UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

DISPUTE SETTLEMENT

REGIONAL APPROACHES

6.1 NAFTA

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NOTE

The **Course on Dispute Settlement in International Trade, Investment and Intellectual Property** consists of forty modules.

This module has been prepared by Mrs. L. Ojeda and Mrs. C. Azar at the request of the United Nations Conference on Trade and Development (UNCTAD). The views and opinions expressed in this module are those of the authors and not necessarily those of the United Nations, the World Trade Organization (WTO), the World Intellectual Property Organization (WIPO), the International Centre for Settlement of Investment Disputes (ICSID), the United Nations Commission on International Trade Law (UNCITRAL) or the Advisory Centre on WTO Law.

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WHAT YOU WILL LEARN

The North American Free Trade Agreement (NAFTA) concluded between Canada, the United States of America and Mexico entered into force in January 1994. The Agreement, which is in accordance with Article XXIV of GATT 1994, aims to establish a free trade area between the three countries, setting rules on the exchange of capital, goods and services between them. Among its objectives are the elimination of barriers to trade, the promotion of fair competition, the protection of intellectual property rights, the encouragement of investment, and, for the purpose of the implementation of the Agreement, the creation of effective procedures for the application and administration of the Agreement and for the settlement of disputes.

This module presents a general analysis of the dispute settlement mechanism of the NAFTA. It provides an overview of the three dispute settlement mechanisms established by the Agreement:

(i) The *general mechanism* for the settlement of disputes relating to the application, interpretation and implementation of the provisions of the Agreement (Chapter 20 of the NAFTA, described in section 1 of this module); and

Two special mechanisms:

(ii) For the settlement of investment disputes (Chapter 11 of the NAFTA described in section 2 of this module), and

(iii) For the review of final determinations and statutory amendments relating to countervailing duty and anti-dumping laws (Chapter 19 of the NAFTA, described in section 3 of this module).

Each dispute settlement mechanism responds to the objectives of the Agreement and to the concerns of the three countries, as follows:

- The general dispute settlement mechanism aims to settle disputes between the three Member States of the NAFTA arising out of the interpretation, implementation and application of the obligations assumed by them under the Agreement. Such disputes cover practically all the areas contemplated by the Agreement, including market access, non-tariff barriers, rules of origin, standards-related measures, government procurement, investment, cross-border services, telecommunications, financial services and intellectual property. This general mechanism fulfils one of the objectives of the NAFTA, which is the creation of effective procedures for the application and implementation of the Agreement.
- A special mechanism is applicable to *investment disputes* arising between an investor of a Member State of the NAFTA and the

host country of the investment, in respect of damages that may be caused by the failure of the host country to implement the protections granted under the Agreement. Given that this mechanism provides investors with the assurance that they have available a specific mechanism that can be put into action by them, it also meets one of the objectives of the NAFTA, which is to increase investment opportunities in the territories of its Members.

- Another special mechanism exists for review of *statutory amendments* and final determinations made by the authorities of a Member State in relation to *anti-dumping and countervailing duty laws*. In the case of statutory amendments, the mechanism applies between the States. In the case of reviews of determinations made by the authorities of a Member State, since the mechanism replaces judicial review in each country, any person that has the right to take part under national legislation may do so under the procedures established by the Agreement. This mechanism also fulfils one of the objectives of the NAFTA, which is to eliminate unnecessary barriers to trade, such as may arise from inadequate application of the Member States' laws on unfair practices.

The nature of the three procedures is similar to that of commercial arbitration, in that there is no standing supranational body; instead there are arbitral tribunals or panels created in each case in accordance with special rules.

OBJECTIVES

After reading this module, the reader should be able to:

- Identify the three dispute settlement mechanisms contained in the NAFTA;
- Recognize the substantive and procedural regulations that are applicable to each of these three mechanisms;
- Identify the various cases that have been submitted to these mechanisms; and
- Apply and analyse the general provisions of each of these mechanisms with reference to specific cases.

1. CHAPTER 20 OF THE NAFTA: DISPUTES RELATING TO THE APPLICATION, IMPLEMENTATION AND INTERPRETATION OF THE AGREEMENT

Objectives

After studying this section, the reader should be able to identify the procedures of the NAFTA for avoidance and administration of disputes between member countries arising out of the interpretation and application of the provisions of the Agreement.

1.1 Introduction

Chapter 20 concerns two subjects of particular importance for the operation of the Agreement: (a) the underlying institutional structure (Section A), and (b) the general mechanism for avoidance and settlement of disputes over the application, implementation and interpretation of its provisions by the Members States of the NAFTA (Section B).

The precursors of this dispute settlement mechanism were Chapter 18 of the Free Trade Agreement (FTA) between the United States and Canada and the Dispute Settlement Understanding (DSU) of the World Trade Organization (WTO).[1]

Certain subjects are outside the scope of application of the mechanism established in Chapter 20,[2] namely dumping and subsidies cases, for which there is an *ad hoc* mechanism in the Agreement.

The Chapter 20 mechanism is supplemented or modified in some instances when specific subjects are involved (i.e. financial services[3] and temporary entry for businesspersons[4]).

1.2 Institutional Provisions

Chapter 20 establishes the Free Trade Commission (hereafter, the Commission or FTC) and the Secretariat — two standing tripartite bodies responsible for the supervision and administration of the Agreement. They facilitate decision-making relating to the operation of the Agreement.

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[1] *Understanding on Rules and Procedures Governing the Settlement of Disputes within the framework of articles XXII and XXIII of the General Agreement on Tariffs and Trade (GATT)*

[2] *For example, refusals by Canada and Mexico to permit acquisitions (Annex 1138.2) and competition policy (Article 1501.3).*

[3] *Article 1414 applies to disputes on financial services issues. This Article provides for a special roster of panellist comprising financial services experts, and establishes special rules concerning the suspension of benefits.*

[4] *Article 1606 provides a special rule as to when the Chapter 20 mechanism may be commenced. The controversy must involve a "pattern of practice". In addition the person affected must have exhausted all available administrative remedies before a Party is able to submit a claim under this Chapter.*

1.2.1 Free Trade Commission

The Free Trade Commission is the highest institution. It is a consultative and supervisory body comprising representatives, or their alternates, of the ministries of trade of each Party. Its main functions are to supervise the implementation of the Agreement and generally to consider any matter that may affect its operation and application. The Commission plays an important role in resolving disputes arising out of the interpretation, application and implementation of the provisions of the NAFTA. Its decisions are taken by consensus, in accordance with the rules and procedures established by the Commission itself.[5]

In the exercise of its functions, the FTC relies on the Secretariat and on more than 20 committees and working groups (Annex 2001.2). It may also delegate some of its functions to these committees, or seek the advice of non-governmental experts and working groups.

The Commission:

- Supervises the implementation of the Agreement;
- Oversees its further elaboration;
- Resolves disputes that may arise regarding its interpretation or application;
- Supervises the work of all committees and working groups established under the Agreement, referred to in Annex 2001.2; and
- Considers any other matter that may affect the operation of the Agreement.

The Commission may:

- Establish and delegate responsibilities to ad hoc or standing committees, working groups or expert groups;
- Seek the advice of non-governmental persons or groups; and
- Take such other action in the exercise of its functions as the Parties may agree.

The Commission establishes its own rules and procedures. All decisions of the Commission are to be taken by consensus, except as the Commission may otherwise agree.

The Commission convenes at least once a year in regular session, and these sessions are chaired successively by each Party.[6]

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[5] Examples of recent decisions taken by the FTC include: "Agreement adopting technical modifications to annexes 300-B, 401 and 403.1 of the North American Free Trade Agreement, to bring them into line with amendments to the Harmonized Commodity Description and Coding System for 2002, consistent with NAFTA's Free Trade Commission. 21-XII-2001"; and "Agreement updating Annexes 401 and 403.1 of the North American Free Trade Agreement, consistent with NAFTA's Free Trade Commission. 01-III-2000." The FTC also takes decisions relating, inter alia, to expediting tariff reductions, creating committees and ad hoc working groups.

[6] Article 2001, paragraphs 2 to 5.

1.2.2 Secretariat

The Secretariat comprises three national Sections, which in practice function in a coordinated but autonomous manner. Each Member State establishes a permanent office of its Section[7] with its own Secretary and staff. Each Member State is responsible for the operation and cost of its Section and pays the remuneration and expenses of panellists, members of committees and scientific review boards.

The Secretariat assists the FTC and gives administrative support to the dispute settlement panels. As directed by the FTC, the Secretariat also provides support to the committees and working groups, and facilitates the operation of the Agreement.

1.2.3 Committees and Working Groups

The Commission has established a number of committees and working groups to review and discuss matters relating to the topics assigned to them. They monitor the application of the NAFTA in their specific area of competence, and, in turn, issue opinions aimed at preventing disputes.[8] For example, the Committee on Agricultural Trade, created under Article 706 of Chapter 7, reports annually to the FTC on progress in implementing the provisions of that Chapter. The Working Group on Trade and Competition, established under Article 1504 of Chapter 15, reports to the Committee the relationship between competition laws and trade policies in the free trade area.

The involvement of the committees and working groups in the exchange of information and in the study of their subject areas has undoubtedly played a very important role in the prevention of disputes, particularly during the consultation phase. This is because the exchange of information prevents misunderstandings, and consequently offers a better chance of reaching agreement

1.3 Dispute Settlement Provisions of Chapter 20

The dispute settlement system established by Chapter 20 proceeds in three stages: consultations between the parties; intervention by the Free Trade Commission; and panel proceedings.

1.3.1 Scope

Chapter 20 concerns disputes between Member States, relating to:

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[7] *These Sections are currently located in Mexico City, Ottawa and Washington DC.*
[8] *There are now more than 20 committees and working groups; see Annex 2001.2.*

(a) The interpretation of its provisions[9] and the non-performance by one of the Parties of its obligations under the Agreement.

(b) The application by one Party of an actual or proposed measure that the other Party or Parties consider inconsistent with the Agreement; or

(c) The application by one Party of an actual or proposed measure consistent with the Agreement that the other Party or Parties consider to cause nullification or impairment.[10]

1.3.2 Terminology

The States are known as the "complaining Party or Parties" and the "Party complained against". The concept of "Third Party" is used to refer to a State which, although not involved in the dispute, has certain rights that it is able to exercise during the proceedings.

Article 201 of the NAFTA gives a broad definition of "measure" to include any law, regulation, procedure, requirement or practice. Under Chapter 20, a measure of the disputing Party that causes nullification or impairment[11] of benefits accruing to a complaining Party with regard to trade in goods, technical barriers to trade, cross-border trade in services and intellectual property.

The concept of nullification and impairment (Annex 204 of the NAFTA and Article XXIII of the GATT 1994) refers to the effect of the application of a measure on the benefits that a Party could reasonably have expected to accrue to it under the Agreement.

1.3.3 Selection of WTO/NAFTA Forum

With the signing of the NAFTA, Mexico, the United States and Canada did not renounce their rights under the WTO. Consequently, disputes regarding any matter arising under both the NAFTA and the WTO agreement may be settled in either forum at the discretion of the complaining Party[12].

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[9] Pursuant to article 102.2 of the NAFTA, "The Parties shall interpret and apply the provisions of this Agreement in the light of its objectives set out in paragraph 1 and in accordance with applicable rules of international law." The objectives of the Agreement set out in Article 102.1 are to: "(a) eliminate barriers to trade in, and facilitate the cross-border movement of, goods and services between the territories of the Parties; (b) promote conditions of fair competition in the free trade area; (c) increase substantially investment opportunities in the territories of the Parties; (d) provide adequate and effective protection and enforcement of intellectual property rights in each Party's territory; (e) create effective procedures for the implementation and application of this Agreement, for its joint administration and for the resolution of disputes; and (f) establish a framework for further trilateral, regional and multilateral cooperation to expand and enhance the benefits of this Agreement."

[10] Article 2004.

[11] In this case it would be necessary to determine in what way the actual or proposed measure nullified or impaired the benefits that a Party to the Agreement might reasonably have expected to accrue to it. Scholars interpret the Agreement as restricting the scope of application of Chapter 20 in respect of the measures that cause nullification or impairment to trade in goods, on the grounds that assessing the reasonably expected benefits is more feasible in this sector.

[12] Article 2005.1.

General rule

In order to avoid parallel proceedings, and above all, contradictory decisions, in cases where the conduct of a Member State might constitute a violation both under the WTO and the NAFTA, the complaining Party chooses the forum for the settlement of the dispute, without the option of referring it to the other; the choice of one forum always excludes the other.[13]

In the event the WTO dispute settlement procedure is chosen, the complaining Party, before initiating the procedure, should notify its intention in writing to the Third Party so that, in the event that the Third Party has a substantial interest in the case and prefers the NAFTA forum, both may enter into consultations in order to agree on the forum. If no agreement is reached, the NAFTA forum takes precedence.[14]

Exceptions

In matters relating to the environment, the agricultural sector, sanitary and phytosanitary measures or standards-related measures, the Party complained against may oppose the use of the WTO forum, by advising its Section of the Secretariat and the complaining Party to that effect. In other words, in these areas, the choice of forum rests ultimately with the Party complained against.[15]

1.3.4 Consultations

Any Party may request, in writing, consultations with any other Party regarding any actual or proposed measure or any other matter that it considers might affect the operation of the Agreement.

Time periods

The consultations last 30 days in the case of bilateral discussions, and 45 days in the case of trilateral discussions,[16] starting from the date of delivery of the request for consultations by the complaining Party.

Obligations of the consulting Parties

The consulting Parties are required to make every attempt to arrive at a mutually satisfactory resolution of any matter through consultations. The consulting Parties should: provide sufficient information to enable a full examination of how the actual or proposed measure or other matter might affect the operation of the Agreement; treat any confidential or proprietary information exchanged in the course of consultations on the same basis as the Party providing the information; and seek to avoid any resolution that adversely affects the interests under the Agreement of any other Party.[17]

Participation of a Third Party

A Third Party that considers it has a substantial interest in the matter is entitled to participate in the consultations. To do so, it must present a written notice to its Section of the Secretariat and to the other Parties.[18]

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[13] *Article 2005.6.*
[14] *Article 2005.2.*
[15] *Article 2005.4.*
[16] *In the case of perishable goods, this period may be reduced to 15 days*
[17] *Paragraph 5, Article 2006*
[18] *Article 2006.3.*

1.3.5 Intervention of the Free Trade Commission

Request for intervention of the FTC

If no settlement is reached during the consultations, any Party may request in writing a meeting of the Free Trade Commission. The FTC is expected to resolve the matter within 30 days, or within such other period as the Parties may agree.

The complaining Party's letter should specify the measure or other matter complained of; indicate the provisions of the Agreement that it considers relevant; and contain a brief statement of the outcome of the consultations. The complaining Party should deliver its letter of complaint to the other Parties and to its Section of the Secretariat.

Mechanisms used by the FTC: good offices, mediation and conciliation

When requested to intervene, the FTC convenes within 10 days of the delivery of the request. The Commission may: [19]

- Call on such technical advisers or create such working groups or expert groups as it deems necessary,
- Have recourse to good offices, conciliation, mediation or such other dispute resolution procedures;
- Make recommendations; or
- Assist the consulting Parties to reach a mutually satisfactory resolution of the dispute.[20]

The aim of the intervention of the FTC provided for in this Chapter is to bring together the governments of the disputing Parties to encourage an atmosphere of negotiation and to avoid costly and lengthy proceedings.

1.3.6 Arbitral Panel Proceedings

If the Commission does not resolve the matter within 30 days, a consulting Party may request, in writing, the establishment of an arbitral panel, which the FTC will establish on delivery of the request.

Selection of panellists and establishment of the panel

Panels comprise five members (four panellists and a chair). The Panel members are selected using a cross-selection procedure from a roster of 30 experts previously agreed upon by consensus of the Parties. The aim of this roster is to ensure that persons appointed as panellists in a dispute have been previously endorsed by the Parties as regards their competence, reputation and knowledge.[21]

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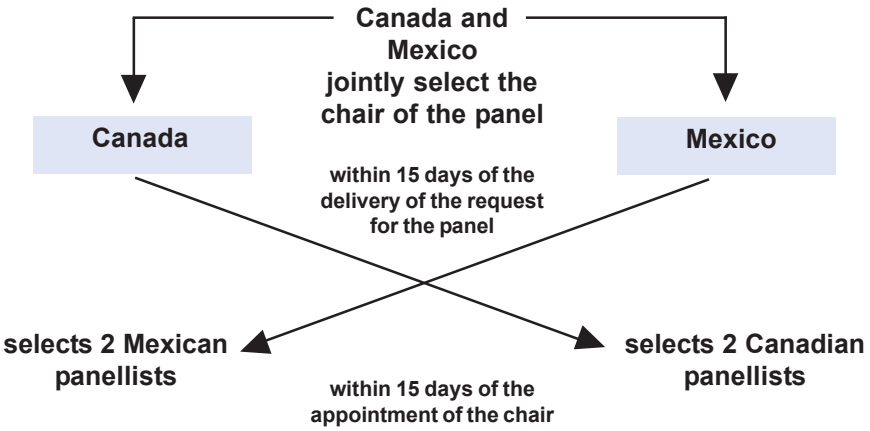
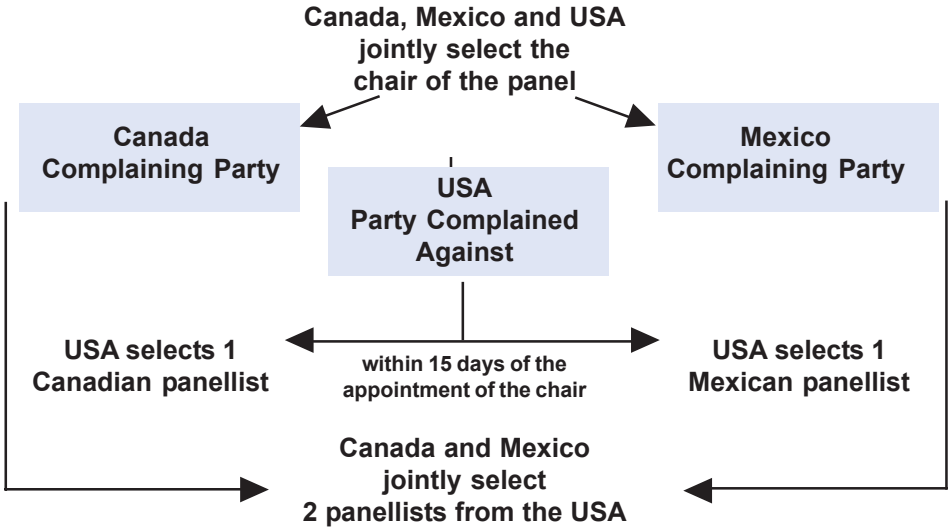
[19] Persons participating in a dispute as experts or advisers may not be appointed subsequently as panellists in the dispute (Article 2010.2).
[20] Article 2007.5.
[21] Article 2009.1.

The diagram below illustrates the "cross-selection" procedure.

Bilateral Dispute:



Trilateral Dispute:



The reason for this novel mechanism for establishing the panel, as illustrated in the diagram, is the importance of ensuring the impartiality of the panellists by not allowing them to be nominated by the governments of their own countries. Although all dispute settlement systems attach great importance to the neutrality of third parties,[22] the Parties to the NAFTA felt that the *cross-selection* system would further reinforce the concept.

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[22] *See Rules of Arbitration of the International Court of Arbitration of the International Chamber of Commerce, Article 15.2; Arbitration Rules of the Commercial Arbitration and Mediation Center for the Americas, Article 8; Arbitration Rules of the Arbitration Center of Mexico, Article 13.*

If the disputing Parties are unable to agree on the chair within 15 days, they shall select as chair, within five days, a roster member who is not one of their citizens. If a disputing Party fails to select its panellists within 15 days, such panellists shall be selected by lot from among the roster members who are citizens of the other disputing Party.[23]

The panellists on the roster who comprise the roster should be professionals with experience in law, international trade and dispute settlement under international trade agreements. They should be independent from any Party and comply with the Code of Conduct (see below).[24]

Code of Conduct and Rules for challenge

The Code of Conduct[25] and Model Rules[26] contain provisions regulating the conduct of the panellists. They are aimed principally at ensuring impartiality and independence. Breach of these regulations may cause a panellist to be challenged and consequently replaced.

Thus, for example, Rules 36 and 37 of the Model Rules establish that the panellists shall not meet or contact a participating Party in the absence of the other participating Parties and the other panellists (*ex parte contacts*).

A panellist must disclose any interest, relationship or matter that might affect his/her independence (i.e. declare it to the Section of his/her Secretariat in good time). Once nominated, panellists maintain this duty throughout the proceedings.[27]

Rules applicable to the proceedings

(i) Principles

Panel proceedings are regulated by Chapter 20 and by the Model Rules of Procedure issued pursuant to Article 2012.2 of the Agreement. These provisions contain the following principles:

- Autonomy of the will of the Parties: The time periods contained in Chapter 20 and the Model Rules may generally be modified with the agreement of the Parties, before or during the proceedings.
- The right to a hearing: The parties have a right to at least one hearing.
- Due process of law: Panel proceedings must ensure equality between the parties and give them full opportunity to exercise their rights.
- Flexibility: If a procedural rule is not covered by the Model Rules, Panel members may adopt an appropriate procedure that is not inconsistent with the Agreement. The parties shall have an opportunity to provide initial and rebuttal written submissions.

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[23] *Article 2011.*
[24] *Article 2009.2.*
[25] *Code of Conduct for Dispute Settlement Procedures under Chapters 19 and 20 of the NAFTA..*
[26] *Model Rules of Procedure for Chapter 20.*
[27] *Paragraph II of the Code of Conduct provides a non-exhaustive list of the interests, relationships and matters that a panel candidate must disclose.*

- Confidentiality of proceedings: Rule 25 lists the persons who may be present at the proceedings, namely:
- Representatives of the disputing Parties;
- Advisers to the disputing Parties, provided that they do not have a personal interest in the case;
- Officials and assistants of the Secretariat; and
- Panellists' assistants.

Rule 16 provides that only the Panel may authorize the participation of translators, administrative assistants and Secretariat staff in its deliberations.

(ii) Determining the remit or terms of reference of the Panel

Unless the disputing Parties agree otherwise within 20 days from the date of the delivery of the request for the establishment of the panel, the terms of reference of the Panel shall be:

> *"To examine, in the light of the relevant provisions of the Agreement, the matter referred to the Commission (as set out in the request for a Commission meeting) and to make findings, determinations and recommendations as provided in Article 2016.2."*

If a complaining Party wishes to argue that a matter has nullified or impaired benefits, the terms of reference should indicate this.

If a disputing Party wishes the panel to make findings as to the degree of adverse trade effects on a Party of a measure found not to conform with the obligations of the Agreement or to have caused nullification or impairment in the sense of Annex 2004, the terms of reference should indicate this.[28]

The aim of the terms of reference, or "statement of case", is to establish clearly the remit of the Panel in relation to the claims of the disputing Parties. This measure gives assurance to the Parties that the Panel shall not exceed its functions and shall not leave the questions covered in the statement of case unresolved.

(iii) Experts and Advisers to the Panel

The Panel may, either on its own initiative or on request of a disputing Party, seek information and technical advice from any person or body that it deems appropriate,[29] subject to the terms and conditions agreed by the Parties.

Likewise, the Panel may choose to request a written report from a scientific review board on matters relating to the environment, health, safety and other

[28] *Article 2012.3, 4 and 5.*
[29] *Article 2014.*

scientific subjects relevant to the case, subject to the terms and conditions agreed by the Parties. The Parties can comment on the factual issues referred to the board and on the report of the board. The panel should take these comments into account in the preparation of its report.[30]

(iv) Third Party with a Substantial Interest

A Third Party which deems to have a substantial interest in the matter may join as complaining Party.[31] In order to exercise this right, the Third Party presents a written notice to that effect to the disputing Parties within seven days from the date of the request by a disputing Party for the formation of a Panel.

(v) Third Party with no Substantial Interest

A Party that is not a disputing Party is entitled to attend the hearings, present oral and written communications to the Panel (*amicus curiae*), and receive the written submissions of the disputing Parties.[32]

(vi) Other rules

In addition to the subjects mentioned, the Model Rules contain regulations relating to the conduct and development of proceedings in respect of:

- Intervention and administrative support of the Secretariat;
- Time periods, computation of time and cases of suspension;
- Means of delivering communications between the Parties, the FTC and the Panel;
- Number of copies of the communications;
- Correction of errors of form;
- Replacement of arbitrators on grounds of death, resignation or challenge;
- Location of hearing and conduct thereof by the Panel;
- Transcription of hearing;
- Language of written submissions and arguments;
- Burden of proof;
- Selection and intervention of scientific review boards;
- Expenses and payment of experts, panellists and assistants; and
- Special rules applicable to suspension of benefits panels.

[30] *Article 2015.*
[31] *Article 2008.3. A Party has "substantial interest in a case" when it considers that the actual or proposed measure affects or may affect it.*
[32] *Article 2013.*

Hearings

Chapter 20 provides for at least one hearing in which the Parties present their oral arguments to the panel. The hearing may be attended by representatives and advisers of the disputing Parties, Secretariat officials and assistants, representatives and advisers of the Third Party, and assistants of the panellists.

Initial report and comments of the Parties

The Panel's initial report is to be delivered within 90 days of the date of formation of the Panel (selection of final panellist), unless the Parties agree otherwise. The report should include the Panel's findings on the facts of the case and its determination as to whether:

- The measure that a Party has adopted or proposes to adopt is or would be inconsistent with the provisions of the Agreement;
- If so requested by the Parties, the measure that causes or may cause nullification or impairment and the degree of the adverse commercial effects so caused.

The Panel's findings are to be based on:

- The submissions and arguments of the Parties;
- When applicable, the information provided by the advisers and technical experts consulted; and
- When applicable, the report of the scientific review board.

The Panel makes recommendations to the parties for the resolution of the dispute. Panellists may append separate opinions on matters not unanimously agreed.[33]

There follows a period of 14 days during which the Parties may submit written comments to the initial report of the Panel. The Panel may request the views of any party; reconsider the contents of its report; or make any further examination that it considers appropriate.[34]

Final report

The panel presents to the disputing Parties a final report, including any separate opinions on matters not unanimously agreed, within 30 days of the presentation of the initial report, unless the disputing Parties agree otherwise. No panel may, either in its initial report or its final report, disclose which panellists are associated with majority or minority opinions.

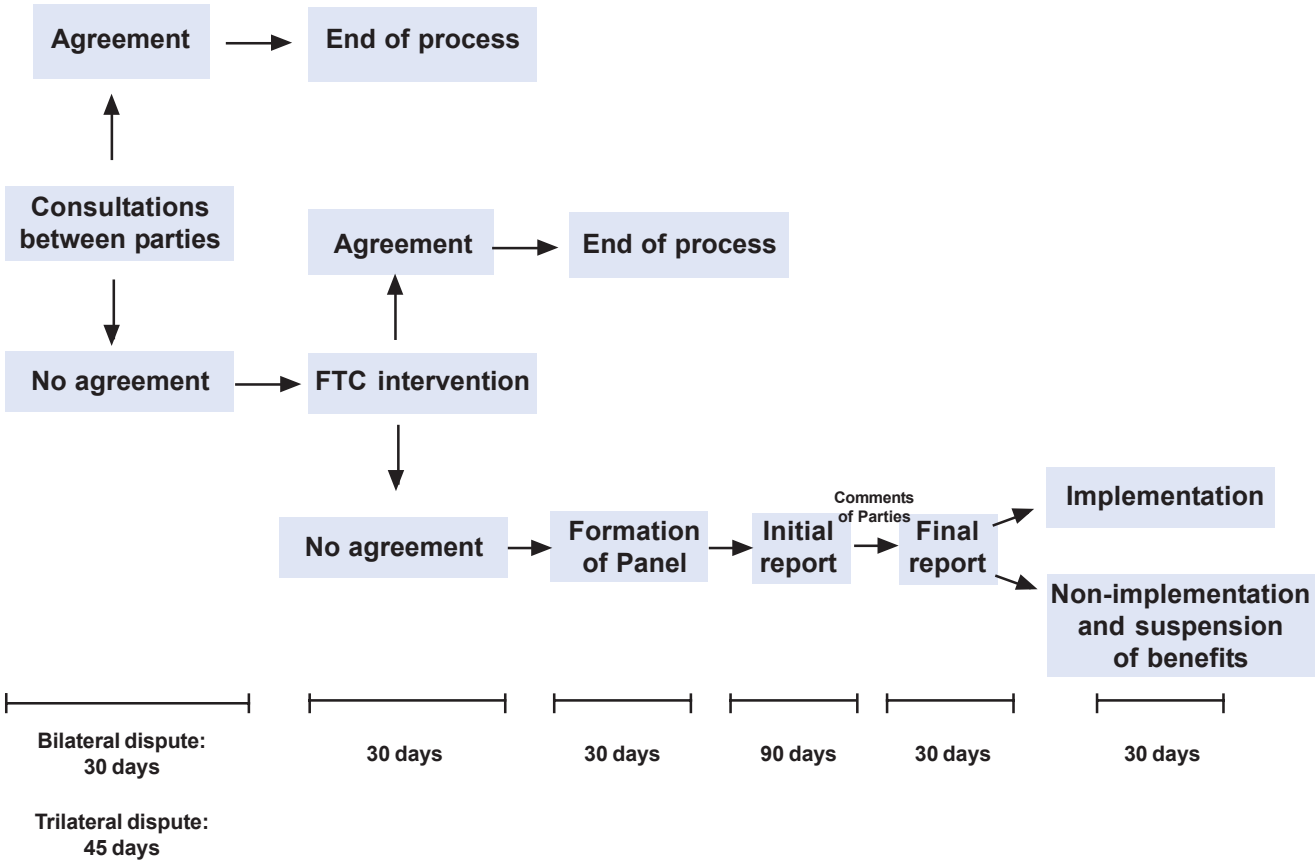
The disputing Parties transmit to the Commission the final report of the panel, including any report of a scientific review board, as well as any written views that a disputing Party wishes to have appended, on a confidential basis, within a reasonable period of time after it is presented to them.

[33] *In recognition of the impartiality and neutrality of the panellists, article 2017.2 states that "no panel may, either in its initial report or its final report, disclose which panellists are associated with majority or minority opinions".*
[34] *Article 2016.5.*

Unless the Commission decides otherwise, the final report of the panel is published 15 days after it is transmitted to the Commission.[35]

It is important to distinguish between the legal status of an arbitral award and a final report issued under Chapter 20. While the arbitral award has executive character and puts an end to the dispute, the Panel's report determines the legitimacy or illegitimacy of the claims of the disputing Parties and makes recommendations thereon, the implementation of which is subject to subsequent agreement by the Parties.

Flow Chart of the General Mechanism of Chapter 20.



1.4 Resolution, Implementation and Non-Implementation

In the event that the Panel rules in favour of the complaining Party, taking the view that a provision of the agreement has not been complied with, or a measure inconsistent with its provisions has been taken or is proposed, or else that a measure has been taken or is proposed that is consistent but causes nullification or impairment to the other Party, the disputing Parties should jointly agree to the manner in which the dispute shall be resolved. The resolution will generally, but not necessarily, conform with the Panel's recommendation.

[35] *Article 2017.1, 2, 3 and 4.*

1.4.1 Implementation of Final Report

In implementing the Agreement of the Parties on the basis of the final report issued by the Panel, the Party that took or proposed the disputed measure may:

- Not implement or remove the measure that is inconsistent with or in breach of the Agreement; or
- Grant compensation, i.e. the Party complained against may grant a benefit to the complaining Party or Parties equivalent to the damage caused (e.g. by reduction of a tariff)

1.4.2 Non-Implementation

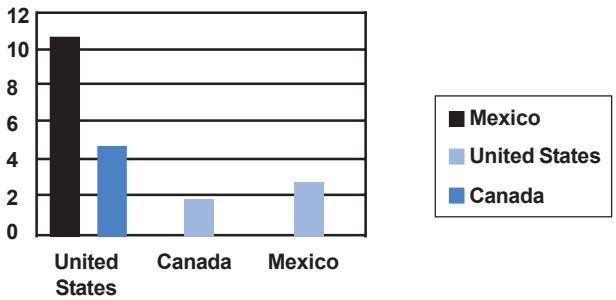
In the event of non-implementation by the Party complained against of the recommendations made by the Panel in its final report, and in the absence of agreement between the Parties within 30 days of receiving the report, the Agreement grants the complaining Party the right to suspend the application to the other Party of benefits of equivalent effect, until an agreement is reached on a resolution of the dispute.[36]

The complaining Party must seek to apply the suspension in the same sector(s) as that affected by the measure in question. Only if this is not possible can the complaining Party take measures in a different sector or sectors.

On the written request of the disputing Party, the Commission establishes a Panel to determine whether the level of benefits suspended by the complaining Party is manifestly excessive. The Panel is required to present its determination within 60 days.[37]

Statistical Data[38]

Cases presented under Chapter 20 of the NAFTA against Mexico, Canada, and the United States (as of August 2002).



The horizontal axis represents the complaining Parties, and the vertical axis indicates the number of cases brought by one member against the other. Thus the largest number of cases were filed by the United States against Mexico.

[36] *Article 2019.*
[37] *Article 2019. 3 and 4.*
[38] *Information supplied by Ricardo Ramírez, Deputy Director of the International Commercial Negotiations Division of the Economy Secretariat of Mexico.*

1.5 Private Commercial Dispute Settlement

1.5.1 Domestic Judicial or Administrative Proceedings

The interpretation and application of the Agreement may be subject to domestic proceedings of a judicial or administrative nature. In such a case, the FTC can be consulted to give an opinion on the subject. The FTC's interpretative report is then submitted to the court or administrative body by the Party in whose territory the said court or body is located. If the members of the Commission do not reach agreement (the Commission decides by consensus) on the interpretation that they are to present, the Parties are free to submit their own interpretation to the court or administrative body in question.[39]

1.5.2 Alternative Dispute Resolution

Another important contribution of Chapter 20 is that it deals with the resolution of disputes between individuals, not by means of a procedural mechanism, but by reference to the obligation of the Parties to promote and facilitate the use of international commercial arbitration and other alternative mechanisms between the nationals of each of the Parties.

Certainly, in their international commercial dealings, individuals do directly apply the benefits that the Agreement brings to commercial relationships. Those who may frequently face disputes therefore require valid, neutral proceedings in order to resolve them. This is why, when the Agreement was negotiated, it was decided that the Member States should strengthen and promote private arbitration in their territory.

Mexico, Canada and the United States recognize agreements to arbitrate and enforce arbitral awards in a country other than the one in which they were made. This has been achieved by the ratification and application of the United Nations Convention on Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) or of the InterAmerican Convention on International Commercial Arbitration (Panama, 1975), and the application of these conventions in an appropriate manner by the judicial authorities. While Mexico, Canada and the United States have ratified the New York Convention, only Mexico and the United States are parties to the Panama Convention.

The Commission established, in October 1994, an advisory committee with a mandate to study the practice of arbitration and alternative dispute resolution between individuals, called the "Advisory Committee on Private Commercial Disputes", sometimes referred to as the "2022 Committee".

The Committee comprises 10 nationals of each Party, professionals who specialize in the settlement of private commercial disputes (2 must be from the public sector and 8 from the private sector).

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[39] *Article 2020.*

The Committee convenes periodically to present reports and recommendations to the Commission on how to encourage and promote alternative dispute resolution between individuals in the free trade area.[40]

Currently the Committee works through six sub-committees responsible for:

- Compilation and assessment of national laws on alternative dispute resolution;
- Identification of the industry sectors in which the use of alternative dispute resolution has been developed;
- Research and development of means for promoting the use of alternative dispute resolution;
- Research into the observance of Agreements to arbitrate and of recognition and enforcement of awards;
- Study of conciliation and methods of alternative dispute resolution other than arbitration; and
- Liaison with the judiciaries of the signatory States.

To date, the activities of the Committee have been constant, but the results modest. Its work is particularly important in extending the reach of these mechanisms into industry sectors that do not necessarily carry out commercial transactions and that in some way may also benefit from arbitration and other alternative dispute settlement mechanisms.[41]

1.6 Summing up

Chapter 20 is at the heart of the NAFTA because it provides for the administration of the Agreement and for the settlement of disputes that arise between the Parties as a result of its operation.

Worth noting is the innovative procedure of cross-selection of panel members, which guarantees greater impartiality and independence of the arbitrators comprising the panel.

In practice, the mechanism has met with criticism and difficulties. To date, the most important procedural problem concerns the formation of the panel, partly due to the Parties' lack of agreement over the roster of candidates from which it is to be formed.

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[40] See Perezcano, Hugo, La solución de controversias en el marco del Tratado de Libre Comercio de América del Norte [Dispute Settlement under the North American Free Trade Agreement], library of the Legal Research Institute of the Autonomous National University of Mexico (UNAM), 1997. http://www.bibliojuridica.org/libros/1/143/33.pdf.

[41] Cf. Perezcano, Hugo, La solución de controversias en el marco del Tratado de Libre Comercio de América del Norte [Dispute Settlement under the North American Free Trade Agreement], 1997. Library of the UNAM Legal Research Institute]

1.7 Test your Understanding

1. **Why does the Agreement provide for trilateral disputes in which there are two complaining Parties and one Party complained against, and not disputes with one complaining Party and two Parties complained against?**
2. **Why is it important to allow the participation of a Third Party, even when it does not have a "substantial interest" in the case?**
3. **What is meant by having a "substantial interest" in the proceedings? How should it be measured?**
4. **In the event of other Parties joining the NAFTA, will it be necessary to amend its institutional structure, or does the current structure allow for new countries to sign up?**
5. **Why is it important that a Third Party interested in participating in the Panel proceedings submit its notice within such a short time period (seven days)?**

2. CHAPTER 11 OF THE NAFTA: SETTLEMENT OF INVESTMENT DISPUTES

Objectives

After studying this section, the reader should be able to:

- **Identify the protections that NAFTA Member States give to investors and to the investments of investors from other signatory countries when they invest in their territory; and**
- **Discuss the mechanism that NAFTA Members have established for investors to claim relief for financial losses arising from breaches of such guarantees.**

Chapter 11 establishes principles concerning the treatment and protection which a Member State should grant to the investors and the investments of investors of another Member (Section 2.1 of this Module) and a mechanism for the settlement of disputes arising between a Party and an investor — an individual or a corporation — and another Party (Section 2.2 of this Module).

2.1 Substantive Provisions: Protections Granted by the Parties in Investment Matters

Chapter 11, Section A establishes a number of substantive rules on the protection of investments in the NAFTA region.

2.1.1 Scope and coverage

Chapter 11 applies to all existing measures[42] adopted or maintained by a Party in relation to the investors and the investments of investors of another Party.[43]

Investment

The Agreement establishes a broad definition of an investment. It refers to an enterprise; shares and bonds; loans and debt securities with a maturity of at least three years or those between affiliate companies; tangible and intangible property, including intellectual property rights, franchises and know-how, and contractual interests or rights arising therefrom (e.g. turnkey contracts).[44]

Investor

The Agreement defines an investor of a Party as a Party or State enterprise thereof, or a national or an enterprise of such Party established or organized in accordance with the laws of a signatory country, irrespective of the origin of the capital.[45]

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[42] *As mentioned earlier, Article 201 of the NAFTA has a broad definition of the concept of "measures", including any law, regulation, proceeding, requirement or practice. Also, the concept of "existing" means in effect on the date of entry into force of the NAFTA.*
[43] *Article 1101.*
[44] *Article 1139.*
[45] *Article 1139.*

The Agreement extends the protection granted to "investors of another Party" to their branches located in the territories of the Parties.[46]

Nevertheless, the three countries have retained the right under this Chapter to deny benefits in their territory to a company controlled by investors from non-NAFTA countries in the following cases:[47] (i) if the country receiving the investment does not have diplomatic relations with the country of which the investors of that enterprise are nationals; (ii) if the country receiving the investment adopts measures against a non- NAFTA country that prevents dealings with investors who are nationals of that non- NAFTA country; or (iii) if the enterprise does not have "substantial business activities" in the territory of the country in which it is constituted.[48]

Exceptions

Despite the broad scope and coverage of Chapter 11, there are a number of scenarios in which the Chapter on investment is not applicable. For example, with regard to the measures covered by Chapter 14 of the Agreement[49] relating to financial services, except in cases expressly established in Chapter 14 itself.[50]

Also, adopting a broad definition of investment in a free trade agreement makes it difficult to achieve a self-contained chapter on investment. In other words, there are other subjects, regulated by other chapters of the Agreement, that may also be concerned with investments. These include intellectual property, cross-border services,[51] government procurement, competition and standards, as well as the energy, agriculture and automotive sectors. Also, due to the complexity of the topics regulated by this Chapter, the provisions on investment affect the obligations entailed in the chapter on market access (e.g. with respect to duty referral programs and waiver of customs duties).

Because of the above, there are provisions throughout the Agreement that regulate the relationships between these chapters and the Chapter on investment.[52] In particular, Article 1112 establishes that: "In the event of any inconsistency between this Chapter and another Chapter, the other Chapter shall prevail to the extent of the inconsistency".

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[46] The Chapter on investment is the only one in the NAFTA that includes branches under the definition of "enterprise" (see article 1139).

[47] Article 1113.

[48] The term "substantial business activities" is not defined in the NAFTA. However, what this concept implies is that the enterprise must have operations in the territory in which it is constituted, thus preventing "shell companies" from benefiting from the protections of the NAFTA.

[49] Article 1101 (3).

[50] The Chapter on financial services incorporates by reference the applicable articles on investment (article 1401.2 of the NAFTA). That Chapter regulates issues both of investment and trade in cross-border services.

[51] It should be remembered that this definition of investment makes it difficult to differentiate clearly between a cross-border service and an investment. Construction services and general transport services are cases in point.

[52] See articles 300, 701, 1101 (3), 1108 (5), 1110 (7), 1307, 1401 (2), 1607 and 2103.

2.1.2 Substantive Provisions

National treatment (Article 1102)

Each Party shall accord, in like circumstances[53], to investors and the investments of investors of another Party treatment no less favourable than that it accords to its own investors and their investments[54] with respect to the establishment, acquisition, expansion, management, conduct, operation or sale of investments.

Most-favoured-nation treatment (Article 1103)

Each Party shall accord to investors and investments of investors of another Party treatment no less favourable than that it accords, in like circumstances, to investors or investments of non-NAFTA countries[55] with respect to the establishment, acquisition, expansion, management, conduct, operation or sale of investments. In principle, this means that any concession granted to investments and investors of non-Parties must automatically be extended to investors and investments of investors of the other Member States of the free trade area.

Standard of treatment (Article 1104)

A Party must accord "national treatment" or "most-favoured-nation treatment", whichever is the better, to investors and investments of investors of the other Parties.

Minimum standard of treatment (Article 1105)

A Party has an obligation at all times to accord to investments of investors of other member countries treatment in accordance with international law. This treatment may be considered as the "base level" to which such investments are entitled, including the right to receive fair and equitable treatment and full protection and security.

Each Party shall accord to investors and to investments of investor of another Party, non-discriminatory treatment with regard to losses suffered owing to civil strike or armed conflict in its territory.

Senior management and board of directors (Article 1107)

A Party may not require that individuals who occupy senior management positions in an enterprise of an investor of another Party shall have a particular nationality. However, a Party is free to require that a simple majority of the members of the board of directors of an enterprise of another Party can be of a particular nationality, as long as this requirement does not impair the ability of an investor to control its investment.[56]

Performance requirements (Article 1106)

The Agreement prohibits the imposition of requirements on investments that have the effect of distorting the flow of international trade and investment (e.g. a requirement that a foreign enterprise should give preference to goods produced locally, or should export a percentage of its goods, or should export to a specific region, or should use locally produced parts in its end product).[57]

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[53] *The expression "like circumstances" is considered crucial, since it provides a point of comparison for the treatment that national investors or investments should be accorded.*
[54] *Article 1102.1 and 2.*
[55] *Article 1103. 1 and 2.*
[56] *Article 1107.*
[57] *Article 1106 contains a list of prohibited performance requirements.*

Likewise, Canada, Mexico or the United States cannot condition the receipt of any advantage on stipulations such as meeting domestic- content or trade balancing requirements.

Transfers (Article 1109)

Each Party should permit all transfers relating to an investment of an investor of another Party in the territory of the Party to be made freely and without delay. Such transfers include proceeds from the sale of the investment, profits, dividends, capital gains and royalty payments. Transfers may be made in a freely usable currency at the market rate of exchange.

Expropriation and compensation (Article 1110)

No Party can expropriate an investment of an investor of another Party, or take any measure *tantamount* to an expropriation, unless it is done for a public purpose, on a non-discriminatory basis, in accordance with due process of law and international law, and on payment of compensation as defined in paragraphs 2 to 6 of Article 1110.

Environmental measures (Article 1114)

A Party may adopt, maintain or enforce a measure that it considers appropriate to ensure that investments in its territory are undertaken in a manner sensitive to environmental concerns. The Parties recognize that it is inappropriate to encourage investment by relaxing domestic health, safety or environmental measures. If a Party feels that another Party has breached this commitment, it may undertake consultations aimed at ending the continuation of the investment incentive.

State enterprises (Article 1503)

Article 1503 requires that State enterprises act in a manner that is not inconsistent with Chapter 11 and Chapter 14 where such enterprises exercise any regulatory, administrative or other governmental authority delegated to them, such as the power to expropriate, grant licenses, approve commercial transactions or impose quotas.

2.1.3 Exceptions

There are specific exceptions that apply to the regulations relating to investment. These exceptions are detailed in: (a) the Reservations annexes at the end of the Agreement; and (b) in the Chapter on general exceptions applicable to the provisions of the Agreement. It is not necessary to consider them here for the purpose of this Module.

2.2 Procedural Provisions: the Dispute Settlement Mechanism

Chapter 11, Section B, establishes a mechanism for the settlement of investment disputes arising under the substantive rules of Section A of Chapter 11. This mechanism is based on the model developed by the United States in its bilateral investment treaties.

The mechanism embodies the following principles:

- Equal treatment of investors of the Parties in accordance with the principle of international reciprocity;
- Guarantee of a hearing and protection of the right of defence of a Party ("due process of law"); and
- Impartial composition of the tribunal.

The mechanism of Chapter 11 does not affect the right of a Party to have recourse to the general dispute settlement mechanism between States established in Chapter 20 of the Agreement.[58]

2.2.1 Consultation and Negotiations

Before proceeding to arbitration, the disputing Parties should first attempt to settle a claim through consultation or negotiation.[59]

2.2.2 Procedural Requirements

Subjects

An investor of a Party may invoke the mechanism, either on its own behalf or on behalf of an enterprise, if it has incurred a loss or damage as a result of the failure of another Party to observe the provisions of Chapter 11 or the provisions relating to State enterprises contained in Article 1502.2 and Article 1503.3 of the Agreement.

Note that the investor has the right to resort to the dispute settlement mechanism if it has incurred loss or damage as a consequence of the breach of a provision of the Chapter. The fact that the Party receiving the investment has adopted a measure contrary to its obligations under Chapter 11 is not sufficient for a recourse to the dispute settlement mechanism.[60]

Time requirements

The arbitral proceeding may be started up to three years after the date on which the investor acquired knowledge, or should have acquired knowledge, of the alleged breach and of the loss or damage incurred. In other words, the action must be brought within three years.

A disputing investor needs to deliver to the disputing Party written notice of its intention to submit a claim to arbitration at least 90 days before the claim is submitted.[61] The request for arbitration may be submitted six months after the breach of a Party's obligation and the resulting damage for the investor occurred (Article 1120.1). These time periods are important, because the first (90 days) allows the disputing State sufficient time to prepare its defence, and the second

[58] *Article 1115 provides in this regard that the mechanism of Chapter 11 is "Without prejudice to the rights and obligations of the Parties under Chapter 20" (emphasis added).*
[59] *Article 1118.*
[60] *Articles 1116 and 1117.*
[61] *The notice of intent to submit a dispute to arbitration must contain: (i) the name and address of the disputing investor or enterprise; (ii) the provisions of the Agreement alleged to have been breached; (iii) the issues and the factual basis for the claim; and (iv) the relief sought and the approximate amount of damages claimed (Article 1119).*

period (6 months) allows time for the disputing parties to find an amicable settlement of their dispute.[62]

2.2.3 Applicable Rules of Arbitration

If it has not been possible to settle the dispute through consultation and negotiation, a disputing investor affected may submit the claim to arbitration under:

- The Convention on Settlement of Investment Disputes between States and Nationals of other States (ICSID Convention);
- The ICSID Additional Facility Rules; or
- The Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL).[63]

The rules of the ICSID Convention may only be used if the investor's country of origin and the State complained against are both parties to the Convention. The ICSID Additional Facility Rules may be used when either the investor's country of origin or the State complained against, but not both, is a party to the ICSID Convention. At present, since neither Mexico nor Canada is a signatory of the ICSID Convention, this Convention cannot be used in disputes involving them. Therefore, in disputes involving on the one hand the Government of Mexico or Mexican investors, and on the other, the Government of Canada or Canadian investors, the UNCITRAL arbitration rules shall be used. This means that for the time being, disputes arising out of the application of Chapter 11 may only be resolved using the Additional Facility Rules of ICSID or the UNCITRAL arbitration rules. Finally, it is important to note that the arbitration rules chosen shall govern the arbitration except to the extent modified by Chapter 11, Section B.

2.2.4 Decision of an Investor Regarding Submission of a Dispute to Arbitration

In the case of Mexico (Annex 1120.1), the investor can decide between submitting the dispute to the mechanism provided for in Chapter 11, Section B or to the Mexican courts. The investor's decision is final. In other words, once legal proceedings are initiated in Mexico, whether directly or through its investment, the investor loses the right to submit the dispute to arbitration. Conversely, if the investor initiates arbitral proceedings, both the investor and its investment waive the right to have recourse to the Mexican courts.[64]

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[62] *Article 1119.*
[63] *Article 1120.*
[64] *The scope of annex 1120.1 has not yet been interpreted by a tribunal convened under Chapter 11. In fact, although the investor's decision shall be exclusive, the text does not establish in what circumstances the investor is considered to have made its decision. What is clear is that recourse may not be had to the procedure established in Chapter 11 if an investor has submitted a claim of a breach of the NAFTA to the Mexican courts.*

The fact that an investor has exhausted the administrative remedies before the authority that passed the measure does not mean it is considered to have selected the forum. It should be considered that an investor has chosen the local forum when it has submitted a claim before a Mexican court or an administrative tribunal.

The rules governing selection of the forum do not allow the investor to submit the dispute simultaneously to the national courts and to arbitration, thus duplicating proceedings and running the risk of having contradictory resolutions regarding a single act. It also prevents a decision handed down by the Mexican courts or even the Supreme Court of Justice from being reviewed by an arbitral tribunal.

Furthermore, simultaneous proceedings are not allowed in cases where the Party complained against is the United States or Canada, although it is possible to have recourse to the dispute settlement mechanism under this Section after having recourse to the local courts.[65] This means that initiating local proceedings does not deny the investor the right to have recourse to the Chapter 11 mechanisms, but the right to continue such proceeding is waived by the investor at the time it submits a claim to arbitration.[66]

2.2.5 Consent

Normally, submission to arbitration requires the consent of the parties to the dispute and this is no different under the NAFTA.

When the investor submits a claim to arbitration, it is understood that all formalities relating to the Parties' consent to arbitration have been fulfilled.[67]

2.2.6 Composition of the Tribunal

Unless otherwise agreed, the tribunal comprises three arbitrators. Each of the disputing parties appoints one arbitrator and the third arbitrator, who presides over the arbitral tribunal, is appointed by agreement of the disputing parties.[68]

If within 90 days from the date that a claim is submitted to arbitration, one of the disputing parties has not appointed its arbitrator, or the disputing parties have not agreed on the appointment of the presiding arbitrator, the appointments shall be made on the request of either disputing Party or by the Secretary-General of the International Centre for Settlement of Investment Disputes (ICSID).[69]

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[65] *See article 1121.*
[66] *Article 1121*
[67] *Article 1122. The formalities referred to are to be found in Chapter II of the ICSID Convention, in the Additional Facility Rules, in Article II of the New York Convention (of June 10, 1958) and Article I of the InterAmerican Convention (Panama, January 30, 1975).*
[68] *Article 1123.*
[69] *Article 1124.*

The Secretary-General can appoint the missing arbitrator(s) at his/her discretion, but selects the presiding arbitrator from a roster of 45 arbitrators, ensuring that the presiding arbitrator is not a national of either of the disputing parties. If the arbitrators on this roster are unavailable, the Secretary-General may appoint from the ICSID Panel of Arbitrators, a presiding arbitrator who is not a national of either of the Parties.[70]

The roster mentioned in the preceding paragraph was to be created on the entry into force of the NAFTA, and was to contain the names of the 45 arbitrators who may serve as presiding arbitrators. Under the Agreement, this roster should be approved by consensus of the three signatory countries.[71] However, although 10 years have passed since the Agreement entered into force, there is no agreed roster from which the Secretary-General of ICSID can appoint the presiding arbitrator. Instead, the appointment is made by selection from ICSID's own roster, ensuring of course that the presiding arbitrator is not a national of the disputing Parties.

The purpose of maintaining a roster of possible presiding arbitrators was to respond to the concern of the Parties that there should be some consistency in decision-making. It was felt that this would be possible if there were a limited group of persons comprising the arbitral tribunals, who would take decisions on those disputes.

Persons appearing on the rosters shall meet the qualifications for arbitrators established by the ICSID Convention; the Agreement places particular emphasis on their expertise in international law and investment. Specifically, these requirements are: to be of good moral standing; to have recognized competence in the fields of law, trade, industry or finance; to inspire complete confidence in the impartiality of his or her judgement; and to have experience in international law and in investment matters.

The complaining investor must agree in writing to the appointment of each of the members of the tribunal,[72] and this must be delivered to the disputing Party.

2.2.7 Consolidation of Claims

The Agreement provides that, "in the interests of fair and efficient resolution of the claims", the tribunal may, after hearing the disputing parties, authorize that claims be consolidated if they have questions of →

[70] Note that the rules on the nationality of the presiding arbitrator vary according to which roster is chosen. In other words, if the presiding arbitrator is taken from the list of 45 arbitrators agreed by the Parties, the presiding arbitrator shall not be a national of any of the disputing parties; this means that in bilateral disputes, the presiding arbitrator may be a national of the "third Party". On the other hand, if the presiding arbitrator is appointed from the ICSID Panel, he may not be a national of Mexico, the United States or Canada.

[71] Article 1124.4.

[72] Article 1125.

law or fact in common arising from the same violation of a provision of the Agreement.

This type of mechanism is of particular benefit to the State complained against, since it can be difficult or impossible for it to defend itself in a number of proceedings at the same time. It also ensures that different decisions are not taken in relation to the same violation of the Agreement.

Any of the disputing parties may request consolidation; the decision on the request shall be taken by a Tribunal established under the UNCITRAL rules.[73] It was felt that the UNCITRAL rules give the required flexibility for a proceeding of this nature. It should be pointed out that neither the ICSID Convention nor its Additional Facility Rules provides for the procedure of consolidation. A request for consolidation is submitted to the Secretary-General of ICSID and the tribunal should be established within 60 days of receipt of the request for consolidation.

Any disputing party may request suspension of the proceedings in other tribunals until a decision has been taken on consolidation.

The Tribunal shall comprise three members appointed by the Secretary-General of ICSID. The reason for this is that the investors involved would find it difficult to reach a rapid Agreement on the selection of an arbitrator, which they would have to do under a different mechanism.

Owing to the importance of the decisions made in such cases due to the number of subjects involved, the Tribunal members are to be appointed from the roster of 45 arbitrators mentioned above. One of the members should be of the same nationality as one of the investors and the other should be a national of the State receiving the investment.[74] The presiding arbitrator should also be selected from the roster of 45.[75]

When there are no arbitrators available from this roster, the members of the tribunal shall be selected from the ICSID Panel of Arbitrators. If none are available from this Panel, the Secretary-General of ICSID shall make the missing appointments at his/her discretion. In this case, the presiding arbitrator should not be a national of any of the Parties (i.e. Mexico, the United States or Canada).

Other claims not included in the first request for consolidation may be consolidated in this proceeding.

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[73] The Tribunal may: (a) assume jurisdiction over all the claims jointly; or (b) assume jurisdiction over part of the claims and its determination shall serve as a basis for resolving the other claims.

[74] It is important to note that in this proceeding there may be binational disputes (e.g. a number of Mexican investors vs the Government of Canada) or trinational disputes (e.g. Mexican and United States investors against the Government of Canada). This should be taken into account when determining the nationality of the members of the Tribunal.

[75] It is important to note that in this situation, the NAFTA does not establish any requirement relating to the nationality of the presiding arbitrator. See Article 1126.5.

Within 15 days of receipt or presentation of a claim, a disputing State should deliver to the Secretariat of the Free Trade Commission a copy of all the arbitration requests or the notices of arbitration for consideration. The Secretariat should maintain a public register of those documents, so that the interested parties may keep abreast of the proceedings that are taking place.[76]

To date, this Article has not been invoked.

2.2.8 General Provisions

Notice and participation by other Parties

The Agreement provides for participation of a non-disputing Member State in the proceedings as follows:

- A disputing Party shall deliver a written notice of the dispute to the other Parties within 30 days after the date that the claim is submitted (Article 1127);
- The Parties have the right to receive at their own cost a copy of all the written pleadings and evidence presented to the Tribunal which they shall treat confidentially (Article 1129); and
- On a written notice to the disputing Parties, a Party may make submissions to a tribunal on a question of interpretation of the Agreement (Article 1128).

Place of arbitration and governing Law

The arbitration proceedings shall take place in the territory of a Party that is also a party to the New York Convention.[77] This means that the proceedings may take place in any of the three Member countries of the NAFTA, as each of them is a signatory of the New York Convention. The requirement that the proceedings shall take place in a signatory country of the New York Convention is important because the objective is to guarantee the enforcement of arbitral awards through the application of the Convention. The place of arbitration is to be selected under the appropriate arbitration rules.[78]

The tribunal should decide the issues in dispute in accordance with the provisions of the Agreement and the applicable rules of international law. An interpretation by the FTC of a provision of the Agreement is binding on an arbitral tribunal established under Chapter 11.[79]

Interpretation of annexes

As described in the first part of this section, the Member States of the NAFTA have expressed a series of reservations and exceptions relating to investment, which are to be found in annexes I, II, III and IV to the Agreement. When a disputing Party asserts as a defence that the measure alleged to be in breach of the Agreement is within the scope of a reservation or exception set out in the annexes, on request of the disputing Party, the tribunal may invite an interpretation of the FTC on the issue.

[76] *Article 1126.10, 11 and 13.*
[77] *Article 1130.*
[78] *Article 1130.*
[79] *Article 1131.*

The FTC is expected to submit its interpretation in writing to the tribunal within 60 days of delivery of the request, and this interpretation will be binding on the tribunal. Only if the Commission fails to submit an interpretation within the time indicated will the tribunal decide the issue.[80]

Expert reports

The tribunal may, on its own initiative or at the request of one of the disputing parties, and in accordance with the terms and conditions that they themselves may agree, appoint one or more experts to provide a written report on any factual issue concerning environmental, health, safety or other scientific matters raised by a disputing party in the proceedings.[81]

This is without prejudice to the appointment of other experts where authorized by the applicable arbitration rules.

2.2.9 Interim Measures and Awards

Interim measures of protection

A tribunal may order an interim measure of protection to preserve the rights of a disputing party or to preserve evidence in the possession of a disputing Party.[82]

Remedies

The tribunal may award separately or in combination monetary damages plus any applicable interest or restitution of property. In the latter scenario, the tribunal may provide that the disputing party pay monetary damages, plus applicable interest, in lieu of restitution of property. A tribunal may not award punitive damages.[83] However, it may award costs in accordance with the selected arbitration rules.

Final award and enforcement of award

An award has binding force for the disputing parties, but only in respect of the particular case. A disputing Party is expected to comply with an award without delay.[84]

An award is considered final after 120 days have elapsed in the case of ICSID, or 90 days in the case of UNCITRAL, assuming of course that there have been no appeals during that time. These periods relate to the time during which the disputing parties, in accordance with the arbitration rules referred to, may request review or annulment of the award in question. At the end of the period, the investor may request enforcement of the award.

As part of their obligations under NAFTA, the Parties have made a commitment to comply, without delay, with an arbitral award made in accordance with these proceedings. Each Party provides for the enforcement of an award in its territory.[85]

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[80] *Article 1132.*
[81] *Article 1133.*
[82] *Article 1134*
[83] *Article 1135.*
[84] *Article 1136.1 and 2.*
[85] *Article 1136.4.*

If a Party fails to abide by or comply with an award, it is deemed to be in breach of the NAFTA. Consequently, the Party, of which the investor in whose favour the award was made is a national, may submit a request to the FTC to establish an arbitral panel empowered to issue a determination recommending compliance with the final award.[86]

Furthermore, regardless of whether the procedure described in the previous paragraph has been initiated, and to provide security for the disputing investor in whose favour the award was made, the investor may seek enforcement of the arbitral award under the ICSID Convention, the New York Convention, or the InterAmerican Convention.[87]

Publication of an award

In case of Canada and the United States, an award may be made public by any of the parties. In the case of Mexico, the applicable arbitration rules apply (e.g. both the Additional Facility Rules and the UNCITRAL Rules require the consent of both parties for the award to be made public).[88]

2.2.10 Exclusions

The dispute settlement provisions of the NAFTA are not applicable to disputes arising from a decision taken for claims of national security by the Parties with a view to prohibiting or restricting the acquisition of an investment in its territory by an investor of another of the Parties.[89] The dispute settlement provisions of NAFTA do not apply to a decision taken by the National Commission on Foreign Investment (*Comisión Nacional de Inversiones Extranjeras*) in Mexico, or in Canada under the *Investment Canada Act*, with respect to whether or not to authorize an acquisition by a foreign enterprise.[90]

Although not strictly exclusions, it is important to mention that in the Agreement there are other provisions that restrict or modify the mechanism set out in this section. Such is the case with disputes involving the provisions of the Chapter on financial services. Where financial services are concerned, the mechanism of Chapter 11, Section B is applicable only to the provisions on transfers, special formalities, denial of benefits and the environment (Article 1401.2), and a Financial Services Committee is established with responsibility to decide on disputes in financial services (Articles 1412 and 1415).

Similarly, Article 2103 (on taxation) provides that if it is claimed that a taxation measure is tantamount to expropriation, the matter shall be referred to the competent authorities of the countries concerned, which shall determine whether or not the tax amounts to an expropriation. If the authorities consider it to be an expropriation, or if no decision is reached within six months, an

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[86] *Article 1136.5.*
[87] *Article 1136.6.*
[88] *Article 1137.4 and Annex 1137.4 apply.*
[89] *Provisions issued on grounds of national security under the United States Exon-Florio Act may not be appealed. This Act entitles the President of the United States to block any acquisition by foreign investors on the ground of national security.*
[90] *Annex 1138.2.*

investor may submit the dispute for resolution in accordance with the procedures of Chapter 11, Section B.

2.3 Cases

2.3.1 Published Information About Cases

Proceedings are not necessarily made public from the outset, because disputes are settled in accordance with the arbitration rules chosen by the investor (i.e. the ICSID Additional Facility Rules or the UNCITRAL Arbitration Rules).

A dispute considered under the Additional Facility Rules is administered by ICSID. The start of the proceedings is made public through the channels available to ICSID (i.e. the Centre's web page and periodical publications in which the cases being heard are listed).

The initiation of arbitration of a dispute handled under the UNCITRAL Arbitration Rules is not made public unless one of the parties makes it public. Tribunals established under the UNCITRAL Rules have generally stipulated what kind of information must be considered confidential and what may be made public by one of the parties. They have determined that the Notice of Intent, Notice of Arbitration**,** Statement of Claim and Statement of Defence may be made public.

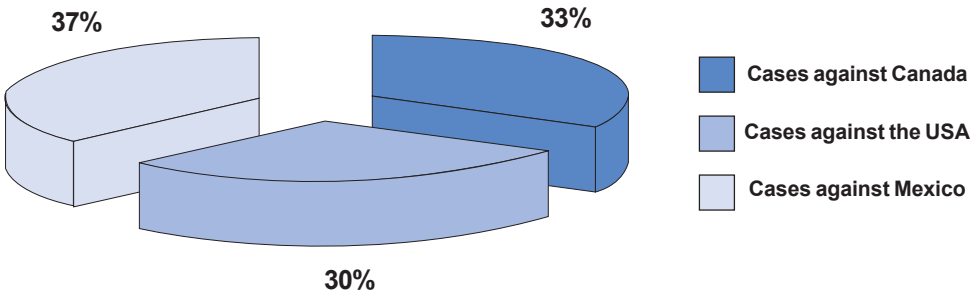
Most proceedings initiated under Chapter 11 have been published on an Internet site called "NAFTA Claims", based on a private compilation made by a student of the subject. While this is the most complete source of these proceedings, it does not constitute an official source.

In July 2001, the FTC, in the exercise of its powers to interpret the provisions of NAFTA, issued an opinion on the subject of transparency in the context of the dispute settlement procedure of Chapter 11. It specified that "nothing in the Agreement imposes an obligation of confidentiality" and "nothing prevents the parties from delivering documents submitted to the tribunal or issued by them", subject to the specific rules governing the proceeding.

2.3.2 Case Statistics

There is no official source that gives an exact picture of the disputes settled using the dispute settlement mechanism of Chapter 11. With this proviso, and based on available information as at August 9, 2002, 27 cases have been initiated using this mechanism. Of these, 9 were brought against the Government of Canada,[91] 8 against the Government of the United States[92] and 10 against the Government of Mexico.[93]

Cases under Chapter 11 of the NAFTA (as of August 2002):



The Articles of the NAFTA alleged to have been breached by the Parties complained against related to: national treatment (1102); fair and equitable treatment (1105); performance requirements (1106); expropriation (1110) and State enterprises (1503).

2.4 Summing up

Despite criticism, the Agreement gives investors an impartial mechanism providing adequate protection to their investments in the Member States. Chapter 11 still faces many challenges, especially as regards making its processes more transparent. As more subjects are brought before tribunals established pursuant to this Article, a stock of precedents will be built up, which ultimately will contribute to giving greater certainty to governments and investors alike with regard to the treatment and protection that should be granted.

2.5 Test Your Understanding

1. **Does the principle of exhausting domestic remedies apply to the proceedings under Chapter 11?**
2. **What qualifications should the arbitrators have to be selected as members of a tribunal constituted under Chapter 11?**
3. **What elements should be taken into account when selecting the arbitration rules applicable to the proceedings?**
4. **What are the rules of transparency and confidentiality that apply to the proceedings?**
5. **Do you think that a permanent body would present advantages for the mechanism?**

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[91] *The cases brought against Canada were as follows (by name of the disputing investor): Signa S.A. de C.V., Ethyl Corp, Sun Belt Water, S.D. Myers, Poep & Talbot, U.P.S, Ketchum Investment Inc. and Tysa Investment Inc., Crompton Corporation and Trammel Crow Company.*

[92] *The cases brought against the United States were: Loewen Group, Methanex, Mondev International, Canfor Corp, Tembec Corp Limited, Kenex Ltd. and Doma Industries.*

[93] *The cases brought against Mexico were: Halchette Distribution System, Robert Aznian, Metalclad Corporation, Waste Management I, Waste Management II, Marvin Ray Feldman, Adams et al, Gami Investments Inc. and Fireman's Fund.*

3. CHAPTER 19 OF THE NAFTA: DISPUTES RELATING TO UNFAIR TRADE PRACTICES

Objectives

After studying this section, the reader should be able to:

- **Identify the types of disputes that are heard in proceedings under Chapter 19 of the Agreement;**
- **Define the mandate of the panel established pursuant to this Chapter;**
- **Analyse the review criteria that a panel must apply; and**
- **Evaluate the experience that has been developed up to now through the disputes that have been submitted to these proceedings.**

Chapter 19 of the Agreement establishes procedures for the review of statutory amendments to the domestic legislation on anti-dumping and countervailing duty of the Parties (section 3.2 of this Module), as well as for the review of final determinations as regards dumping and subsidies (section 3.3 of this Module), before binational panels (section 3.4).

The objective of the Agreement is to establish fair and predictable conditions for the progressive liberalization of trade between the Parties while maintaining effective and fair disciplines on unfair trade practices.[94]

In this context, Chapter 19 establishes procedures which seek to ensure that domestic legislation on unfair trade practices shall not be applied by a Party in a manner that creates unnecessary obstacles to the trade of another Party, or that gives unfair protection to the national industry of a Party adopting such legislation.

3.1 Definitions

For an understanding of the trade effects of dumping and subsidies and the disciplines established by the World Trade Organization, please refer to Modules 3.6 and 3.7 of this Course.

3.2 Review of Statutory Amendments

Chapter 19 concerns: (a) existing domestic legislation on unfair trade practices at the time of the entry into force of the NAFTA on 1 January 1994; and (b) amendments to domestic legislation in the field of unfair trade practices.

[94] *Article 1902.2(d)ii.*

3.2.1 Retention of Domestic Legislation

The Agreement authorizes each Party to continue to apply its domestic legislation on dumping and subsidies to goods imported from the territory of another Party. Domestic legislation includes statutes, legislative history, regulations, administrative practice and judicial precedent.[95]

3.2.2 Amendments to Domestic Legislation

Each Party agreed to introduce, by the date of the entry into force of the Agreement in 1994, a number of amendments in its domestic laws on unfair trade practices.[96] The general nature of the amendments is identified in Article 1905.15. Specific amendments for adoption by each Party are set out in a schedule to the Agreement (Annex 1904.15). The purpose of the amendments is to create greater similarities between the procedural rules concerning unfair trade practices of the Parties.

3.2.3 Statutory Amendments to Anti-dumping and Countervailing Duty Laws

Each Party reserves the right to change or modify its antidumping and countervailing duty laws, provided that:

1. Before enactment of the amendment, the Party proposing the amendment shall:

- Notify in writing the other Parties; and
- Consult with that Party, if requested, before the enactment of the amendment.

2. The proposed amendment should not be inconsistent with:

- The *General Agreement on Tariffs and Trade* 1994 (GATT), the *Agreement on Implementation of Article VI of the GATT 1994* (the Anti-dumping Code) or the *Agreement on Subsidies and Countervailing Measures*; or
- The object and purpose of the NAFTA and Chapter 19, which is to establish fair and predictable conditions for the progressive liberalization of trade between the Parties while maintaining effective and fair disciplines on unfair trade practices.[97]

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[95] *Article 1902.1*
[96] *Article 1904. 15.*
[97] *Article 1902. 2. d (i) and (ii).*

3.2.4 Disputes Concerning Statutory Amendments

A Party may request in writing that an amendment of another Party's antidumping or countervailing duty laws shall be referred to a binational panel for a declaratory opinion as to whether: (a) the amendment is consistent with the provisions of Article 1902.2 quoted above; or (b) the proposed amendment seeks to overturn a prior decision of a binational panel.[98]

Panel procedures

The binational panel establishes its own rules of procedure, unless the Parties agree otherwise prior to the establishment of that panel. The procedures should ensure a right to at least one hearing before the panel, as well as the opportunity to provide written submissions and rebuttal arguments. The proceedings of the panel are confidential, unless the two Parties agree otherwise. The panel bases its decisions solely on the arguments and submissions of the two Parties.

Unless the Parties to the dispute agree otherwise, the panel presents to the Parties, within 90 days after its chairperson is appointed, an initial written declaratory opinion containing findings of fact and its determination.

If the findings of the panel are affirmative, the panel may include in its report its recommendations as to the means by which the statute that is being amended could be brought into conformity with the provisions of Article 1902(2)(d). In determining what, if any, recommendations are appropriate, the panel considers the extent to which the amending statute affects interests under this Agreement. Individual panellists may provide separate opinions on matters not unanimously agreed. The initial opinion of the panel becomes the final declaratory opinion, unless a Party to the dispute requests a reconsideration of the initial opinion.

Within 14 days of the issuance of the initial declaratory opinion, a Party to the dispute, disagreeing in whole or in part with the opinion, may present a written statement of its objections, and the reasons for those objections, to the panel. In that event, the panel can request the views of both Parties and may reconsider its initial opinion. The panel shall conduct any further examination that it deems appropriate, and will issue a final written opinion, together with the dissenting or concurring views of individual panellists, within 30 days of the request for reconsideration.

The final declaratory opinion of the panel is made public, along with any separate opinions of individual panellists and any written views that either Party may wish to be published, unless the Parties to the dispute agree otherwise.

Meetings and hearings of the panel take place at the office of the amending Party's Section of the Secretariat, unless the Parties to the dispute agree otherwise.[99]

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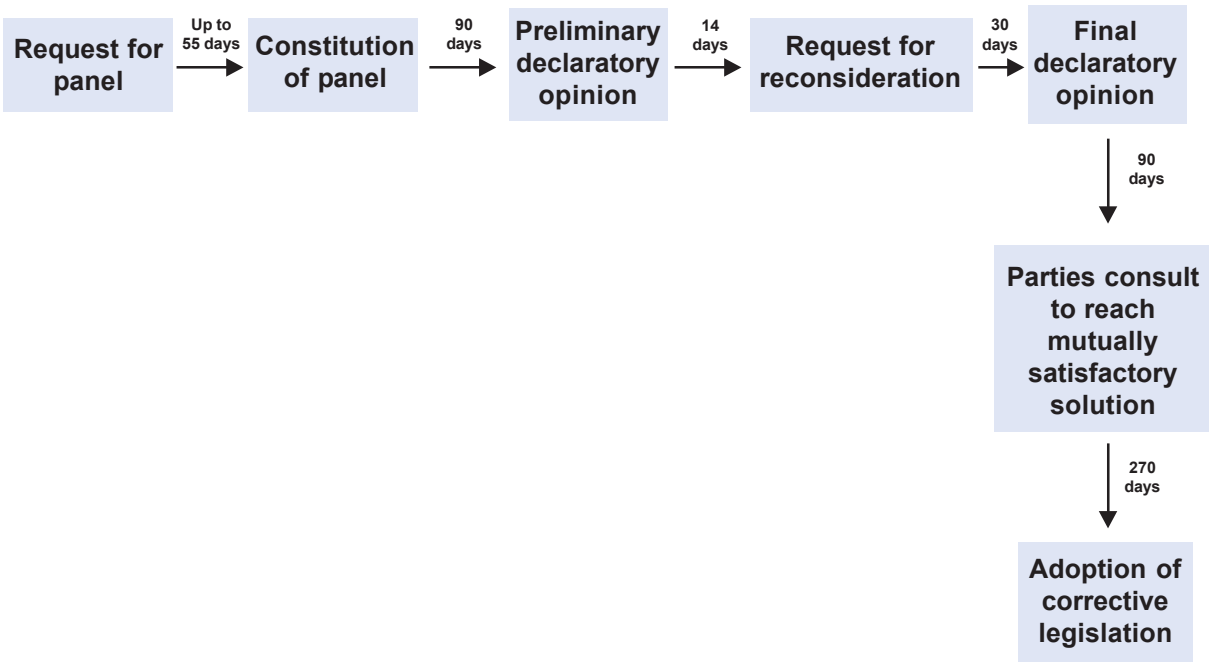
[98] *Article 1903.1.*
[99] *Annex 1903.2.*

The procedures for reviewing statutory amendments may be illustrated as follows:



Corrective action

In the event that the panel recommends modifications to the proposed amendment to remedy a non-conformity that it has identified in its opinion: the two Parties can immediately begin consultations and seek to achieve a mutually satisfactory solution to the matter within 90 days of the issuance of the panel's final declaratory opinion. Such a solution may include seeking corrective legislation with respect to the statute of the amending Party.

If corrective legislation is not enacted within nine months from the end of the 90-day consultation period, and no other mutually satisfactory solution has been reached, the Party that requested the panel may either take comparable legislative or equivalent executive action, or terminate the Agreement with regard to the amending Party on 60 days' written notice.[100]

3.3 Review of Final Anti-dumping and Countervailing Duty Determinations

Article 1904.1 requires that each Party replace its judicial review of final anti-dumping and countervailing duty determinations with a binational panel review carried out in accordance with its provisions. An exporting Party may request that a panel review a final anti-dumping or countervailing duty determination

[100] *Article 1903.3.*

made by a competent national investigation authority of an importing Party in order to judge whether it was made in accordance with the anti-dumping or countervailing duty laws of the importing Party. In other words, the review procedure represents an alternative to the judicial review provided for in the domestic law of the Parties.[101]

A review by a binational panel of final determinations may be requested only by a Party acting either on its own initiative or at the request of a person authorized under the domestic laws of the importing Party to request a judicial review before a judicial or administrative authority of the latter.[102]

3.3.1 Choice of Forum

National fora

The Agreement does not abolish the possibility of submitting a final determination for review to a judicial authority in the importing Party. Domestic procedures for judicial review of a final determination may not be commenced until a period of 30 days following the publication of the final determination has elapsed..[103]

In other words, the complaining Party has the choice between a review by a binational panel established under Chapter 19 or a judicial review under the domestic legislation of the importing Party.

International fora

The WTO also has a procedure for review of final determinations of countervailing and dumping measures. This means that the Members of the NAFTA can choose between the following fora:

- A judicial review provided for in the domestic legislation of the importing Party;
- A binational panel established under Chapter 19, or
- The procedures of the Dispute Settlement Understanding of the WTO.

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[101] *The replacement mentioned in Article 1904.1 should not be interpreted in such a way that the binational panel provided for in the NAFTA renders incompetent the courts and administrative bodies of each Party, but it should represent an exclusive alternative to the review that may be carried out before such courts and bodies. In other words, the objective was not to establish a supranational tribunal, but to provide an alternative for the review of the determinations of the investigating authorities. See Thomas, J.C. and Sergio López Ayllón "El capítulo XIX del Tratado de Libre Comercio de América del Norte: desafíos en la interpretación de los tratados internacionales y en la reconciliación del civil law y el common law en la zona de libre comercio" [Chapter 19 of the North American Free Trade Agreement: challenges in the interpretation of international agreements and the reconciliation of civil law and common law in the free trade area] in Revista de Derecho Privado [Journal of Private Law], year 6, num. 20, 1996.*

[102] *Article 1904.50. See the definition of "interested person" in Rule No. 3 of the Rules of Procedure of Article 1904.*

[103] *Article 1904.15 (c) (i), Article 1904.4 in fine, and Article 1904.11.*

3.3.2 Relationship Between Chapter 19 and Domestic Legislation of the Parties

In reviewing whether a product has been imported on discriminatory terms, causing or threatening to cause material damage to the domestic industry, a binational panel seeks to establish whether or not the national authorities acted in accordance with the legal provisions of the importing Party. The task of determining whether an unfair trade practice exists and, where applicable, of imposing a duty, rests in the first instance with the competent authorities of each Party.

3.3.3 Review

The request for a panel should be made in writing by a Party to the other Party within 30 days following the publication of the final determination. A request made within this time period renders a judicial review of the final determination in the importing Party inadmissible. In other words, review before binational panels has precedence over domestic judicial review. In addition, the decision of a binational panel may not be appealed to a domestic court.[104]

Remit of the panel

The task of the binational panel is to review whether the national authority that investigated the allegedly unfair import of goods issued a determination that is or is not in accordance with the statutes, legislative history, regulations, administrative practice and judicial precedents of the importing Party. This means that the panel interprets and applies the domestic legislation of the Party importing the goods.

Standard of review

The standard of review that a panel applies is stipulated for each Party in Annex 1911 of the Agreement. In the light of the domestic legislation of each Party it appears that the binational panel is required to:

- Confirm the competence of the authority that conducted the proceedings and issued the final determination;
- Review whether the procedural formalities required by the applicable domestic laws were observed; and
- Whether the facts giving rise to the claim were sound.

Panel procedures

The panel applies the Rules of Procedure of Article 1904 and the Code of Conduct for Dispute Settlement Procedures of Chapters 19 and 20 of the Agreement (Code of Conduct).

(i) Rules of Procedure[105]

The following principles apply:

[104] *Article 1904.2.*
[105] *Rules of Procedure for Article 1904 - Extraordinary Challenge Committees.*

- Limitation of the remit of the panel to claims of errors of fact or of law that are set out in the statements of claim submitted by the Parties, and to the procedural and substantive defences raised by the Parties.
- Freedom of the panel members to adopt rules of procedure and to conduct proceedings as they consider appropriate, provided that the disputing Parties have not agreed otherwise, and that they do so in accordance with the provisions of Chapter 19 and these Rules.[106]
- Right of the investigating authority to appear and be represented by counsel.
- Right of other authorized persons to appear and be represented by counsel
- Obligation to submit documentation relating to the final determination to which the panel review relates.
- Protection of proprietary or privileged commercial information submitted by the disputing Parties, by the investigating authority or by any person interested in the matter.
- Definition of the content and form of the pleadings of the Parties presented to the panel, number of copies, notes on the confidential nature of certain documents.
- Respect for the right to a hearing and the principle of adversarial proceedings.
- Responsibility of the disputing Parties to assume the direct and indirect costs of their participation in the panel review proceedings.

(ii) Code of Conduct[107]

Experts appointed to a binational panel must act pursuant to the provisions of a Code of Conduct, i.e. respecting standards of:

- Impartiality;
- Integrity;
- Honesty;
- Confidentiality;
- Personal conduct, and
- Full and timely performance of their functions.

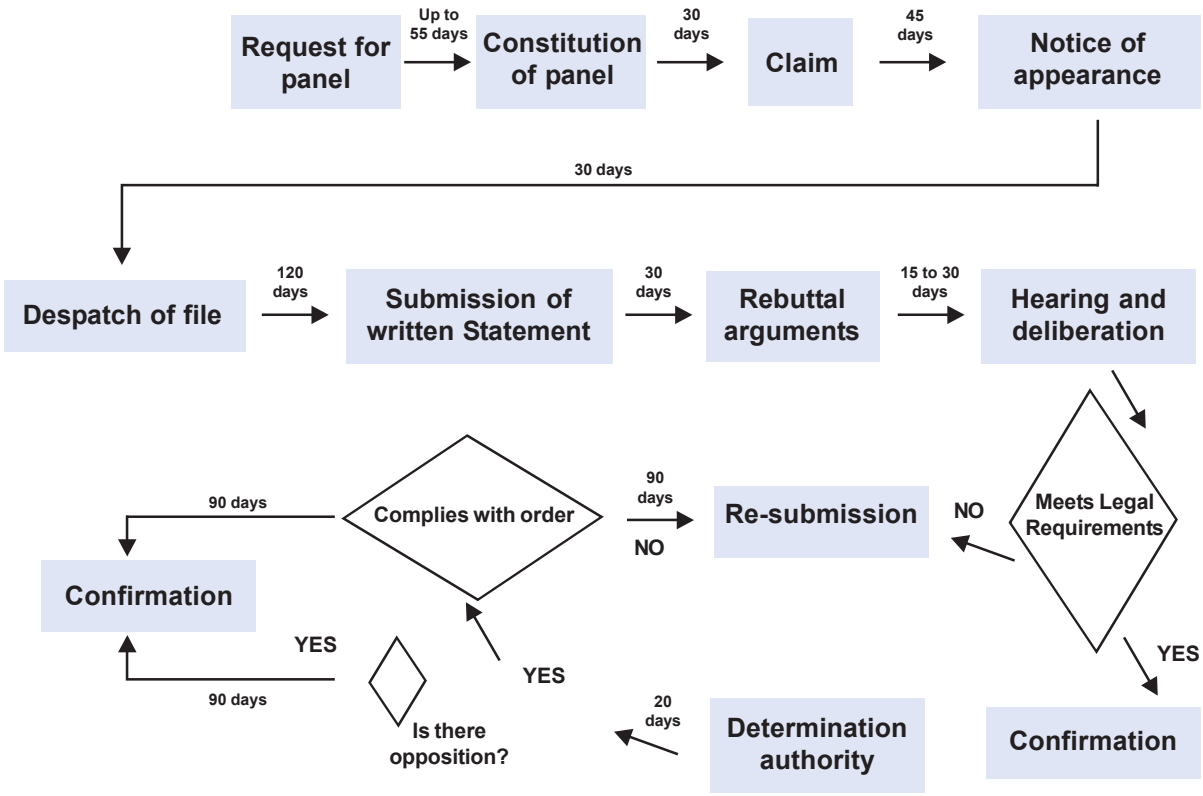
(iii) Functions of the Secretariat in the Proceedings

The Secretariat provides administrative assistance to the panels, organizes hearings and meetings, and makes translations and transcripts which the panels require for the proper performance of their task. The principal obligations of

[106] *See Rule No. 20 of the Rules of Procedure of Article 1904.*
[107] *Code of Conduct for Dispute Settlement Procedures under Chapters 19 & 20 of the NAFTA.*

the Secretariat in the administration of the proceedings are set out in rules 8 to 16 of the Rules of Procedure of Article 1904[108].

Summing up, the review of final determinations before a binational panel involves the following stages:



Panel decision

The decision of the panel is binding on the Parties and may:

- Confirm the final determination that was challenged, or
- Remand the final determination to the investigating authority for action that is consistent with the decision of the panel.

In the latter case, the investigating authority delivers a report specifying how the measures recommended by the panel were implemented. This report is to be delivered within the time period specified by the panel in its decision.[109]

[108] *See also Rules 22 and 23 of the Rules of Procedure of Article 1904.*

[109] *Article 1904.8. In fixing this time period, the panel shall take account of the complexity of the matter and the nature of its decision. The time period fixed by the panel shall in all cases be no more than the maximum period allowed by domestic legislation for an investigating authority to make a final determination in an investigation of unfair practices.*

3.3.4 Extraordinary Challenge

Although Article 1904 prohibits a domestic appeal against the determination of a binational panel, it provides for an extraordinary challenge procedure before a Committee.[110] This Committee may only be convened at the request of the Governments of the three countries and shall comprise three federal judges, the disputing Parties appointing each one, and the third appointed by the Party that is selected by the drawing of lots.

A Party may request that an Extraordinary Challenge Committee be convened if it considers that:

- A panellist is in serious violation of the Code of Conduct;
- A panel seriously departs from a fundamental rule of procedure; or
- The Panel manifestly exceeds its powers.

Furthermore, the Party that challenges the panel's determination must prove that the grounds for challenge put forward did indeed:

- Affect the validity of the panel's decision; and
- Represent a threat to the integrity of the panel review.

It is clear from the above that the object of the extraordinary challenge proceedings is not to appeal against the substance of the panel's determination, but to review whether the panel proceedings were affected by a material violation of the procedural rights of the Parties.

Within 90 days following its formation, the Committee is expected to issue a binding determination to:

- Confirm the panel's determination;
- Set aside the panel's determination, in which case a new panel shall be established, or
- Remand the determination back to the original panel for stipulating measures to be adopted that are consistent with its decision.

3.3.5 Safeguarding the Panel Review System

Chapter 19 provides also for a procedure to safeguard the binational panel review system. This procedure came into being as a result of concerns over domestic challenges to the determinations of binational panels, especially in Mexico where domestic legislation provides for the *juicio de amparo* (challenge on the grounds of unconstitutionality).[111]

[110] *Article 1904.13*

The safeguarding procedure begins with a consultation phase between the Parties concerned. If a successful conclusion is not reached within 45 days, a Special Committee is formed.[112]

The interested Party may request a determination as to whether another Party's domestic law has:

- Prevented the establishment of a binational panel;
- Prevented the panel from rendering its decision;
- Challenged the binding nature of the decision or prevented its implementation; or
- In any way unjustifiably opposed the conduct of the review mechanism provided for in Article 1904.

Annex 1905.6 of Chapter 19 establishes certain principles for safeguarding the Special Committee procedure. These principles are similar to the procedural provisions in other mechanisms provided for in the NAFTA, such as the right of the Parties to at least one hearing, the opportunity to make written submissions and rebuttals, and the confidentiality of the procedure are guaranteed. However, there are time periods and features specific to the safeguarding procedure,.

Once the Committee has issued its initial report and the Parties' observations have been received, a final report is issued after having been sent to the Parties. In this report, the Special Committee determines whether the Party complained against has indeed been guilty of one or more of the failings mentioned above, and orders reparation, unless the Parties are able to agree on another mutually satisfactory solution. Failing that, the complaining Party may suspend either the right of the adverse Party to request the formation of panels pursuant to Article 1904 or the application of other benefits. At the request of the Party whose benefits have been suspended, the Special Committee may assess whether or not that suspension is excessive.

3.4 Binational Panels and their Establishment

Chapter 19 provides for the establishment of binational panels to review: (a) proposed amendments to domestic legislation; and (b) final determinations of countervailing duty and anti-dumping. In both cases, the panels comprise five members, selected from a roster of 75 professionals compiled by the three countries (25 appointed by each Party).

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[111] *According to the Mexican Legal Dictionary of the Legal Research Institute of the UNAM, "the Mexican juicio de amparo constitutes .... the last challenge procedure for judicial, administrative and even legislative proceedings, for which reason it protects the whole domestic legal system from violations by any authority, provided that such breaches translate into an actual, personal or direct impact on the rights of a legal person, whether individual or collective."*

[112] *Special Committees that consider the safeguarding mechanism are formed in the same way as Extraordinary Challenge Committees. Articles 1904.4 and 1904.5 and Annex 1904.13.*

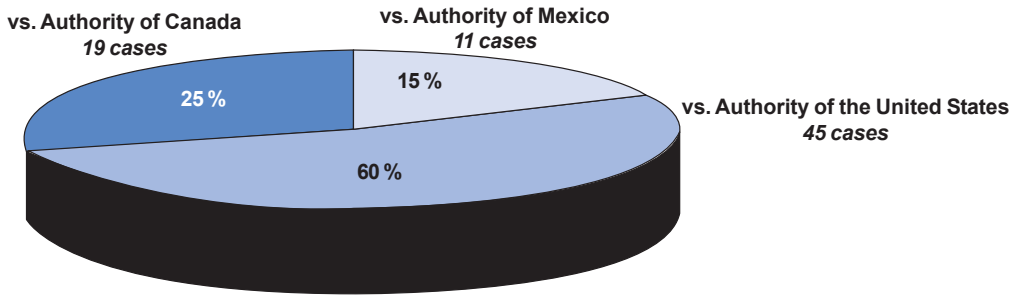
Following the request for a Panel:

- Each involved Party, in consultation with the other, shall have 30 days to appoint the panellists;
- Both involved parties shall have 45 days to put forward any challenges they consider relevant; and
- The fifth member of the panel shall be appointed within 55 days following the request for a panel.

Appointments of panellists or replacements of challenged panellists that are not made within the established time periods are to be made from the above-mentioned roster by the drawing of lots, except in the case of the fifth panellist, who shall be appointed by the Party chosen to do so by the drawing of lots. Selected panellists must in all cases meet the standards of good reputation, standing, objectivity, good judgement, trustworthiness and knowledge of international commercial law. Prospective panellists must also guarantee their neutrality and independence vis-à-vis the Parties, and respect the Code of Conduct established by them.

Statistical Data[113]

Cases by investigating authority (as of January 2002):



Number of cases initiated on the basis of Chapter 19:

Cases	Mexico	USA	Canada	Total
Concluded	5	11	10	26
Withdrawn	3	14	4	21
Pending	3	20	5	28
Total	**11**	**45**	**19**	**75**

[113] *Tables produced using information, as at January 2000, from the Secretariat of the Economy of Mexico and the Mexican Section of the NAFTA Secretariat, with the help of Beatriz Léycegui and Mario Ruiz Cornejo.*

Average duration of cases:

Cases	Process (26 cases)	Formation of Panel (38 cases)	Implementation of Decision (26 cases)
Canada (days)	522	164	148
USA (days)	568	303	138
Mexico (days)	843	184	260
Average (days)	**603**	**245**	**165**

3.5 Summing up

Chapter 19 provides for annual consultations between the competent investigating authorities of the Parties relating to the legislation, administrative practices and the functioning of binational panels in the field of unfair trade practices. The Parties also agreed to ensure adequate administration of applicable legal provisions, which will no doubt encourage consistency between the Parties and the legal security of producers in general.

Even with the difficulties and inequalities that may arise from the review of administrative determinations of the domestic investigating authorities of Member States, caused in part by the different standards of review applied in the countries, the binational panels have achieved their aim of preventing national authorities from using their laws on unfair trade practices as instruments for the protection of their domestic industry.

3.6 Test Your Understanding

1. **Who are the parties in a dispute contemplated in Chapter 19?**
2. **Are the proceedings before a panel established in accordance with Chapter 19 always confidential?**
3. **Regarding disputes on statutory amendments, is the initial opinion of the panel binding for the parties?**
4. **Who is able to request a review of a final anti-dumping determination?**
5. **What is the objective of an extraordinary challenge?**

4. CONCLUDING REMARKS

Ten years on from the entry into force of the NAFTA, the three dispute settlement mechanisms have generally achieved the purpose for which they were created. However, they have also displayed certain weaknesses. Nonetheless, each of them has helped considerably in the functioning of the Agreement and its objectives. Moreover, as an instrument that allows for constant development and reflection through the bodies it has created (i.e. the various committees and working groups), the Agreement is in a position to identify the weaknesses that each mechanism has displayed and to improve the procedures:

General mechanism (Chapter 20)

The main weakness of the general dispute settlement mechanism has been the difficulty in forming panels. The aim of having a quasi-permanent mechanism through the establishment of a roster of candidates has broken down because the countries do not view the finalization of the roster as a priority.

There are various proposals that need to be analysed by the member countries. With the WTO Understanding on Dispute Settlement currently in the process of being reviewed, this is a good time for the members of the FTC to consider what general mechanism the FTC needs in order to be able to meet the future challenges and respond effectively to the ever more complex problems that face the three nations as a result of their increasing interaction. Topics such as transparency, confidentiality, establishment of a permanent system of panellists, the implementation of panel decisions and the establishment of compensatory measures play an important role in a phase of renewal.

The case settled between the United States and Mexico regarding cross- border trucking services has shown that disputes between nations are not immune from political pressure. Whichever mechanism is adopted, success depends on political will and the conviction that the integrity of the Agreement, which overall is beneficial to the three countries, must be safeguarded through the implementation of commitments, including the decisions of panels.

Special mechanism for investment disputes (Chapter 11)

The very existence of a dispute settlement mechanism that can be directly invoked by a complaining investor when making investments in another country is in itself a triumph for the NAFTA and is considered as a relevant factor in attracting investment into the free trade area.

Interestingly, it was initially thought that Mexico would be the country that would have to face almost all the claims, because of its status as an importer of capital, and because it was felt that an investor was liable to greater discrimination and violations there than in countries such as the United States and Canada. However, the reality has been different; all three countries have experienced a similar number of claims. It is certainly true that Chapter 11 may lend itself to "frivolous" disputes, especially because the text of the Chapter has invited interpretations of the extent of its obligations. However, this

mechanism will develop in the future, and the actual decisions of the tribunals will settle any current problems of interpretation.

Nevertheless, it is clear that the mechanism of Chapter 11 can be improved. What is certain is that the greatest weakness of the mechanism lies in the process for setting aside awards, as highlighted by the *Metalclad* case. After having obtained an award against the Mexican Government, Metalclad (the investor) had to face a setting aside procedure, initiated by Mexico, before the British Columbia Courts since the arbitration took place in Vancouver. A possible solution to this problem might be the creation of a permanent body designed specifically to serve as a forum for extraordinary challenges of awards.

It is still difficult to judge the effectiveness of this mechanism, especially given that most cases have not reached a conclusion. However, the very existence of the mechanism regulates the actions of the States and contributes to the objective of establishing clear rules for investments in the member countries.

Special mechanism for unfair trade practices

This mechanism, doubtless unique in that it replaces judicial review of anti-dumping and countervailing duty determinations of each State, has basically achieved its aim since it has allowed the Parties to monitor the application of national laws in this matter on behalf of national authorities.

By its nature, this mechanism has faced a number of criticisms. Perhaps the main one lies in the differences in standards of review that each panel must apply under the laws of each country. Indeed, the standard of review applicable in the United States gives significant weight to the decisions of administrative authorities, while in Mexico, that weight is not applied in judicial courts reviewing administrative decisions. However, despite the different weighting and taking everything into account, in half the cases that have reviewed decisions of the United States authorities, the determination has been sent back to those authorities for correction or clarification, in accordance with the panel's instructions.

Also, the different legal traditions of the Parties (i.e. common law Vs civil law) has involved a learning process, particularly for Mexico, given that the mechanism was created by two States that have a common law tradition.

The major operational criticism that can be made of this mechanism is the difficulty of convening panels, due to the absence of an agreed roster of panellists.

However, until the three countries can develop a regime in this matter that minimizes the friction and uncertainty caused by the application of measures against unfair trade practices, this mechanism will have to continue operating to the benefit of the three countries.

4.1 Test Your Understanding

1. **In what respects could each of the dispute settlement mechanisms be improved?**
2. **Do you think that Mexico has benefited from the establishment of the three dispute settlement mechanisms?**
3. **Do you think that the existence of the three mechanisms is justified in the light of NAFTA's objectives and the results achieved to date?**
4. **Why do you think the Parties have not been able to agree on the composition of the different rosters contemplated in the NAFTA?**
5. **What is the role of the Secretariat in the three dispute settlement mechanisms?**

5. CASES

5.1 Chapter 20 case

Factual background

Tariff Quota on Diapers Imposed by Canada

For the past 25 years (since 1972), Canada has maintained tariff rate quotas on imports of diapers.[114] The structure of the most favoured nation (MFN) tariffs has been as follows:

A quantity of 10,000,000 diapers could enter at a duty of 15 per cent *ad valorem*. For imports in excess of that amount, the applicable duty was 10 cents each for diapers valued at not more than 50 cents each and 21 per cent *ad valorem* for diapers valued at over 50 cents each.

The NAFTA Tariff Provisions on Diapers

Under the North American Free Trade Agreement (NAFTA or the Agreement), Canada agreed to grant preferential tariff treatment to imports of diapers coming from the United States of America (USA), as follows:

All diapers valued at not more than 50 cents became duty free as of the date of entry into force of the Agreement on 1 January 1994;

For diapers valued at over 50 cents, a tariff rate quota was created under which the first 10,000,000 were duty free; imports in excess of 10,000,000 were subject to a duty of 12.7 per cent *ad valorem* for calendar years 1994 through 1996; 10 per cent for 1997 through 1999; and zero duty thereafter.

These tariff rates were entered in the Canada Schedule to Annex 302.2 of Chapter Three of NAFTA

According to the Section 2 of Annex 300-B:

> *"Except as otherwise provided in this Agreement, each Party shall progressively eliminate its customs duties on originating textile and apparel goods in accordance with its Schedule to Annex 302.2 (Tariff Elimination), and as set out for ease of reference in Appendix 2.1."*

Moreover, Article 302 provides:

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[114] *5601.10: Sanitary articles of wadding of textile materials, including sanitary towels, tampons and diapers.*

1. Except as otherwise provided in this Agreement, no Party may increase any existing customs duty, or adopt any customs duty, on an originating good.
2. Except as otherwise provided in this Agreement, each Party shall progressively eliminate its customs duties on originating goods in accordance with its Schedule to Annex 302.2.

The NAFTA Safeguards Provisions

Chapter 8 of the NAFTA,[115] "Emergency Action," allows Parties' governments to impose temporary tariff increases ("safeguard measures") otherwise prohibited by the obligations of Chapter 3, whenever it is determined that increasing imports are causing or threatening to cause serious injury to domestic industries under certain specified conditions.

Safeguards Procedures in Canada

Under Canadian law, any national company or person requesting the imposition of safeguard measures on imports of a particular product may file a petition with the Foreign Trade Committee (FTC). The Committee determines whether imports of such a product are causing or threatening to cause serious injury to domestic sectors. If the FTC's determination is affirmative, the Committee is entitled to adopt safeguard measures that should be ratified by the Minister of Commerce of Canada.

The Canadian Safeguards Proceedings on Diapers

On 17 June 1995, the Canadian Textile Chamber filed a petition under the provision of Canadian law authorizing global safeguard actions before the FTC. The petition alleged that diapers were being imported into Canada in such quantities as to be a substantial cause of serious injury to the domestic industry.

The FTC made its affirmative injury determination on 14 November 1995. Following that determination, the Committee adopted the following safeguard measures, to be in force as of that date, for a two-year period.

Diapers from the United States valued at no more than 50 cents were to remain duty free under NAFTA if imported in quantities within the global tariff quota of 10,000,000, but if imported in quantities over 10,000,000, they would become subject to an over-quota tariff rate of 15 cents in the first year, to be reduced to 7.5 cents in the second year, and then to zero in accordance with the NAFTA schedules.

The Canadian Minister of Commerce ratified the FTC determination.

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[115] *Reference to Articles 801, 802 and 803.*

The NAFTA Dispute Settlement Proceedings

On 15 December 1995, the United States requested formal consultations under Article 2006.4 of the NAFTA. Consultations took place on 12 and 13 January 1996 but they failed to resolve the dispute. Therefore, pursuant to NAFTA Article 2007, on 10 February 1996 the Government of the United States requested a meeting of the FTC.

The FTC met on 23 March 1996, but did not find a solution to this case.

Following the United States request on 1 August 1996, for establishment of a panel under Article 2008 of the NAFTA, this was constituted on 18 February 1997.

Exercise

Based on the above-mentioned facts, prepare and discuss the arguments of the Parties, and imagine the different stages of the procedure before the panel.

5.2 Chapter 11 case

Factual Background

In 1995, Mr. John Bradley (JB) purchased land in Acapulco. Upon his death on 10 March 1998, his four children inherited the land in *pro indiviso* equal shares. On 4 July 1998, Laura Bradley (LB), one of such four children, purchased the *pro indiviso* shares of her siblings, thus owning the totality of the land.

Upon her death on 1 December 1999, her children, Peter Smith (PS) and Emily Smith (ES), born in Vancouver, inherited the land in *pro indiviso* equal shares. Since PS's will was executed in Mexico City, PS and ES were recognized as legitimate heirs and joint *albaceas* (executors) of PS's Estate. However: (i) the land had not been adjudicated to PS and ES; (ii) the title to the land was still in LB's name; and (iii) the Estate had participated in all administrative and judicial proceedings related to the land.

PS's claim arose from the fact that the local government of Acapulco (the local government) wrongly disposed of part of the property without the Estates' consent or authorization. Private parties had occupied part of the property since 1998 and such occupation was the result of an act of the local government.

Judicial Proceedings in Mexico

On 9 March 1989 the Estate initiated *amparo*[116] proceedings in Mexico for the unlawful disposition of a portion of the Estate's property by the municipal

[116] *The amparo is a constitutional resource in Mexico.*

government of Acapulco (the municipal government). This action was apparently prompted by ES's discovery of the fact that such land had been donated by the local government to the Union of Fruit Growers. This *amparo* was not admitted.

This *amparo* action was admitted on 10 December 1989, and the local government was ordered to revoke the donation and to return the property to the Estate.

Exercise

Based on the above-mentioned facts, determine the applicability of NAFTA's investment protection provisions to the case and review the procedural requirements that PS should take into account to submit the claim to the mechanism established in Chapter 11 of the NAFTA.

6. FURTHER READING

6.1 Books and Articles

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6.2 Internet Pages

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