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The USMCA/CUSMA/T-MEC's Entry into Force: An Obituary for NAFTA's Investment Chapter

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On July 1, 2020, the investment chapter of the North American Free Trade Agreement (NAFTA) expired quietly in its North American home, at the age of 26. It left behind a generation of investment treaties and investment chapters in free trade agreements that are its direct descendants. It served as inspiration for many other agreements. It is succeeded by the investment chapter of the US-Mexico-Canada Agreement (USMCA). DNA testing to ascertain the progeny of that chapter is ongoing, as discussed below.

NAFTA's investment chapter was born following an intensive negotiating process – likely the most intensive one in history at that point. The first text was tabled in December 1991. The text then underwent an astonishing 40 iterations before it became final. Most unusually, the negotiators continued revising the text *after* the treaty was signed in 1992. The investment chapter, with the rest of the treaty, came into the world on its effective date of January 1, 1994.

Its parents recognized that this would be a busy child. Unlike prior investment agreements, the capital flows among the United States, Canada and Mexico were enormous. While the policy objectives of the US and Canada were to protect their investors in Mexico, the negotiating dynamic at the time required reciprocity in the investment obligations. The likelihood of substantial claims inspired closer scrutiny of the provisions than was the case in other negotiations.

The result was an investment chapter that was spare in its statement of obligations (except for the innovative attempt to define performance requirements), expansive but precise in its statement of exceptions and detailed in its crafting of the investor-state dispute resolution system. Its comprehensive investment promotion and protection system looked different and was different in important respects from any other agreement at the time.

The adolescence and young adult life of NAFTA's investment chapter was indeed an active one. The first claim came just a few years after its birth. Dozens followed, including some of the most controversial of the era.

NAFTA quickly proved to be a trendsetter. It opened its proceedings to the world long before other systems did. It was a beacon of transparency in arbitration. Other systems of investment arbitration slowly and sometimes grudgingly followed.

The flow of cases, inevitably, illustrated some of the defects in the conception of the NAFTA

investment chapter. The negotiators could not anticipate every permutation that might arise in practice. With time, a few cracks in the treaty became apparent.

The result was the first generation of direct descendants of the NAFTA investment chapter: the model investment chapters and bilateral investment treaties that Canada and the US developed in 2003 and 2004 based on their experience with NAFTA investment disputes. The basic structure of the NAFTA's investment chapter, and indeed many provisions word-for-word, were retained. But a number of provisions were improved in their wording, and a number of innovations added.

These new models served as the basis for many of the most important investment agreements of the past 15 years, including the Central American Free Trade Agreement, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership and the Canada-European Union Trade Agreement. Indeed, computational analysis of the TPP's investment chapter has noted that 81% of the text has been taken from previous US investment treaties, with 58% of its text similar or identical to the NAFTA itself.

In addition, the NAFTA served as the starting point for the investment chapter of the Free Trade Agreement of the Americas – an ambitious project that never saw the light of day. However, a generation of investment treaty negotiators in Latin America learned their trade in the FTAA negotiations. The NAFTA served, again, as inspiration for a whole range of agreements when those negotiators had the leverage to propose new text.

Comparatively, the USCMA's investment chapter is a significant break from the evolution of investor-state dispute settlement that began with NAFTA. Even though the investment chapter contains several instances of innovation and evolution from the NAFTA's Chapter 11, such provisions are largely overshadowed by the foreign policy approach to investment dispute resolution and the corresponding significant limitations on access to investor-state dispute settlement.

At the outset, Canada is not a party to the investment chapter's dispute resolution procedures. In some respects, this is not such a departure. As noted, it was never an objective of the US and Canada to have investor-State dispute resolution as between the two countries. They accepted it in order to ensure dispute settlement with Mexico. But the dynamic in the late 2010s was different, and reciprocity was no longer such an important issue for Mexico. Further, within the USMCA negotiations, at least two parties, Canada and Mexico, knew that investments made by their own nationals were already governed by the terms of the Trans-Pacific Partnership, a NAFTA descendent. The real departure is in ISDS between the US and Mexico.

The US-Mexico dispute resolution mechanisms are included in Annex 14-D and 14-E and align with the Trump administration's doctrine of economic nationalism. Under these Annexes, dispute resolution is tiered between privileged government contracts in oil and gas, power generation, telecommunications, transportation and infrastructure sectors, with a less favourable dispute resolution process for all other covered investment disputes. While contract claims may proceed directly to international arbitration, general investment claims are relegated to a Calvo-esque procedure with a requirement to commence local dispute resolution proceedings for 30 months as a condition precedent to access to international arbitration. Further, general investment claims are limited to claims of national treatment, most favoured nation treatment save for claims related to establishment and acquisition, which are specifically excluded, and direct expropriation, also explicitly excluded.

While the USMCA's investment chapter contains certain procedural and substantive evolutions and innovations, the significance of the above-noted limitations far outweighs any innovations contained therein. That said, it remains noteworthy that the USMCA's investment chapter contains important procedural advances through the inclusion of provisions on transparency of arbitral proceedings, the explicit public access to hearings and pleadings, arbitrator compliance with the IBA Guidelines on Conflicts of Interest in International Arbitration, and a prohibition on arbitrators acting as counsel or party-appointed expert or witness in any pending arbitration under the agreement for the duration of the proceedings.

On a substantive level, certain investment protections under the USMCA follow the trend of states narrowing and further defining substantive investment protections, with many provisions drafted responsively to previous investment award interpretation. For example, the USMCA's expropriation provision further qualifies what constitutes indirect expropriation through detailed criteria in Annex 14-B, most favored nation treatment is limited to substantive obligations, and article 14.6(5) effectively writes out claims based on legitimate expectations from the minimum standard of treatment. Further, the USMCA does mirror new provisions such as article 14.17 on corporate social responsibility, also found within the CPTPP. However, given the overall limitations on access to dispute resolution, and what may be claimed by investors that are not parties to covered contracts, such developments may be all for not. Indeed, it will remain to be seen whether US and Mexican investors will ever bring non-contract claims.

In sum, the NAFTA led a long life (by investment agreement standards), fathered a large family of other investment chapters and agreements and led a rich if controversial existence before passing on July 1, 2020. It is succeeded by the USMCA, which although contains certain elements of further evolution from the NAFTA; it marks a distinct and separate direction for ISDS by limiting international access to justice in lieu for local and contract-based dispute resolution. In doing so, at its core, the USCMA rejects certain core elements of NAFTA's Chapter 11 and related underlying foreign policy doctrine. While legacy claims based on NAFTA are likely to be still brought after July 1, 2020, until July 2023, the North American investor-state dispute settlement landscape has been significantly altered, at least for now.

For the full scope of our coverage of USMCA to date, click here.

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