Columbia Center on Sustainable Investment
A JOINT CENTER OF COLUMBIA LAW SCHOOL AND THE EARTH INSTITUTE, COLUMBIA UNIVERSITY

Lise Johnson*
January 2015

Key Points

1. In 2014, the US again emerged the winner in investor- state arbitration.
2. Yet despite winning the case against it, the US lost on several important issues.
3. Those losses leave the US more vulnerable to future claims, litigation costs, and potential liability.

Table of Contents

New Weaknesses: Despite a major win, arbitration decisions in 2014 increase the US's future exposure to litigation and liability

1. Overview

The US Trade Representative's office has made a number of statements defending its push to include investor-state arbitration in its investment treaties, including the assertion that "[a]s a country that plays by the rules and respects the rule of law, the United States has never lost an [investor-state dispute resolution (ISDS)] case."[1] While technically true, this glosses over the US's vulnerability, as highlighted by several decisions involving the US and US treaties in 2014. The US did not lose a case, but did lose on important issues which not only resulted in the US having to bear certain costs of litigation,[2] but which will likely have the effect of increasing future investment claims against the country. Those claims, in turn, represent potential liabilities that, as cases

[1] Lise Johnson is the Investment Law and Policy Program Head at the Columbia Center on Sustainable Investment.

[2] The author is grateful to Jan Kleinheisterkamp, Howard Mann, Lisa Sachs, and Karl Sauvant for their helpful comments and suggestions.

have shown, can amount to billions of dollars.

This year-end review highlights four particular issues on which tribunals decided in favor of the investor, and rejected the contrary arguments of the United States. These issues, which arose in claims under the North American Free Trade Agreement (NAFTA), were (1) the meaning of the "relating to" jurisdictional test; (2) the meaning of the "treatment" element in particular causes of action on the merits; the (3) the scope of the "fair and equitable treatment" (FET) requirement; and (4) the ability of the state parties to provide tribunals with their views on issues of treaty interpretation. The tribunals' decisions on these issues resulted in an expanded view of the types of claims that can be brought under the NAFTA and minimized the role of the US and its treaty parties in influencing and shaping how tribunals interpret investment treaties.

Finally, this review also highlights a fifth issue in which a tribunal similarly decided in favor of the investor in a case against Peru under the US-Peru Free Trade Agreement. The tribunal's decision on this point chips away at the US's claim that its modern investment treaties provide adequate "mechanisms for expedited review of frivolous claims."[3]

2. *Apotex Holdings and Apotex Inc. v. United States*[4] -- Taking a broad view of the power of the tribunal to review trade issues and scrutinize discretionary decisions

In *Apotex Holdings and Apotex Inc. v. United States*, the claimants sought over $1 billion in damages[5] from the US after the US Federal Drug Administration (FDA) imposed an "Import Alert" on certain generic drugs manufactured in Canada and exported to the US. The "Import Alert" aimed to restrict entry and sale into the US market of drugs that were produced by two Apotex family facilities. The US imposed the Import Alert after FDA inspections of those two Canadian facilities identified serious and systematic non-compliance with good pharmaceutical manufacturing practices. In brief, the claimants argued that the "Import Alert" violated the fair and equitable treatment (FET) requirement under the NAFTA, and discriminated against them in violation of the NAFTA's national treatment and most-favored nation treatment obligations.

The "relating to" requirement

Among its arguments, the US countered that the claimants' grievances related to treatment of two Apotex manufacturing facilities located *in Canada* (the "Etobicoke" and "Signet" facilities), and not to any investments *in the* US, and were therefore not claims covered by the NAFTA. As emphasized by the US, Article 1101 of the NAFTA makes clear that Chapter 11 only applies to "measures adopted or maintained by a Party" that "relat[e] to" covered foreign investors or investments *in* the United States. The Apotex claims, the US asserted, did not pass that "relating to" test.

The meaning of "relating to" in the NAFTA had first been addressed in *Methanex v. United States*.[6] In that dispute, all three NAFTA states had made submissions to the tribunal emphasizing that the "relating to" requirement was a jurisdictional gatekeeper designed to ensure that the NAFTA's

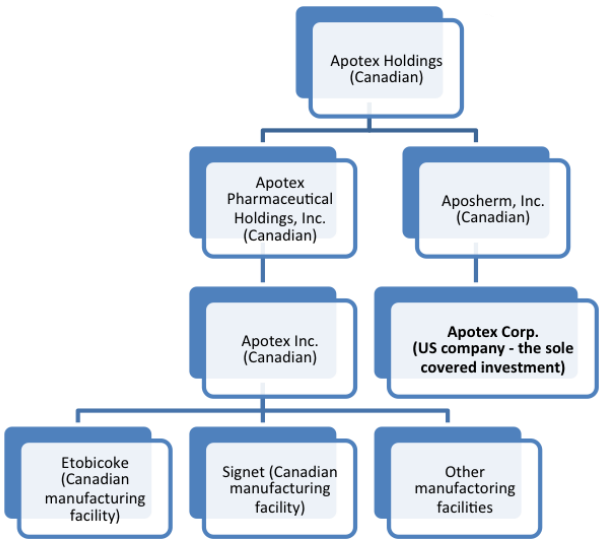
investment chapter did not provide foreign investors protection against measures that merely affected their investments in the US.[7] Rather, and as subsequently affirmed by the *Methanex* tribunal, there had to a "legally significant connection" between the measure and an investment in the US, or between the measure and the investor with respect to its investment.[8]

According to the US, the *Apotex* tribunal had no jurisdiction over the dispute because the Import Alert did not "relate to" or have any "legally significant connection" with Apotex Holdings as an "investor" in the country, nor did it "relate to" or have any "legally significant connection" with any "investment" in the United States.

The claimants argued that the Import Alert in fact "relat[ed] to" investments in the US. They emphasized that those US investments were (1) certain intellectual property rights in the US (i.e., abbreviated new drug applications (ANDAs)) directly held by Apotex Inc. and indirectly held by Apotex Holdings; and (2) Apotex Corp., a US-based subsidiary of Apotex Holdings that had been set up to market and distribute drugs in the US including, in particular though not exclusively, drugs produced by other Apotex companies such as the Etobicoke and Signet Canadian manufacturing facilities.

Siding with the US, the tribunal determined that the ANDAs were not "investments" in the US.[9] Consequently, the only "investment" at issue in the dispute was Apotex Corp., a US-based marketing and distribution subsidiary of Apotex Holdings; similarly, the only investor with an investment in the US was Apotex Holdings. That left the question of whether the Import Alert – a measure that was taken to control imports of adulterated pharmaceutical products produced in Canadian drug manufacturing facilities – was sufficiently "relat[ed] to" the relevant investor (Apotex Holdings) or its investment (Apotex Corp.) in order to trigger jurisdiction under the investment treaty.

Figure 1: Apotex Holdings Corporate Structure (relevant firms)



The tribunal found that it was. Although the disputing parties agreed that the "relating to" requirement involved more than an inquiry into the mere effects of a measure,[10] it was precisely the impacts of the Import Alert on Apotex Corp. that seemed to be the key reason behind the tribunal's

determination that the "relating to" requirement had been met. Even though other US-based firms were also affected by the Import Alert, and even though Apotex Corp. could have marketed and distributed pharmaceutical products from other Apotex and non-Apotex companies (and in fact did so), the tribunal considered the Import Alert's impact on Apotex Corp. to be sizeable and disparate enough as compared to other firms to satisfy the "relating to" requirement. According to the tribunal, there was no "warrant for interpreting NAFTA Article 1101(1) so narrowly as to require [Apotex Corp.] to be the exclusive purchaser of all Apotex Inc.'s products for the USA or Apotex Inc. to be [Apotex Corp.'s] sole supplier in the USA."[11] In the tribunal's view, the fact that Apotex Corp. was "by far the enterprise most immediately, most directly and most adversely affected by the Import Alert… suffice[d] to satisfy" the "relating to" test.[12]

An implication of this holding is that if a manufacturer of goods or services from one NAFTA state wants to obtain protections offered under the NAFTA's investment chapter for treatment of its exports, it can do so by establishing an investment in an importing NAFTA state to be the primary marketer or distributor of those products. As the US argued before the tribunal, this blurs the line between trade and investment disputes and gives the NAFTA's investment chapter a broader scope than had been intended.[13] Post-*Apotex*, there will thus likely be a rise in companies using their "corporate relatives as a kind of Trojan horse" to challenge trade-related measures under the NAFTA's investment chapter.[14]

The meaning of "treatment"

In reaching its conclusion on the meaning of "relating to", the tribunal showed its reluctance to interpret Article 1101 as imposing a strict test on jurisdiction. The jurisdictional phase, the tribunal reasoned, was not the place for such an inquiry into the relationship between the measure and the covered investor or investment. According to the tribunal, it would be "inappropriate to introduce within NAFTA Article 1101(1) a legal test of causation applicable under Chapter Eleven's substantive provisions for the merits of the Claimants' claims."[15]

The tribunal thus distinguished between jurisdiction and the merits, and indicated that analysis of the causal link between the measure and investor or investment would not happen in the former phase, but would happen in the latter. Nevertheless, when examining whether the required connection between the measure and the covered investor or investment was present for the purpose of establishing a violation on the merits, the tribunal did not conduct that additional causal analysis. Instead, the tribunal merely reused its jurisdictional "relating to" reasoning.

Specifically, in its substantive provisions, the treaty has additional language on the required relationship between the measure and the investor/investment. Establishing that there has been a breach of the national or most-favored nation treatment obligations at issue in the case, for instance, requires establishing that there has been (1) discriminatory (2) "treatment" of (3)(a) an investment or (3)(b) an investor with respect to its investment. Breach of the FET requirement similarly requires there to have been unfair or inequitable "treatment".

In its briefs, the US argued that the Import Alert on the products based on the operations of the Canadian facilities did not accord any "treatment" (much less any discriminatory or unfair or inequitable treatment) to US-based Apotex Corp., nor did it accord "treatment" to Apotex Holdings with respect to its investment in Apotex Corp. Yet rather than explore the meaning of the word "treatment" as used in the treaty's substantive obligations, the tribunal simply referred to and incorporated its discussion on the "relating to" requirement.

According to the tribunal, the fact that the measure was "relat[ed] to" the investor or investment for the purposes of the jurisdictional test meant that the measure accorded "treatment" to the investment, or the investor with respect to its investment, for the purposes of analysis on the merits.[16] This is notable given that the tribunal's interpretation of the "relating to" requirement was specifically influenced by the provision's role as a *jurisdictional* gatekeeper; the tribunal rejected the US's argument that the "relating to" test required analysis of causal links,[17] indicating that such analysis was better left for the merits phase. Its reliance on the "relating to" test as the basis for determining there had been "treatment" thus meant both that that the word "treatment" never received independent consideration as an element of the NAFTA's substantive obligations, and that analysis of the causal relationship between the measure and the investor or investment in fact never occurred.

By allowing the investor to pass the "relating to" test on jurisdiction, and then holding that the investor had satisfied the "treatment" element on the merits, the tribunal deemed that it had the power to scrutinize the US's decision to impose the Import Alert. Furthermore, in applying that scrutiny, it adopted a flexible and wide view of its authority to review the government's actions. In particular, rather than focusing specifically on whether Apotex Corp., the sole investment at issue in the dispute, received discriminatory treatment in violation of the national treatment and most-favored nation treatment obligations, or whether Apotex Holdings had received discriminatory treatment with respect to that investment, the tribunal scrutinized facts and arguments regarding whether and why the two manufacturing facilities *in Canada* indirectly owned by Apotex Holdings were treated differently by the FDA than manufacturing facilities in the United States (for the purpose of the national treatment analysis) or manufacturing facilities located in third countries (for the purpose of the most-favored nation treatment analysis). As those two Apotex Canadian manufacturing facilities are neither investments in the United States nor investors with investments in the United States, it is unclear why the "treatment" accorded to them, even if arbitrary or discriminatory, would establish a national or most favored nation treatment claim under the NAFTA. The simple fact that a US-based corporate affiliate of the Canadian manufacturers stood to be disproportionately affected by the Import Alert appeared to be the sole hook that justified the tribunal's scrutiny of how the US treated those foreign-based companies.

Through its liberal interpretations of the terms "relating to" and "treatment", as well as its conflation of all of the various members of the Apotex corporate family, the tribunal's decision signals that the NAFTA and other investment treaties provide an avenue for claims that may arise when the products of a foreign manufacturer or supplier are restricted or banned (whether due, e.g., to the safety of the

products or the processes or production methods through which they are manufactured) and that foreign manufacturer or supplier has a corporate affiliate in the host state that is primarily (but not necessarily exclusively) responsible for marketing or distributing the affected products.

Scrutiny of prosecutorial discretion

In its national treatment and most-favored nation treatment claims, the claimants argued that the US violated the treaty's non-discrimination obligations by imposing the Import Alert on Apotex's products but not taking similarly strong enforcement actions against other drug manufacturers found to have comparable problems. The tribunal analyzed evidence on US laws, policies and practices regarding regulation of foreign pharmaceutical manufacturing facilities, and then agreed with the claimants that the US had in fact treated the Canadian manufacturers less favorably than other foreign companies also found to have violated manufacturing standards.

According to the tribunal, because the claimants had established de facto discrimination, the claimants would prevail on their most-favored nation claim *unless* the US could provide satisfactory evidence to establish that it had legitimate reasons for treating Apotex's Canadian facilities differently from other sub-standard performers located overseas.[18] The claimants, the tribunal stated, were not required to prove discrimination on account of nationality in order to succeed on their claims. Rather, the burden of proof shifted on to the US to establish the legitimacy of its actions. If the US could not meet that burden, a breach of the treaty would be found.

Particularly in cases such as the *Apotex* dispute where rules of privilege, protection of confidential business information, and exercises of prosecutorial discretion can make clear explanations difficult to produce, this obligation to provide the tribunal with a satisfactorily legitimate reason for treating one company differently from another may not be easy for respondent governments to satisfy. Ultimately, in *Apotex*, the tribunal concluded that the US established sufficient evidence that the FDA's actions were "materially influenced by the FDA's genuine concerns" about public health.[19] While the tribunal did not clearly explain whether or what level of deference it applied to the government's explanations, the tribunal's willingness to scrutinize the actions of the FDA absent evidence of the agency's bad faith or intentional discrimination, and the tribunal's use of the qualifiers "materially" and "genuine", suggest a relatively heightened standard of review.

This stands in notable contrast to the weight of US jurisprudence. Due to the doctrine of separation of powers,[20] the "discretionary function" exemption to the Federal Tort Claims Act,[21] the myriad rules addressing judicial review of administrative actions or inactions that are set forth in the Administrative Procedure Act and case law interpreting it,[22] the deliberative process privilege,[23] and other laws and doctrines,[24] court scrutiny of administrative decisions is carefully governed and often highly circumscribed. Nevertheless, when a measure is challenged under an investment treaty, those mandatory rules on deference to agency decisionmaking, judicial standards of review, and privilege that apply in the context of domestic law to prevent US courts from reaching too far into the realm of

administrative expertise and policy decisions do not apply to arbitral tribunals.[25]

Apotex thus signals that companies challenging FDA or other agency enforcement action can use the NAFTA to subject government decisions to a different type and level of scrutiny than permitted under US law. Moreover, the decision indicates that to establish a violation under the national or most-favored nation treatment obligations, the claimant is not required to prove nationality-based discrimination. Once a claimant can establish treatment of itself or its products that is de facto different from treatment of another company or its products, the burden shifts to the government to establish the legitimacy of any different treatment; and the tribunal – operating under unclear and not necessarily deferential standards of review – becomes the ultimate arbiter of whether the government's actions were indeed legitimate.

Fair and equitable treatment of investors?

Article 1105 of the NAFTA states:

> Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.

In response to the claimants' arguments that the Import Alert violated that provision, the US argued that Article 1105, by its terms, only governs treatment of "investments" (i.e., Apotex Corp.). Wrongful treatment of "investors" (i.e., Apotex Inc. or Apotex Holdings) is, according to the US, not covered by that treaty provision.[26]

The tribunal declined to address that argument; accordingly, the tribunal scrutinized the US government's policies and practices regarding the Import Alert placed on the products produced by the Etobicoke and Signet facilities as opposed to more specifically identifying whether there was any allegedly wrongful treatment of Apotex Corp., the only covered investment at issue in the dispute. Had the tribunal limited itself to considering only the treatment accorded to the investment, Apotex Corp, as the US had argued, its inquiry into the government's conduct would have been much more narrowly circumscribed; however, by interpreting the provision to include investors -- and therefore, in this case, Apotex Holdings and Apotex, Inc., and those companies' manufacturing facilities in Canada -- the tribunal assumed much broader powers to review the government's conduct.

By adopting that approach and not ruling on the scope of the FET obligation, the tribunal's decision signals that other companies can similarly seek to use the FET provision to challenge actions of the FDA (or other government agencies or branches) that are primarily targeted at actors or activities outside of the US. This raises many questions regarding whether and in what circumstances tribunals will entertain claims that actions or omissions by US agencies, the legislature, or courts directed at foreign individuals or entities give rise to investment treaty

claims when those government actions or omissions have an effect on the targeted individuals' or entities' investments in the US.

3. The power of treaty parties v. the power of the tribunal

Apotex – *The relevance of the treaty parties' agreement*

In 2001, the NAFTA parties, through their Free Trade Commission (FTC), issued an interpretation of Article 1105.[27] The FTC interpretation, which is binding on NAFTA tribunals,[28] clarifies that the fair and equitable treatment obligation as used in NAFTA Article 1105 prescribes the customary international law minimum standard of treatment (MST), and does not require any standard of treatment that goes beyond what is required under that MST. In order to circumvent that clarification and seek the protections of an arguably higher standard of treaty protection, the claimants sought to use the NAFTA's most-favored nation provision to import from the US-Jamaica bilateral investment treaty (BIT) a fair and equitable treatment provision that has not been expressly tethered to the MST.

The US, in response, argued that the most-favored nation obligation cannot be used to alter the substantive content of Article 1105 by importing provisions from other treaties.[29] It also highlighted that the other NAFTA parties shared the same view.[30]

Rather than evaluate the NAFTA parties' positions or the legal significance of agreement among the three states on the issue,[31] the tribunal proceeded to evaluate the claimants' claims under the US-Jamaica BIT as if the most-favored nation provision could in fact be used to import more favorable standards of protection. "[W]hether the NAFTA Parties [were] correct" in their interpretation that the most-favored nation provision could not play such a role would, according to the tribunal, "have to await the decision of another NAFTA tribunal."[32] The tribunal did not give any reasons for declining, itself, to consider the contested issue.

By adopting this approach, the tribunal left the door conspicuously open for other claimants to seek to similarly use the most-favored nation provision to import substantive protections from other treaties. If, in contrast, the tribunal had decided that such importation was not permitted, the *Apotex* award would likely have discouraged reliance on those most-favored-nation-based arguments in other NAFTA cases. Even though there is no system of binding precedent in investment arbitration, an award in one NAFTA case has *de facto* authority and relevance in other NAFTA arbitrations; and the effect of this decision on other disputes, if anything, will be to increase efforts to use the most-favored nation provision as an importation tool, and to generate future litigation on whether that is allowed.

Furthermore, by so summarily disregarding the NAFTA parties' position on whether the most-favored nation provision can be used to expand protections under their treaty, the tribunal

failed to give due consideration and legal weight to the ongoing and important roles of states in shaping interpretation of the treaties they have concluded.[33] By simply punting to another tribunal the question of whether the US, Canada and Mexico were "correct" in their understanding of the treaty, the tribunal missed an important opportunity to engage with those countries and establish additional clarity in NAFTA jurisprudence.[34]

In order to avoid other "importation" arguments, the NAFTA parties may wish to again invoke the FTC and issue a binding statement on the proper role of the most-favored nation provision.

Detroit International Bridge Co. (DIBC) v. Canada[35] *and state-party access to hearings*

In another NAFTA case, *DIBC v. Canada*, the tribunal appeared to be similarly unmoved by state-parties' interest in shaping interpretation of their treaties, and their special rights under international law to do so. In an apparent first in a NAFTA case, the tribunal issued a procedural order denying the request of one NAFTA party (the US) to attend hearings in a NAFTA dispute against another treaty-party (Canada).[36]

Canada had supported the request for the US to attend; DIBC opposed it.[37] The US asked the tribunal to reconsider its order excluding the government from the *DIBC* hearings. The US emphasized that, under Article 1128 of the NAFTA, non-disputing parties to the treaty have the right to make submissions to the tribunal on issues of treaty interpretation. Nothing in Article 1128, the US further noted, required that the submissions be in writing. The US also argued that, in order to ensure the NAFTA parties could effectively exercise their Article 1128 rights (whether through oral or written submissions), the non-disputing state parties needed to be able to attend hearings in NAFTA disputes to stay abreast of arguments and respond as necessary.[38] Canada and Mexico likewise made submissions to the tribunal indicating that they shared the same interpretation of Article 1128.[39]

Despite the NAFTA parties' agreement on the issue of their treaty rights to attend NAFTA hearings, the tribunal did not modify its order. Instead, it simply noted that the non-disputing state parties could *request* access to transcripts of the hearings in order to be able to make future *written* submissions on issues of interpretation.[40] The tribunal thus rejected the state parties' contentions that non-disputing states have a *right* to receive information submitted during hearings whether by attending the hearings or obtaining the transcripts, and that they have a *right* under Article 1128 to make oral submissions to the tribunal. In doing so, the tribunal showed itself to be unpersuaded by the "basic premise" under international law that "states are the masters of their treaties" and have the power to shape the interpretation of those instruments through agreement and practice.[41]

To avoid future instances in which the tribunal limits the ability of non-disputing state parties to attend and make submissions in hearings on issues of interpretation, NAFTA parties may want to invoke the FTC mechanism on this issue as well to give binding direction to future

tribunals.

4. *Renco v. Peru* and dismissal of meritless claims

In another decision issued in 2014, the tribunal in *Renco v. Peru*[42] ruled on an issue of first impression in the US-Peru Free Trade Agreement (FTA), narrowly interpreting a clause providing respondent states an avenue to seek early dismissal of certain claims. Because this clause can be found in a number of other treaties concluded by the US such as the US-DR-CAFTA, the decision in *Renco v. Peru* may affect the US and other respondent states' abilities to use that early-dismissal mechanism in disputes arising under those agreements.

The clause, which is contained in Article 10.20.4 of the US-Peru FTA, reads:

> Without prejudice to a tribunal's authority to address other objections as a preliminary question, such as an objection that a dispute is not within the tribunal's competence, a tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favor of the claimant may be made under Article 10.26.

The treaty also states that:

> In deciding an objection under [Article 10.20.4], the tribunal shall assume to be true claimant's factual allegations in support of any claim in the notice of arbitration (or any amendment thereof) and, in disputes brought under the UNCITRAL Arbitration Rules, the statement of claim referred to in Article 18 of the UNCITRAL Arbitration Rules. The tribunal may also consider any relevant facts not in dispute.[43]

The US began negotiating for insertion of those clauses after the dispute in *Methanex*. In that case, the US had raised various objections to the claimant's claims that the US argued could have speedily disposed of the case. The tribunal, however, ruled that it did not have the authority to decide on those objections as a preliminary matter, and instead postponed their resolution to a full decision on the merits and jurisdiction.[44] While the US was ultimately successful in the case, its victory came only "after three more years of pleading on jurisdiction and merits and millions of dollars of additional expense" to the government.[45]

In order to avoid similar wastes of time and expense, the US has included Article 10.20.4-type provisions in all post-*Methanex* treaties that the US has concluded. According to the US, this provision is similar to what is "used in the U.S. courts to dispose quickly" of frivolous claims.[46] Article 10.20.4 is most frequently analogized[47] to Rule 12(b)(6) of the US's Federal Rules of Civil Procedure, which permits defendants to secure early dismissal of all or part of complaints that fail "to state a claim upon which relief can be granted." Rule 12(b)(6) dismissals can be used, for example, when complaints do not state required elements of the relevant cause of action, or

when claims fall outside of the applicable statute of limitations. Similar to the procedure under Article 10.20.4, when deciding a Rule 12(b)(6) motion, courts take all facts alleged by the plaintiff in its pleadings to be true and determine whether there is "sufficient factual matter" to "state a claim to relief that is plausible on its face."[48] If no such plausible claim is stated in the complaint, the complaint is dismissed on the merits. If a 12(b)(6) motion is denied, the defendant can raise the complaint's alleged failings during other phases of the dispute such as in a motion for summary judgment or at trial.

Motions for early dismissal on other grounds, such as whether the claim is properly before the federal court (i.e., whether there is "subject matter jurisdiction") or whether the court has jurisdiction over the defendant (i.e., whether there is "personal jurisdiction") are governed under different rules of procedure, namely Rule 12(b)(1) and 12(b)(2) of the Federal Rules of Civil Procedure.

In *Renco v. Peru*, Peru sought to use Article 10.20.4 to seek dismissal of Renco's claims on various grounds: (1) presentation of an invalid waiver; (2) violation of the waiver; (3) lack of jurisdiction *ratione temporis*; (4) violation of the treaty's three-year limitations period; (5) failure to state a claim for breach of the investment agreement; and (6) failure to submit two factual issues for determination by a technical expert prior to commencement of the arbitration. According to Peru, Article 10.20.4 was broad, and could be used to raise objections to the tribunal's "competence" as well as other legal failings of the complaint.

Renco, in contrast, sought a narrower reading of Article 10.20.4. It argued that objections as to "competence" could not be raised under Article 10.20.4's mechanism and that all of Peru's objections except for one (#5 above) were objections to "competence" that could not be brought under Article 10.20.4's pre-discovery avenue for dismissal. In its submissions, Renco relied on the US Federal Rules of Civil Procedure; according to Renco, Article 10.20.4 was modeled off of Rule 12(b)(6) and, just as Rule 12(b)(6) is not used to address objections to "subject matter jurisdiction", Article 10.20.4 is not used to address objections to "competence".[49]

In a non-disputing party submission, the US provided the tribunal with its views on the meaning of the contested provision. It agreed with Renco that Article 10.20.4 does not cover objections as to "competence". Nevertheless, the US did not explain what it considered an objection as to "competence" to include, nor which, if any, of Peru's objections were covered by Article 10.20.4.

The tribunal agreed with the US and Renco that Article 10.20.4 does not cover objections to "competence", and explained that it viewed objections to "competence" as including both objections to jurisdiction and admissibility. It then determined that none of Peru's objections except its objection that the claimant had failed to "state a claim for breach of the investment agreement" could proceed under Article 10.20.4.

By determining that all but one of Peru's objections were "competence" objections not within the scope of Article 10.20.4, the tribunal narrowed the provision beyond even the reach of Rule 12(b)(6). Under US law, for example, a defendant can use Rule 12(b)(6) motions (as opposed to Rule 12(b)(1) motions for lack of subject matter jurisdiction) to seek dismissal of claims on the ground that they were filed outside of the relevant statute of limitations.[50] Peru had argued that the claimant's claims failed in part because they were brought outside of the treaty's three-year limitations period. That argument – a 12(b)(6) argument under US law for failure to state a claim upon which relief can be granted – was deemed by the tribunal to be a "competence" objection falling outside of Article 10.20.4. Similarly, under US law, defendants can use Rule 12(b)(6) motions for failure to state a claim to seek dismissal of claims when prerequisites to filing suit had not been met.[51] According to the *Renco* decision, however, Peru's request for dismissal on the ground that certain prerequisites to suit had not been met were "competence" objections that could not be brought under Article 10.20.4.

Assuming the *Renco v. Peru* tribunal's approach to the meaning of "competence" objections is followed in other decisions, that early-dismissal provision may be of much less use to respondent states than Rule 12(b)(6) (or any other 12(b) motion) is to defendants in US federal court proceedings. Similarly, assuming that "competence" objections do, as the *Renco* tribunal concluded, include objections to "jurisdiction" and "admissibility", that would arguably sweep in *all* objections that the US had tried to raise on a preliminary basis in *Methanex*, and render Article 10.20.4 useless as a tool for seeking speedy resolution of those issues.[52] The decision in *Renco* thus raises the question of whether US treaties post-*Methanex* actually include "provisions similar to those used in U.S. courts to dispose quickly of claims a tribunal finds to be frivolous."[53]

5. Conclusion

As the US has emphasized, it has yet to lose an investor-state arbitration. In 2014, it secured a significant victory with its largely successful outcome in *Apotex*. Nevertheless, it lost on certain important issues that will likely be adverse to the US's interests as a respondent state in future cases.

For one, over the US's objection, the *Apotex* tribunal took a broad view of the scope of allowable claims under US treaties, signaling that other largely trade-related disputes can be readily framed as investment disputes. Additionally, and again over the US's objection, the tribunal adopted a flexible approach to assessing treatment of a corporate family, allowing investment law claims to be based on actions targeting foreign companies when those actions have disparate impacts on corporate family members in the US. As a result of the *Apotex* decision, the US is likely to face additional trade-related or corporate-family-related claims under the NAFTA or other investment treaties, subjecting a greater range of policies, laws and decisions to the potential scrutiny of investment tribunals than the US intended.

Moreover, while *Apotex* increased the US's vulnerability to future claims, the decision in *Renco* will limit the grounds on which respondent states can seek and secure speedy dismissal of claims that are legally meritless. Together, these 2014 decisions thus broadened the US and its treaty parties' exposure to increased investment arbitration claims and litigation expenses.

Increased claims and litigation will not necessarily lead to increased liability. Yet, the risk of liability rises when, as shown by the *Apotex* and *DIBC* tribunals, arbitrators do not feel bound to accord adequate weight to input by states on the meaning of their investment treaties. Both of those cases revealed tribunals remaining unmoved by the three NAFTA parties' agreement on different issues of interpretation, ignoring the states' position on the role of the most-favored nation position and rejecting their arguments on the rights of non-disputing parties to make submissions to the tribunal. Those approaches leave state parties in a weak position vis-à-vis tribunals, with minimal power to shape or anticipate how their own treaties will be interpreted. In order for governments to ensure that arbitrators give treaties the meaning that the state signatories intend, the US and its treaty parties may need to increase their use of the FTC mechanism under the NAFTA or similar mechanisms under other treaties to issue interpretations that are binding on tribunals. And in the case of treaties without those provisions, the US and its treaty parties are left with little assurance of their ability to influence or even predict investment treaty jurisprudence.

---

[1] Office of the United State Trade Representative, Press Office Blog, The Facts on Investor-State Dispute Settlement: Safeguarding the Public Interest and Protecting the Investment, March 27, 2014.

[2] The disputing parties in *Apotex Holdings Inc. and Apotex Inc. v. United States*, ICSID Case No. ARB(AF)12/1, had agreed that the tribunal should follow a "loser pays" principle with respect to the parties' legal fees. The claimants were thus required to pay the US's legal costs and expenses incurred in defending the NAFTA dispute. However, the tribunal required the US to pay 25% of the arbitration costs based on the fact that the US lost some of its jurisdictional objections. The arbitration costs included fees and expenses for members of the tribunal, and expenses and charges of the ICSID Secretariat. The final amount of those expenses was to be calculated after the award was rendered. At the time of the award, it amounted to US$350,000.

[3] Office of the United State Trade Representative, Press Office Blog, The Facts on Investor-State Dispute Settlement: Safeguarding the Public Interest and Protecting the Investment, March 27, 2014.

[4] Apotex Holdings Inc. and Apotex Inc. v. United States, ICSID Case No. ARB(AF)12/1, Award (Aug. 25, 2014) (hereinafter "*Apotex*").

[5] *Apotex*, Hearing on Jurisdiction and the Merits, Nov. 25, 2014, p. 1516, lines 9-21.

[6] Methanex Corp. v. United States of America, NAFTA/UNCITRAL, First Partial Award (Aug. 7, 2002).

[7] *Apotex*, US Counter-Memorial and Objections to Jurisdiction, paras. 265-271.

[8] Methanex Corp. v. United States of America, NAFTA/UNCITRAL, First Partial Award, para. 147 (Aug. 7, 2002)

[9] In reaching this conclusion, the tribunal applied the reasoning of a previous NAFTA tribunal in a separate, likewise unsuccessful, claim brought by Apotex, Inc. against the US, *Apotex Inc. v. United States*, UNCITRAL, Award, June 14, 2013, paras. 206-225. *Apotex*, Part VII.

[10] *Apotex*, para. 6.13.

[11] Id. para. 6.25.

[12] Id. para. 6.24.

[13] *Apotex*, Hearing on Jurisdiction and the Merits, November 18, 2013, pp. 30-32, 38-40.

[14] Id. p. 39.
[15] *Apotex*, Award, para. 6.20.
[16] Id. para. 8.14 ("Having regard to the Tribunal's decision in Part VI above under NAFTA Article 1101(1) to the effect that the Import Alert 'related to' Apotex-Holdings and Apotex-US, the Tribunal concludes that the Import Alert qualifies as 'treatment' for the purposes of NAFTA Articles 1102 and 1103.").
[17] See, e.g., *Apotex*, US Counter-Memorial, paras. 200, 212-214.
[18] *Apotex*, para. 8.65.
[19] *Apotex*, paras. 8.71 and 8.73.
[20] The US Supreme Court examined the issues of prosecutorial discretion and separation of powers in *Wayte v. United States*, 470 U.S. 598, 607 (1985), a case arising in the context of criminal prosecution. While noting that there were certain constitutional limits on the scope of prosecutorial discretion and therefore a role for some judicial oversight, the court emphasized that there are various policy considerations supporting judicial restraint in reviewing challenges to executive decisions:

> Such factors as the strength of the case, the prosecution's general deterrence value, the Government's enforcement priorities, and the case's relationship to the Government's overall enforcement plan are not readily susceptible to the kind of analysis the courts are competent to undertake. Judicial supervision in this area, moreover, entails systemic costs of particular concern. Examining the basis of a prosecution delays the criminal proceeding, threatens to chill law enforcement by subjecting the prosecutor's motives and decisionmaking to outside inquiry, and may undermine prosecutorial effectiveness by revealing the Government's enforcement policy. All these are substantial concerns that make the courts properly hesitant to examine the decision whether to prosecute.

Id. at 607-08.
[21] The "discretionary function exemption" provides that the government is not liable for:

> any claim based upon an act or omission of an employee of the Government, exercising due care, in the execution of a statute or regulation, whether or not such statute or regulation be valid, or based upon the exercise or performance or the failure to exercise or perform a discretionary function or duty on the part of a federal agency or an employee of the Government, whether or not the discretion involved be abused.

28 U. S. C. § 2680(a). "[T]he purpose of the exception is to 'prevent judicial "second-guessing" of legislative and administrative decisions grounded in social, economic, and political policy through the medium of an action in tort.'" United States v. Gaubert, 499 U.S. 315, 323 (1991) (internal citations omitted).
[22] The Administrative Procedures Act (APA) governs judicial review of agency action unless judicial review is precluded by statute or agency action is committed to agency discretion by law. 5 USCS § 701. See also 5 USCS § 706 (setting forth the different grounds under which courts are to compel or set aside agency action).
[23] In brief, the deliberative process privilege is a qualified privilege that protects from discovery "intra-governmental pre-decisional documents 'reflecting advisory opinions, recommendations, and deliberations comprising part of a process by which governmental decisions are formulated.'" Ford Motor Co. v. United States, 94 Fed. Cl. 211, 217 (Fed. Cl. 2010) (quoting NLRB v. Sears, Roebuck & Co., 421 U.S. 132, 150, 95 S. Ct. 1504, 44 L. Ed. 2d 29 (1975) (internal quotations omitted)). The privilege restricts the ability of reviewing courts and private citizens to scrutinize the contents of agency deliberations. It has been described as serving three main functions: (1) "protecting candid discussions within an agency," (2) "preventing public confusion from premature disclosure of agency opinions before the agency established its final policy," and (3) "protecting the integrity of an agency's decision [, in that] the public should not judge officials based on information they considered prior to issuing their final decisions." Cobell v. Norton, 213 F.R.D. 1, 4 (D.D.C. 2003) (internal citations omitted). See also In re Subpoena Duces Tecum Served on the Office of the Comptroller of the Currency, 156 F.3d 1279, 1279-1280 (D.C. Cir. 1998) (discussing application of privilege to claims that agency action was arbitrary and capricious).
[24] Some provisions of environmental laws state specifically that persons cannot challenge the actions of executive environmental agencies if the action is a discretionary one. See, e.g. Clean Air Act § 304, Pub.L. No. 91-604, § 12(a), 84 Stat. 1676, 1991-92 (1970) (current version at 42 U.S.C. §§ 7604(a)(2) (2012)) ("Except as provided in subsection (b), any person may commence a civil action on his own behalf— . . . against the Administrator where there is alleged a failure of the Administrator to perform any act or duty under this Act which is not discretionary with the

Administrator.") (emphasis added). These provisions make it extremely difficult to bring actions against agencies. However, courts have the ability, so long as a statute does not foreclose judicial review, to set aside agency actions if they are found to be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." Administrative Procedure Act § 706(2)(A).

[25] When addressing the claimants' fair and equitable treatment claims, the tribunal noted its agreement with another NAFTA tribunal's statement that, "[w]hen interpreting and applying the 'minimum standard', a Chapter 11 tribunal does not have an open-ended mandate to second-guess government decision making." Apotex, para. 9.39. The tribunal thus suggested some caution in scrutinizing government actions when evaluating Article 1105 claims, but not with the precision of rules regarding judicial review under US law. Moreover, the tribunal did not similarly describe what level of deference it should apply to agency explanations regarding exercises of prosecutorial discretion for the purpose of evaluating the non-discrimination claims. The tribunal in *Apotex* permitted the US to withhold from discovery documents that the US had argued were protected by the deliberative process privilege. Nevertheless, it noted that it was not bound to do so as a matter of applicable law, stating:

> [I]n Paragraph O of its March Order, the Tribunal decided that it was not minded to take into account deliberative process privilege, attorney-client privilege, attorney work-product doctrine privilege (or any other privilege or like impediment) as a matter of any applicable national law or rules of law, but rather as one or more factors falling within Article 9(2) of the [International Bar Association Rules on the Taking of Evidence in International Arbitration. The Tribunal continues here to apply this general principle to the Parties' present dispute over document production.

Apotex, Procedural Order on Document Production Regarding the Parties' Respective Claims to Privilege and Privilege Logs, July 5, 2013, para. 14.

[26] See *Apotex*, US Rejoinder on Merits and Reply on Objections to Jurisdiction, Sept. 27, 2013, paras. 288-289.

[27] NAFTA Free Trade Commission, Notes of Interpretation of Certain Chapter 11 Provisions (July 31, 2001).

[28] See NAFTA, art. 1131 ("An interpretation by the [FTC] of a provision of this Agreement shall be binding on a Tribunal established under this Section."). Some other investment treaties contain similar provisions. (See, e.g., US-CAFTA-DR, art. 10.22(3); US-Singapore FTA, art. 15.22(2); US-Rwanda BIT, art. 30(3)). Others do not. (See, e.g., US-Egypt BIT).

[29] *Apotex*, US Counter-Memorial and Objections to Jurisdiction, Dec. 14, 2012, paras. 385-390.

[30] Id.

[31] As highlighted by the US in its briefs, the Vienna Convention on the Law of Treaties requires tribunals, when interpreting a treaty, to take into account subsequent practice of the state parties to a treaty establishing agreement on the treaty's meaning. See *Apotex*, US Rejoinder on Merits and Reply on Objections to Jurisdiction, Sept. 27, 2013, para. 389.

[32] *Apotex*, para. 9.71 (emphasis added).

[33] Vienna Convention on the Law of Treaties, Art. 31(3), May 23, 1969.

[34] Georg Nolte, "Jurisprudence under special regimes relating to subsequent agreements and subsequent practice," in Georg Nolte, ed., Treaties and Subsequent Practice (Oxford, United Kingdom: Oxford University Press, 2013), p. 237.

[35] Detroit International Bridge Company (DIBC) v. Canada, UNCITRAL, PCA Case No. 2012-25.

[36] Detroit International Bridge Company (DIBC) v. Canada, UNCITRAL, PCA Case No. 2012-25, Procedural Order No. 6, Mar. 18, 2014.

[37] Id.

[38] *DIBC*, Letter Submission from the US, Apr. 29, 2014.

[39] *DIBC*, Procedural Order No. 7, Mar. 25, 2014.

[40] Id. Both the US and Mexico subsequently requested, and the tribunal granted, access to the transcripts. Contrary to what is often US practice, however, the transcripts are confidential and will not be disclosed to the public. Luke Eric Peterson, After Excluding USA and Mexico from NAFTA Hearings, Tribunal Grants Access to Transcripts and Frowns on Investor's Attempt at Wholesale Redaction, Investment Arbitration Reporter, July 13, 2014.

[41] Julian Arato, "Treaty Interpretation and Constitutional Transformation: Informal Change in International

Organizations," 38 Yale J. Int'l L. 289, 308 (2013) (citing Ian Sinclair, The Vienna Convention on the Law of Treaties 98 (1984) (citing Lord McNair, The Law of Treaties 169 (1961))).

[42] Renco Group, Inc. v. Peru, UNCT/13/1, Decision as to the Scope of Preliminary Objections, Dec. 18, 2014.

[43] Article 10.20.4(c) (hereinafter "*Renco*").

[44] See *Methanex*, First Partial Award, August 7, 2001, Chapter I.

[45] *Renco*, Submission of the United States, Sept. 10, 2014, para. 2.

[46] See, e.g., United States-Peru Trade Promotion Agreement Implementation Act, p. 22 (Dec. 14, 2007).

[47] See, e.g., Oxford Handbook of International Investment Law 957-59 (Peter T. Muchlinski, Federico Ortino, and Christoph Schreuer eds., 2008); Renco also sought to rely on Rule 12(b)(6) in its arguments regarding the scope of Article 10.20.4.

[48] Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 570 (2007); *accord* Ashcroft v. Iqbal, 556 U.S. 662, 678–679 (2009).

[49] See *Renco*, Decision as to the Scope of Preliminary Objections, para. 112.

[50] See, e.g., Moseke v. Miller & Smith, Inc., 202 F. Supp. 2d 492, 501 (E.D. Va. 2002) ("A motion to dismiss based on the expiration of the statute of limitations is analyzed under Rule 12(b)(6)").

[51] See, e.g., Oliveras Sifre v. Department of Health, 38 F. Supp. 2d 91 (D.C. Puerto Rico 1999) (dismissing a claim under Rule 12(b)(6) due to the plaintiff's failure to receive a "right-to-sue" letter); Anderson v. Bd. of Educ. of Chi., 169 F. Supp. 2d 864 (N.D. Ill. 2001) (dismissing a claim under Rule 12(b)(6) for failing to exhaust administrative remedies).

[52] In *Methanex*, First Partial Award, August 7, 2001, para. 108, the tribunal categorized certain of the US's objections as objections to "jurisdiction" and others as objections to "admissibility". It stated, "[T]he USA's challenges to jurisdiction primarily concerned Article 1101(1) and other provisions of Section B of Chapter 11 (Articles 1116-1117 and 1121), whilst the USA's challenges to admissibility concerned substantive provisions under Section A of Chapter 11, namely Articles 1102, 1105 and 1110, which are the individual provisions in respect of which Methanex alleges breach by the USA."

[53] United States-Peru Trade Promotion Implementation Act, p. 22 (Dec. 14, 2007).

The Columbia Center on Sustainable Investment (CCSI), a joint center of Columbia Law School and the Earth Institute at Columbia University, is a leading research center and forum dedicated exclusively to the study, practice and discussion of sustainable international investment (SII) worldwide. Through research, advisory projects, multi-stakeholder dialogue and educational programs, CCSI constructs and implements an investment framework that promotes sustainable development, builds trusting relationships for long-term investments, and is easily adopted by governments, companies and civil society.