is Canadian.[162] I have argued that, in order to distinguish Chapter 11 national treatment claims from broader national treatment cases that unjustifiably infringe on sovereignty issues, a Chapter 11 panel must focus on whether there is sufficient evidence of economic protectionism (or,

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[157] *Id.*
[158] *Id.*
[159] *Id.*
[160] *Id.* at ¶ 154.
[161] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶¶ 150-62.
[162] *Id.* ¶¶ 139-40.

conversely, whether a State interest unrelated to economic protectionism may be found).[163]

If a court intentionally discriminates against a foreign party, the foreign party's costs of doing business in a given jurisdiction increase, putting the investor at a disadvantage vis-à-vis domestic competitors. There is no difference between such a situation and a case where a regulation imposes a greater burden on foreigners than it does on local enterprise. In both instances, the measure may be challenged under Chapter 11, and it will not infringe on national sovereignty because the practice of discrimination is clear-cut and not countervailed by any domestic interest unrelated to economic protectionism.

However, in *Loewen*, the discrimination that took place was not based on the nationality of the defendant. As the United States claimed, there is no reason to believe that Mr. Gary would have argued his case any differently had Loewen been a New York company.[164] In fact, he might have stoked more prejudice had he been able to point to Yankee corporate interests, rather than to those of our calmer neighbors to the North. In addition, the biases to which Mr. Gary appealed were primarily class based.[165] The imagery was that of the greedy corporate interests taking advantage of the "little guy."[166] Repeated references to Mr. Loewen's yacht and tycoon business habits, in contrast with the quaint, wholesome and local nature of the plaintiff's personality and business, dominated the trial discourse.[167] In other words, the discrimination, was part and parcel of a jury system that accommodates local attitudes and allows for a certain amount of prejudice and stereotyping to affect a decision, but it could not be said to primarily reflect economic discrimination against foreign interests.[168]

Likewise, regarding the takings claim, the panel was correct to find that Loewen's argument was without merit. Here, Chapter 11 did not reach any farther than the domestic law on takings.[169] It is clear, under the

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[163] Legitimacy Crisis, *supra* note 16, at 89-90. *See also* Not in My Backyard, *supra* note 35.

[164] The United States' argument was noted by the panel. *Loewen*, ICSID Case No. ARB/(AF)/98/3, ¶ 70.

[165] *Id.* ¶¶ 39, 68-70.

[166] *Id.* ¶¶ 68-70.

[167] *Id.* ¶ 68.

[168] As touched on below, *infra* note 201, there is also a State interest in allowing appeals to jurors' prejudice; however misguided that policy may be, it allows in U.S. trial practice for community views to find their expression in a verdict on liability. Foreign intervention and meddling with such a practice would unsettle the domestic equilibrium, and would therefore raise serious legitimacy questions. In these circumstances, then, it was proper for the NAFTA panels to dismiss the national treatment claim.

[169] Legitimacy Crisis, *supra* note 16, at 42-50. *See also* Not in My Backyard, *supra* note

applicable U.S. jurisprudence, that a jury verdict of this type does not constitute a taking or a regulatory taking actionable in federal court.[170] This case illustrates the absurdity of going through a regulatory takings analysis without the guidance provided by national law. Under a literal interpretation, it may be argued that a defendant in any jury case has a protected property interest: the right not to have assets seized and attached in satisfaction of a judgment that is not warranted by facts or law. Any arbitrary decision, under this logic, would give rise to a counterclaim against the government because, by enforcing the award, the sheriff or other local official is taking the property of the defendant.

The difficult aspects of the *Loewen* case, and its most instructive portions, relate to the international law pillar of Chapter 11. Here, Loewen had (as mentioned above) a valid Chapter 11 case. The Mississippi trial involved a national practice with profound economic consequences: the award of punitive damages to deter wrongful behavior. The American legal system's endorsement of punitive damages is in tension with international practice,[171] so it is not surprising that a NAFTA panel would find the award of large monetary sums in tension with international law. Loewen's submission to the NAFTA panel included compelling evidence that the trial was botched and did not satisfy minimal standards of justice.[172] In its pleadings, Loewen supplied an affidavit by the former president of the International Court of Justice (ICJ), stating that an award of punitive damages under those circumstances violated customary international law.[173] Repeatedly, the company pointed to the magnitude of the award, which was so disproportionate to the harm incurred.[174] While most of the U.S. officials would concede that a half-billion dollar verdict is excessive, many found it unsettling to know that an integral component of civil actions in the United States might be scrutinized internationally.[175] This sentiment was especially resonant because tort reform has been a vigorously debated issue

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[170] Fifth Amendment jurisprudence turns not only on substantive due process but the procedural variant also. By definition, the delivery of a jury verdict presupposes "due process of law." Moreover, U.S. case law on takings has heretofore considered only deprivation of property rights when it concerns real property interests. *See, e.g.*, Lucas v. South Carolina Coastal Council, 505 U.S. 1003 (1992); Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982); Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 123 (1978).

[171] *See* Affidavit of Sir Robert Jennings, on file with author.

[172] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶ 119 ("By any standard of measurement, the trial involving O'Keefe and Loewen was a disgrace.").

[173] *See* Affidavit of Sir Robert Jennings, on file with author.

[174] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶¶ 46, 96-113.

[175] *See, e.g.*, Note, *'Common Sense' Legislation: The Birth of Neoclassical Tort Reform*, 109 HARV. L. REV. 1765 (1996).

in the United States for many years, making democratic consensus all the more important.[176] If a judgment limiting punitive damages was left to stand, it would be seen as a flagrant assault on the processes by which political legitimacy is established.

In addition, the case raised important issues related to the administration of justice in the United States. The United States is known throughout the world as a bad place for corporate defendants to litigate.[177] The reasons for fearing the U.S. system are numerous. One most obvious is that juries are said to use punitive damages gratuitously to punish what cunning lawyers for the plaintiff depict as gross violations of justice.[178] At the end of the day, whether in the Bronx or in Hinds County, Mississippi, the U.S. justice system contains a series of pitfalls for the unwary that foreign business interests might do best to avoid—as would their similarly situated domestic counterparts.

Regardless of the sensitivity of the issue, however, the facts supported Loewen's denial of justice under international law. The concept of "denial of justice" as commonly understood under international law lies at the core of Article 1105.[179] The notion conjures up images of kangaroo courts blindly favoring local interests, which are deterrent to investment and the security of property rights. By definition, a denial of justice is arbitrary. In a case where a party otherwise would be entitled to redress, he or she is shut out of the court on account of a fundamental defect in the legal system. If arbitrary means "without reason," there is virtually no better application of the concept than in the denial of justice context: There is no legitimate reason, in any jurist's mind, why someone entitled to redress should not receive it just because the local system produces unfair results.

Applying the concept of arbitrariness, a strong argument could be made for Loewen's victory before the NAFTA panel. Putting aside technical difficulties with Loewen's case to reach the merits of its claim, it is beyond doubt that the panel was right when it held that Loewen was denied justice.[180] The trial was simply a mockery. Willie Gary, his talent notwithstanding, mostly provided a lesson in the effective use of jury inflammation,[181] and blatant appeals to their xenophobia and other prejudices.[182] He shifted attention away from the facts and pitted the "little

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[176] *Id.*

[177] *See* Blumberg, *supra* note 131, at 504-06.

[178] *Id.*

[179] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶ 132 (stating "[m]anifest injustice in the sense of a lack of due process leading to an outcome which offends a sense of judicial propriety is enough. . .").

[180] *Id.* ¶¶ 48-54.

[181] *Id.* ¶¶ 57-59.

[182] *Id.* ¶¶ 56-64.

guy" against "corporate greed," in terms that evoked epic battles of good versus evil.[183] The judge simply abdicated his responsibilities, brazenly stating that in his view lawyers should be free to play the "race card," and knowing full well that only the plaintiff could benefit from this tactic.[184] The jurors bought the scenario wholeheartedly.[185]

The Mississippi Supreme Court abdicated its appellate responsibility as well.[186] Loewen gave reasonable assurances that it would not squander its assets pending a trial, yet the court insisted on the posting of a bond that was impossible to procure.[187] If arbitrariness is indeed the yardstick, it would be hard to find a clearer instance than in the conduct of the judicial authorities that oversaw the *Loewen* trial.

Yet, the Chapter 11 panel did not rule against the United States.[188] Instead, the tribunal chastised the State of Mississippi for its demonstrated lack of commitment to justice.[189] It intimated that disproportionately high punitive damages might, in proper circumstances, be the subject of a valid Chapter 11 action, especially when administered in a case where due process is not respected.[190] However, the panel relied on Loewen's failure to seek certiorari in the United States Supreme Court and on the general international law principle that domestic remedies must be exhausted (i.e., the "finality principle"), to dismiss Loewen's claim.[191] In my view, this result was justified not because of the reason stated by the tribunal, but because it was rooted in a healthy dose of realism in the application of international law, with a view to minimizing domestic challenges to the legitimacy of the international law.

In order to illustrate this point, let me go back to a decision of the European Court of Justice in an early case that arose under the provisions of European law dealing with measures burdening intra-Community trade. In *Torfaen Borough,* the Court was asked to determine if the United Kingdom's Sunday closing laws violate European norms.[192] Under the applicable legal structure, the Court had to hold that the measures were a burden on trade, but that it would be justified if it furthered a valid

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[183] *Id.*

[184] *Id.* ¶ 65.

[185] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶¶ 54-70.

[186] *Id.* ¶¶ 53-54.

[187] *Id.* ¶¶ 5-7, 39, 48-51.

[188] *Id.* ¶¶ 162, 165, 215-17.

[189] *Id.* ¶¶ 137.

[190] *Id.*

[191] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶¶ 142-71.

[192] Case C-145/88, Torfaen Borough Council v. B & Q, 1989 E.C.J. CELEX LEXIS 6265.

government purpose.[193] It is evident, however, that the Court could not hold, while remaining consistent with democratic principles of separation of church and state, that the U.K. government could promote the Christian Sabbath.[194] That left a dearth of rationale for the government to justify its burdening of trade. In order to achieve its goal, the Court scrambled to explain that a single day of rest may properly be instituted to ensure that all workers are off at approximately the same time.[195] While disconnected from the reality of the Sunday closing law's purpose, this reasoning guaranteed that the law would remain in force and, more fundamentally, the ruling avoided a clash with the U.K. public that was weary of European domination and unwilling to give up local mores as a result of *laissez faire* trade pressures.[196]

Like *Torfaen Borough*, the *Loewen* case was the first challenge under Chapter 11 to a measure adopted by the United States.[197] As described above, there was an outcry in the United States against even the suggestion that a supranational tribunal could review sensitive domestic policies like punitive damages, tort liability, and justice.[198] It is true, critics admit, that the United States should engage in a debate over whether reforms should be adopted on those issues.[199] We should balance the extent to which our commitment to individual justice outweighs the efficient operation of businesses. We should think about due process, and whether punitive damages may be so overly disproportionate to the actual harm as to constitute an unacceptable punishment of the defendant. However, the critics would claim these are essentially domestic questions that an international panel may not legitimately determine.

In other words, in the *Loewen* case, the international system tapped

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[193] *Id.* ¶ 13.

[194] I heard the insight that the Court had to find a social objective for the measure separate from the furtherance of religion in a course taught from my teacher and mentor, Professor Joseph Weiler.

[195] *Torfaen Borough,* 1989 E.C.J. CELEX LEXIS 6265, ¶¶ 13-14.

[196] Fears in the United Kingdom might have been particularly relevant since this was the very first case to come out of the United Kingdom in this area of trade law.

[197] NAFTA Chapter 11's history of cases is relatively brief: S.D. Myers v. Canada, Partial Award (Nov. 13, 2000), *available at* http://www.dfait-maeci.gc.ca/tna-nac/documents/myersvcanadapartialaward_final_13-11-00.pdf; Pope & Talbot, Inc. v. Canada, Award of Damages (May 31, 2002), *available at* http://www.dfait-maeci.gc.ca/tna-nac/documents/damage_award.pdf; Metalclad Corp. v. Mexico, Award, ICSID Case No. ARB(AF)/97/1 (Aug. 4, 2000), *available at* http://www.economia-snci.gob.mx/sphp_pages/importa/sol_contro/consultoria/Casos_Mexico/Metalclad/laudo/laudo_ingles.pdf Another case involving U.S. regulatory practice, *Methanex v. United States*, succeeded *Loewen* and is still pending. First Partial Award (Aug. 7, 2002) *available at* http://www.state.gov/documents/organization/12613.pdf.

[198] *See, e.g.* PUBLIC CITIZEN, *supra* note 4.

[199] *Id.*

into a national debate over the extent to which certain practices are arbitrary, and it threatened to take an outlier case as the vehicle to impose an international norm on the debate. It was more prudent for the international system to let national actors carry on the debate. The judges must have recognized that a ruling against the United States would do more harm than good. It would have given the critics of the treaty an easy weapon to brandish: international law preempts the jury system, interferes with the proper administration of justice, and (yet again) favors the rich against the poor. In these circumstances, it was prudent for the tribunal to refrain from intervening.[200]

In addition, in *Loewen* as in *Mondev,* the international panels were asked to intervene in the affairs of the domestic judiciary.[201] Not only were the issues sensitive of their own right, but as the European experience demonstrates supranational law encounters greater risks of illegitimacy when it forces or threatens to force domestic judges and courts to change their normal course of operation. Administration of justice lies at the core of the domestic private law norms that international law may not displace without carefully considering the attendant legitimacy problems.[202] There should be a natural and healthy reflex in the good international judge that prevents her or him from unduly interfering with the work of national counterparts. That was a factor at work here as well.

However, as described in the next section, the panels should have explicitly articulated the basis for their decisions. An explicit articulation of the applicable norms would, as I explain below, resolve the legitimacy concerns inherent in a potential conflict between sensitive domestic norms and international standards that is adjudicated under ambiguous language, confine Chapter 11 to its proper place in the world of international trade and investment in light of the object and purpose of the treaty, and further the international common law enterprise.

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[200] This is not to say that a developed country like the United States gets to hold an internal debate over which practice is arbitrary in light of contemporary practice, while a less developed country like Mexico is banned from arguing that historical circumstances should inform what is arbitrary. The distinction is that *Loewen* was an example of a judicial practice that may be the byproduct of a system that is overall not arbitrary, in that it protects the rights of plaintiffs, and the United States should be free to decide, out of an internal debate, that the practice should be maintained despite the cost of freak occurrences such as *Loewen.*

[201] *Loewen* ICISD Case No. ARB/(AF)/98/3, ¶¶ 42-53, 122, 137; *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶ 75.

[202] *See, generally,* Caruso, *supra* note 133.

C. How *Loewen* and *Mondev* Could Have Been Drafted to Contribute to the Development of a Common Law Framework for Interpreting Chapter 11.

Chapter 11 suffers from a legitimacy problem because it threatens to displace domestic law if its interpreters do not resolve the ambiguity problems of the treaty. NAFTA is unlike classical trade agreements in that its dispute resolution mechanisms exist for the benefit of *private* parties, not the state.[203] Plaintiffs are broadly defined as foreign investors, while defendants are host governments. Each state actor party agrees to surrender some of its rights in exchange for the protection and security that accompanies membership to the polity at large.[204] Depending on how Chapter 11 is interpreted, supranational law may unduly favor the interests of investors over the domestic norms that they will challenge using the treaty.

These propositions are reflected in both *Mondev* and *Loewen*. The *Mondev* tribunal acknowledged that the plaintiff's argument against blanket statutory immunity had merit.[205] The *Loewen* tribunal came close to denouncing a whole range of state trial practices in the United States, especially since the tribunal determined that the corporate plaintiff was denied justice.[206] These arbitral decisions could have ushered in victories not only for the Canadian litigants involved, but for private interests generally. Every decision that favors (or at least sympathizes with) investors at the expense of government policies elevates the status of foreign enterprise in all three member states. That is, a victory for Canadian business over the U.S. government bodes well for the U.S. ventures in Canada and Mexico, should the parties' rights and privileges ever be called into question.[207] The flip side of this alignment, of course, is that NAFTA panels' construction of customary international law may invalidate countervailing domestic norms, thereby further polarizing the goals of government and business and the opposing sides in the debate over the legitimacy of Chapter 11.

In order to resolve this tension and to facilitate the cross border flow of investment without unsettling the equilibrium between domestic and

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[203] NAFTA, *supra* note 1; *see also* DUNOFF, *supra* note 44, at 811.

[204] I am of course making the assumption that, without NAFTA's Chapter 11, investment would not flow into the Mexican market. *See* Vandevelde, *supra* note 11.

[205] *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶ 151.

[206] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶ 137.

[207] *E.g.*, S.D. Myers, Inc. v. Canada (NAFTA Ch. 11 Arb. Trib. Award of Damages, Nov. 13, 2000), *available at* http://naftaclaims.com/disputes_canada/disputes_canada_sdmyers.htm (finding that Canadian legislation prohibiting toxic waste exports unfairly blocked a US competitor from entering the market). It should be noted, however, that the case was decided under national treatment, not customary international law.

international law, the tribunals should explicitly state their grounds for resolving the ambiguity inherent in Chapter 11. The *Mondev* and *Loewen* decisions could have been victories for a common law approach that would not only follow a teleological methodology, but also take the pulse of the extent to which the international law should take grounds within the domestic legal system, and at what pace. In order to refrain from falling prey to the pitfalls encountered (but avoided) in *Mondev* and *Loewen*, the NAFTA panels need to follow and explicitly articulate a methodology, such as the one advocated in this article, and to continue to reconstruct Chapter 11 in a way that comports with its object and purpose.

In addition to resolving ambiguity in Chapter 11's meaning and correlatively to resolving its legitimacy problem, such an approach would further the development of the "common law" in international trade.[208] Professor Joseph Weiler has observed that cross-fertilization among various international fields has been taking place with increasing frequency.[209] Since the world of private international law is no longer discretely divided into EU, NAFTA, or WTO specializations (among others), some ideas, aided by significant collaborative efforts, are surfacing in numerous contexts.[210] It is not inappropriate, therefore, to suggest that principles being employed in trade at large are also relevant to Chapter 11's provisions on investment.

If NAFTA were to examine these nascent common law principles, it would likely scale back the number and species of cases over which it asserts jurisdiction. A careful reading of *Mondev* and *Loewen* testifies to the tribunals' difficulty with adhering to NAFTA's charter while staying above the political fray.[211] But if NAFTA jurists reinvent their notion of how Chapter 11's provisions function to protect investors, they can sidestep, in large part, the interpretative problems addressed previously. If they accomplish this task, the NAFTA panels would revert back to their original object and purpose (i.e. commercial arbitration where cases with far-reaching implications are typically avoided). Then, NAFTA's panels might resemble conventional arbitral panels that resolve money disputes that do not implicate sensitive state interests. Adopting this approach would narrow Chapter 11's authority but deepen its legitimacy.[212]

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[208] TOWARDS A COMMON LAW, *supra* note 22.

[209] *Id.*

[210] *Id.*

[211] *E.g., Mondev*, ICSID Case No. ARB(AF)/99/2, ¶ 153; *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶¶ 137-38.

[212] *Cf.* Robert Howse, *Adjudicative Legitimacy and Treaty Interpretation in International Trade Law: The Early Years of WTO Jurisprudence, in* TOWARDS A COMMON LAW, *supra* note 22, at 59; Legitimacy Crisis, *supra* note 16. Howse's "institutional sensitivity" is an especially important marker of whether or not a trade area such as NAFTA is respecting its adjudicative bounds.

In concrete terms, the key to executing this shift of purpose is to focus on resolving cases where purely protectionist or arbitrary measures are at work, and not to entertain regulatory takings claims that go beyond what is actionable under local law. In addition, the panels should engage in a separate process, illustrated by the *Loewen* case, to evaluate any prudential consideration arising from the relationship between the national and international spheres that militate against intervention in domestic affairs.

Arbitrary or discriminatory measures may span a broad variety of subject matter areas. In each instance, a NAFTA tribunal would not be required to engage in a careful balancing test in which foreign investors' needs are weighed against an important national interest; by definition, an arbitrary act is one without justification and a discriminatory act furthers economic protectionism only—not an unrelated, valid state interest. In addition, the prudential level of the analysis will act as a safety net to ensure that, even when an action might be viewed as arbitrary or discriminatory (as in *Loewen*), the panel might still reject a claim because ruling in favor of the private parties would unsettle the balance between the domestic and the international realms.[213]

Unlike *Loewen* or *Mondev*, where intervention was inappropriate, the cases that are properly subject to Chapter 11 intervention do not necessitate a careful weighing of interests—national versus supranational, public versus private—which is best left to other adjudicative channels.[214] Adopting a more narrow view of its competence will enable Chapter 11 to regain its footing. Obviously, for those concerned about national sovereignty, an agreement to hear cases only when well-established, deeply entrenched practices are not being litigated would be welcome news. In addition, investors can still be adequately protected under NAFTA's auspices without having to guess whether or not tribunals will follow their own interpretations of the investment chapter. This kind of security is one that will sustain the treaty's viability over the long haul, as confusion and cynicism in North American business communities gradually subside.

These principles should be clearly articulated by panels, rather than inferred from the result after the fact. The tone of the panels' decision in *Loewen* and *Mondev* gives cause for hope.[215] The opinions were transparent, thoroughly researched and well-written. They were reminiscent of a well reasoned U.S. appellate court opinion. The issue of legitimacy has much to do with transparency and issuing judgments that

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[213] Legitimacy Crisis, *supra* note 16; *see also* Not in My Backyard, *supra* note 35.

[214] *See* Legitimacy Crisis, *supra* note 16. Outside of domestic legal remedies, cases that involve more complicated, nuanced clashes between trade values and social norms would probably be taken up by the WTO.

[215] *Loewen*, ICISD Case No. ARB/(AF)/98/3, ¶¶ 241-42; *Mondev*, ICSID Case No. ARB(AF)/99/2, ¶¶ 154-57.

have the hallmarks of those rendered by national courts. To that extent, the NAFTA panels did well in both cases. It remains necessary for them to explicitly articulate principles that will formally guide their decisions in future cases.

V. CONCLUSION

Chapter 11's legitimacy crisis was brought about by the potential for its broad construction of "investment" and, therefore, the broad jurisdiction it assumed over all kinds of commercial disputes—including those requiring the kind of strict scrutiny for which NAFTA jurists are not particularly well-suited.[216] As a result, natural tensions imbued in the treaty's structure were exacerbated; national, supranational, public, and private interests all seemed to be shortchanged. The very fact that decisions such as those in *Mondev* and *Loewen* were rendered brought the conflict to a head, further casting Chapter 11's usefulness into doubt.[217]

This article proposes a solution that may, over time, help to achieve Chapter 11's original object and purpose. As NAFTA looks south to the future FTAA, it is crucial to resolve any lingering ambiguities about the meaning of foreign investment. Borrowing concepts used in the larger world of international trade, I have suggested that Chapter 11 panels reduce their caseload by adjudicating only those disputes in which no important national (or public) objective, institution, or practice is at stake. If such a change can be agreed to, the three-state coalition may very well evolve into a more mature polity in its own right. And, equally important, it would help solidify the development of an international common law capable of negotiating boundaries in national and global contexts.

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[216] *See* Legitimacy Crisis, *supra* note 16, at 30-43.

[217] *See* PUBLIC CITIZEN, *supra* note 4; *NAFTA's Powerful Little Secret; Obscure Tribunals Settle Disputes, but Go Too Far, Critics Say*, *supra* note 8.