Trading Away Our Climate?
How Investment Rules Threaten the Environment and Climate Protection

Our planet is in trouble. Widespread deforestation has accelerated rates of biodiversity loss and soil erosion;[1] world fisheries are on the verge of collapse;[2] and climate disruption stands to destabilize world food supplies, undercut economic development, and threaten communities with extreme weather and sea level rise.[3] As we move toward planetary tipping points, strong climate policies, ambitious environmental laws, and decisive governmental action are desperately needed.

Unfortunately, right when we need active policymaking most, investment rules in bilateral investment treaties (BITs) and free trade agreements (FTAs) are restricting the ability of governments to set policies in the interest of the public. While foreign investment can be an important driver of economic development, current investment rules go too far in granting broad privileges to corporations at the expense of the public welfare and the environment. And, the most harmful of the investment rules stand to be expanded in the Trans-Pacific Partnership free trade agreement that the U.S. is currently negotiating with 11 countries across the Pacific Rim and in the Transatlantic Trade and Investment Partnership between the U.S. and the European Union (EU).[4]

Among the most harmful components of investment rules are vaguely worded provisions that guarantee investors a "minimum standard of treatment" and "fair and equitable treatment." When a corporation feels that its rights have been violated or the monetary value of its investment has been reduced by the introduction of a new law or policy, the investor-state dispute settlement mechanism allows foreign firms to bypass domestic court systems and sue governments in private trade tribunals that lack transparency and public accountability. Corporations have used investor-state dispute settlement provisions to challenge environmental, land-use, energy, and other socially beneficial laws passed by democratically elected governments.

To date, corporations have launched nearly 600 cases against nearly 100 governments.[5] Of the 274 cases that have been concluded, nearly 60% either settle or are decided in favor of the investor.[6] The impacts of these cases are harmful not only to the environment, but also to economies. In 2012, for example, the government of Ecuador was ordered to pay Occidental Oil nearly U.S. $2.4 billion including compound interest (described below).[7]

Finally, it is important to note that numerous studies have found no significant correlation between a country's level of foreign direct investment and its decision to adopt treaties with broad investor protections, including investor-state dispute resolution.[8] Moreover, there *is* significant evidence that broad investor protections threaten communities and the environment.[9]

The Rules

Investment rules have become a significant threat to the functioning of democracies, the safety of the public, and the protection of the environment. The following are some of the rules—only a subset of the standard investment rules included in FTAs and BITs—that have allowed foreign corporations to attack critical public interest measures.

Definition of Investment: The definition of investment in FTAs and BITs goes far beyond real property and capital investments and includes, for example, the "expectation of gain or profit." [10] This broad definition of investment opens up governments to a wide range of cases not even related to actual investments.

Minimum Standard of Treatment: Among the standard investment rules are provisions that guarantee investors "minimum standard of treatment" and "fair and equitable treatment." These vaguely worded provisions have been interpreted by some international tribunals as a standstill on regulation, meaning that governments are vulnerable to lawsuits from foreign corporations simply for introducing or amending laws and policies while an investor is present. For example, a ban on a chemical found to be harmful to the health of communities and the environment, or new regulations in the oil, gas, or coal industries, could be considered a violation of minimum standard of treatment and challenged by a corporation for financial compensation in a private trade tribunal.

Indirect Expropriation: Under today's investment agreements, foreign corporations are often protected from "indirect" expropriation, which can include laws or regulatory measures that merely reduces the value of a foreign firm's future expected profits.[11] For example, a new regulation in the natural gas industry which reduces the profits of an investor, such as additional permit requirements, could be considered not only a violation of fair and equitable treatment described above, but also expropriation.

Investor State Dispute Settlement: Perhaps the most damaging component of investment rules is the investor-state dispute settlement mechanism that allows foreign corporations to circumvent domestic courts and sue a host country's government in private trade tribunals. Not only do these tribunals give private corporations the same legal standing as democratically-elected governments, but they also lack transparency and public oversight.[12] Moreover, since there is no cap on the amount of damages a tribunal can award to a corporation, the mere threat of an investor-state suit can be enough to dissuade governments from enacting important public-protecting measures.

Illustrative Cases

These are not hypothetical dangers. In fact, current trends demonstrate that investor-state cases challenging public-interest regulations are quickly becoming the norm. Listed below are just a few investor-state suits that exemplify how investment rules can limit a government's ability to enact climate change measures, protect the environment, and ensure the safety of its people.

Fracking in Quebec

In September 2013, Lone Pine Resources, a U.S. oil and gas firm, filed its notice of arbitration against Canada for U.S. $250 million under the North American Free Trade Agreement (NAFTA).[13] The crime: A bill passed by Quebec's National Assembly that instituted a moratorium on shale gas exploration and development, including fracking, under the St. Lawrence River.[14] According to Lone Pine representatives, the Quebec government acted "with no cognizable public purpose," and violated the Enterprise's "valuable right to mine for oil and gas under the St. Lawrence River," despite the fact that the fracking process is known to contaminate

drinking water, pollute the air, and cause earthquakes.[15] Lone Pine, however, argues that its loss of a "stable business and legal environment" violated its minimum standard of treatment and should be counted as expropriation.[16]

Nuclear Energy in Germany

Following Japan's Fukushima Daiichi nuclear disaster of 2011, and in the midst of significant public pressure, the German Parliament made a decision to phase-out its nuclear power program and shift toward cleaner renewable energy sources. In response, Vattenfall, a Swedish energy firm with investments in German nuclear energy, filed a request for arbitration against Germany at the World Bank's International Centre for Settlement of Investment Disputes (ICSID).[17] Citing the fair and equitable treatment provisions of the Energy Charter Treaty, an EU trade and investment agreement for the energy sector, Vattenfall is now seeking US $4.6 billion in damages from the German people for future losses that it may sustain during the nuclear phase-out.[18]

Mining in Peru

In 1997, Doe Run Peru—a Peruvian subsidiary of the U.S.-based company, Renco Group Inc.—took control of a metallic smelter and refinery complex in La Oroya, Peru. La Oroya is one of the ten most polluted sites in the world. As part of its contractual and legal obligations, Doe Run was required to implement a series of environmental clean-up projects in La Oroya, including the installation of new sulfuric acid plants to help combat the pollution produced by its complex. The company, however, had twice failed to meet its contractual deadlines and had twice been granted extensions by Peruvian authorities to complete its environmental remediation obligations. When the Peruvian government failed to give Doe Run a third extension, Renco Group Inc. retaliated on behalf of its subsidiary by initiating an investor-state case against Peru under the U.S.-Peru FTA. The corporation claimed that the government's failure to grant Doe Run yet another time-consuming extension violated provisions in the U.S.-Peru FTA, including minimum standard of treatment and indirect expropriation protections. Instead of fulfilling its legal obligations to clean up the pollution caused by its metallic smelter and refinery complex, Renco Group Inc. is demanding U.S. $800 million from Peruvian taxpayers.[19]

Toxic Chemicals Ban in Canada

In 1995, Canada banned the export of Polychlorinated biphenyl, or PCB, wastes to the United States. PCBs are a group of man-made chemicals that were found to pose serious risks to human health and the environment. In response to the ban, S.D. Myers, Inc., an Ohio-based corporation that processes and disposes of PCB waste, filed an investor-state claim against Canada under NAFTA claiming violations to minimum standard of treatment, among other provisions. While Canada defended its measures as justified by environmental considerations, and despite the fact that Canada – as a signatory of Basel Convention, the multilateral environmental treaty on toxic-waste trade – was committed to banning the trade of toxics, the tribunal ruled in favor of SD Myers and ordered Canada to pay $5 million.[20]

Oil Exploration in Ecuador

In 1999, Occidental Petroleum Corporation signed a twenty-year contract with Ecuador for oil exploration and production rights in the Amazon forest. In accordance with Ecuador's laws on oil production, the agreement explicitly prohibited Occidental from selling its oil production rights without government approval, thereby providing the government officials the opportunity to evaluate any companies seeking to produce oil within Ecuador's national boundaries. The country had good reason to be cautious of foreign oil companies. For three

decades, Texaco, which Chevron later acquired in 2001, drilled for oil in Ecuador's Amazon rainforest, during which time it dumped over 18 billion gallons of toxic waste into the ecosystem.[21]

Just one year later, however, Occidental violated its contractual agreement (and Ecuadorian law) when it sold 40 percent of its production rights to Alberta Energy Company (AEC) without formally informing, or seeking authorization from, the Ecuadorian government. In response, Ecuador terminated its contract with Occidental, which prompted Occidental to initiate investor-state proceedings under the U.S.-Ecuador Bilateral Investment Treaty.[22] Although the investor-state court agreed that Ecuador was within its legal rights to annul the contract, the international tribunal ultimately sided with Occidental and fined Ecuador nearly U.S. $1.8 billion (U.S. $2.4 billion including compound interest), the largest investor-state award ever to be issued by an ICSID tribunal. The panel justified their decision by using an extremely broad interpretation of "minimum standard of treatment," "fair and equitable treatment," and "indirect expropriation."[23]

Conclusion

To address our environmental and climate crisis, governments must act quickly and decisively. Now, more than ever, governments need to have at their disposal a wide array of policy tools for promoting clean energy use, reducing reliance on fossil fuels, and protecting the environment.

The investment rules in many current and proposed free trade agreements and bilateral investment treaties threaten to undermine current environmental safeguards and constrain future climate policy action. By creating a system that privileges corporate profits over the well-being of communities and the environment, these investment rules have allowed foreign corporations to attack sound and democratic policymaking. A new model of trade and investment is urgently needed that provides governments with the unconstrained freedom to safeguard our environment, protect communities, and tackle climate change.

For questions or comments, or to get involved in Sierra Club's Responsible Trade Program, please write to Courtenay.Lewis@sierraclub.org

ENDNOTES

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[7] (UNCTAD). "Recent Developments in Investor-State Dispute Settlement." Also important to note that in an extreme example of investor-state litigation, in 2006 Argentina was sued by over 30 corporations for more than US$17 billion in compensation – an amount that rivals the government's national budget. Sources: UNCTAD "Latest Developments in Investor-State Dispute Settlement." *IIA Issue Note*, March, 2013. Accessible at: http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d3_en.pdf ; Tienhaara, Kyla. "Investor-State Dispute Settlement in the Trans-Pacific Partnership Agreement." *Submission to the Australian Department of Foreign Affairs and Trade*, May 19, 2010. Accessible at: http://www.dfat.gov.au/fta/tpp/subs/tpp_sub_tienhaara_100519.pdf

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