

Challenging Corporate Investor Rule

How the World Bank's Investment Court, Free Trade Agreements, and Bilateral Investment Treaties have Unleashed a New Era of Corporate Power and What to Do About It

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The Institute for Policy Studies is an independent, multi-issue think tank that transforms ideas into action for peace, justice, and the environment. IPS was founded in Washington, DC in 1963.

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Summary

This report examines how global corporations have increased their power through rules and institutions designed to provide unprecedented and sweeping protections to private foreign investors. These increasingly controversial protections are promoted by the World Bank and other international financial institutions, codified by bilateral investment treaties and free trade agreements, and enforced through international arbitration tribunals. Civil society groups – including labor, environmental and human rights groups -- have been harshly critical of these rules, charging that they elevate the narrow interests of global corporations above social and environmental goals. They have been joined by an increasing number of legislators around the world, including in the United States, who have attacked these measures as fundamentally undemocratic. And now, new political leaders, particularly in South America, are beginning to explore ways of challenging these excessive investor protections and putting forth proposals for more just trade and investment regimes.

Key Findings

Investor Protections and Lawsuits Have Exploded Worldwide

- Number of bilateral investment treaties in 1989: 385¹
- Number of bilateral investment treaties in 2006: >2,500²
- Total number of investor-state lawsuits: unknown (some arbitration bodies keep cases secret)³
- Number of known investor-state lawsuits filed as of November 2006: 255⁴
- Proportion of these lawsuits that have been filed since 2002: >2/3⁵

Much of the World is Still Not Bound by U.S. Investor Protection Agreements

- Number of U.S. bilateral investment treaties: 40 (19 in the former soviet bloc, 9 in Latin America and the Caribbean, 7 in Africa, 3 in the Middle East, and 2 in Asia)
- Number of countries that have U.S. free trade agreements containing similar investor protections: 14⁶
- Number of U.S. investor protection agreements with China and Brazil, the two biggest recipients of foreign direct investment in the developing world: 0
- Number of U.S. investor protection agreements with the European Union and Japan, the top sources of foreign direct investment in the United States: 0

Economic Threats are Significant

- Largest known damage award ever paid in an investor-state case: \$877 million (by the Slovak Republic to the Czech bank CSOB)⁷
- Largest known pending damages claim: \$28.3 billion (by British-based Group Menatep against Russia over alleged expropriation of Russian oil giant Yukos. Menatep was a major shareholder in Yukos.)⁸

Governments Often Face Deep-Pocketed Legal Opponents

- Number of investor-state cases pending before the International Centre for the Settlement of Investment Disputes (ICSID), the most-used international arbitration body, as of the end of February 2007: 109
- Number of these cases in which the investor's revenues exceeded the GDP of the country they were suing: 7 (see *Table 1*)

- Number of these lopsided cases that were against Argentina: 4
- Most lopsided case: Shell Brands International and Shell Nicaragua (subsidiaries of Royal Dutch Shell) v. Nicaragua
- Ratio of Royal Dutch Shell 2005 earnings to Nicaragua's GDP: 62:1
- Percentage of pending and concluded ICSID cases filed by corporations that rank among the Global 500: 20%

Developing Countries Hit Hardest

- Percentage of concluded and pending ICSID cases filed against "middle-income developing countries": 74%⁹
- Percentage of concluded and pending cases filed against "low-income developing countries": 19%
- Percentage of cases filed against G-8 countries: 1.4% (all filed against the US)
- Proportion of pending ICSID cases that are against Argentina: 1/3 (32 of 109)

Investor-State Claims are often Disputes over Natural Resources and Public Services

- Number of ICSID claims over water disputes: 7
- Percentage of cases involving the services sector (water, electricity, telecommunications, and waste management): 42%
- Percentage of cases related to oil, gas and mining: 29%

Investors' Odds of Winning are High

- Percentage of ICSID rulings in favor of the investor: 36%
- Percentage settled out of court with compensation for the investor: 34%

Domestic Courts Fight Back

- Number of domestic court cases challenging the awards of investor-state lawsuits between June 2005 and November 2006: 5¹⁰
- Number of successful challenges: 0¹¹

A Secret Court?

- Number of investor-state cases that have permitted public attendance at the hearings: 2¹²
- Number of investor-state cases that have permitted third parties to file amicus curiae briefs: 4¹³



I. Introduction

When Bolivian President Evo Morales took office in January 2006, international gas companies made it clear they were considering suing his government if he followed through on campaign promises to increase the Bolivians' share of revenues from this natural resource.¹⁴ Previous Bolivian governments had signed a flurry of bilateral investment treaties that gave foreign investors the right to file such lawsuits through international tribunals. In April 2006, Morales said these types of rules made him feel like a "prisoner" in the Presidential palace.¹⁵

His predicament was a common one for political leaders around the world who are caught in an inter-locking web of rules and institutions committed to promoting and protecting foreign investment – with little regard for the costs to democracy, the environment, and the public welfare. In the Bolivian gas case, the Morales government dismissed the threats and managed to renegotiate contracts with all of the foreign investors, substantially increasing the government's revenues.¹⁶

Other leaders have not been so fortunate. In nearby Argentina and Ecuador, for example, governments are facing potentially crippling investor lawsuits. Argentina has been hit by more than 30 investor claims, many of them in retaliation for actions taken in 2002 to alleviate the pain of the country's financial meltdown on average citizens. The government has lost four cases in the past two years. Most recently, it lost a case brought by the German electronics giant Siemens, and was ordered to pay \$217 million in February 2007.¹⁷

Both governments are attempting to challenge the power of the International Centre for the Settlement of Investment Disputes, which is in charge of arbitrating the cases. Argentine Minister of Justice Horacio Rosatti said, "ICSID does not have authority over the economic measures taken by a country during a crisis."¹⁸ Newly elected Ecuador-

ian President Rafael Correa has vowed to fight a \$1 billion lawsuit filed by Occidental Petroleum, saying that "Ecuador has not accepted and will not accept arbitration in ICSID or any other body. The Occidental case has been resolved and national sovereignty has prevailed."¹⁹

Rich country governments have not been immune to investor lawsuits. The United States and Canada have both faced a number of expensive suits filed under the investment chapter of the North American Free Trade Agreement. Canada even repealed an environmental health regulation in the face of one threatened lawsuit by a U.S. corporation. The U.S. government is currently facing a suit by a Canadian company over regulations to reduce the environmental damage of a gold mining project. However, foreign investors have used their sweeping new powers most often against the governments of poorer nations. And the countries of the former Soviet bloc and Latin America that have most rapidly privatized state enterprises and opened their doors to foreign investment have been hardest hit.

The disturbing implications of the new global investment regime, detailed in this report, have not gone unnoticed. The U.S. government's demand to include sweeping investor protections in the Free Trade Area of the Americas was one factor in the collapse of those negotiations, after 11 years of talks involving 34 countries. Similar proposals to incorporate such rules in the OECD through the Multilateral Investment Agreement were aborted in the late 1990s, while developing country governments nixed plans to hold investment discussions through the World Trade Organization in 2003.²⁰

At a time of growing backlash to the excessive power of corporate investors, it is important to take stock of the record thus far and to consider strategies towards developing a new global framework that allows democratic governments to play responsible roles in ensuring that foreign investment supports social welfare and environmental goals.

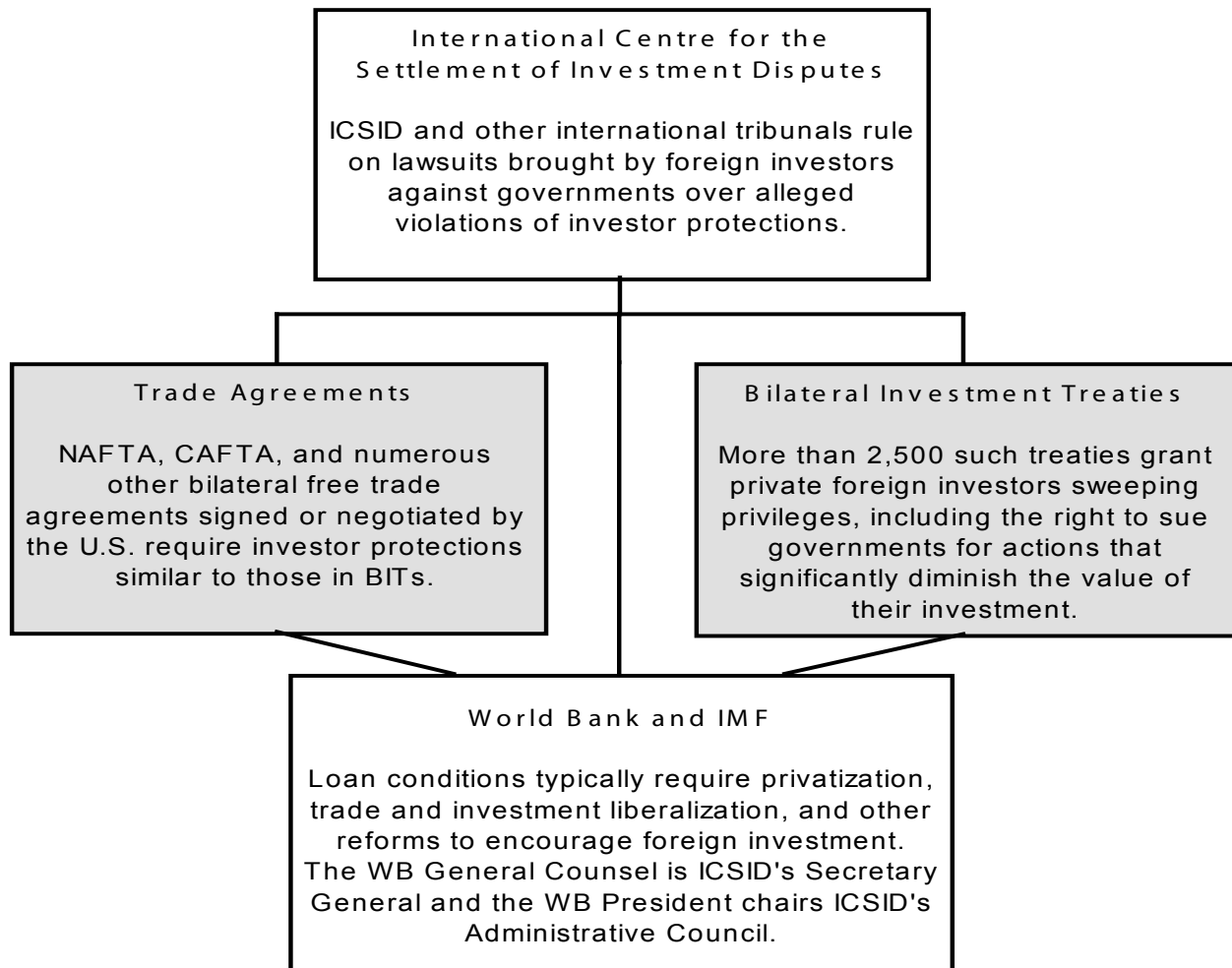
II. The Infrastructure of Excessive Investor Powers

Global corporations have lobbied successfully to build a worldwide infrastructure to protect their interests. The World Bank, International Monetary Fund and other international financial institutions have broken down barriers to international corporate activities in most countries on the planet by imposing policy conditions on their lending. These reforms have typically included privatization of state-owned enterprises and services, trade and investment liberalization, and other reforms aimed at creating “investment friendly” environments. Through an explosion of multilateral and bilateral trade and investment agreements, global firms have acquired new protections against government acts that might reduce their profits. And to enforce these new privileges, they can turn to an arbitration body connected to the World Bank, the International Centre for the Settlement of Investment Disputes, and other similar international tribunals.

International Centre for the Settlement of Investment Disputes (ICSID)

ICSID is a practically unknown part of the World Bank Group. Yet decisions made by ICSID tribunals are changing the course of global economic relations. ICSID is an investor dispute mechanism that provides multinational corporations with powers to sue governments when they impose domestic laws or regulations that have a significantly detrimental effect on corporate profit-making. The World Bank organized the international body in 1966.²¹ Historically, capital-exporting countries have used a variety of “carrots and sticks” to protect the economic interests of their major corporations abroad. The breakdown of diplomatic channels often meant these disputes were resolved through force, or “gunboat diplomacy.” The United States has a long history of sending its military to foreign shores where U.S. investments are threatened.

The World Bank argued that such an institutional mechanism would “promote increased flows of international investment.”²² Multinational corporations investing in foreign countries argued that such a mechanism was needed



Argentina has been hit by more than 30 investor claims, many of them in retaliation for actions taken to alleviate the pain of the country's financial meltdown on average citizens.

because the domestic court systems in the host states did not provide adequate protection.²³ In international law, foreign investors had no standing and no direct cause of action against a government when they felt their investments were adversely affected. ICSID fulfilled the corporations' wishes by giving them the same standing in international law as states.²⁴

Although ICSID was founded in 1966, it was almost dormant for the first 30 years of its existence. A half decade went by before ICSID saw its first case when the Holiday Inns Corporation sought arbitration over a dispute with the Moroccan government.²⁵ For the next quarter century there was still just a trickle of cases. Today there are more than 100 cases pending, with total investor claims against governments estimated at more than \$30 billion.²⁶ Two-thirds of all known investor-state lawsuits have been filed since 2002.²⁷ And almost a third of those pending at the end of February 2007 (32 out of 109) were filed against one country – Argentina.

Bilateral Investment Treaties and Free Trade Agreements

The metamorphosis that brought ICSID to life was the explosion of bilateral investment treaties (BITs). There are now more than 2,500 BITs, with approximately 1,500 signed in the past 12 years.²⁸ Pakistan's Attorney General, Makhdoom Ali Khan, explained that such treaties have been treated simply as photo-opportunities, "when someone is coming over for a visit and an 'unimportant' document has to be signed." As reported by Investment Treaty News, Khan recently told a crowd of investment experts that "These are signed without any knowledge of their implications. And when you are hit by the first investor-state arbitration you realize what these words mean."²⁹

The U.S. government has also demanded that similar investor protections be included in a rash of multilateral and bilateral trade agreements, such as the North American Free Trade Agreement (NAFTA) and the Central America Free Trade Agreement (CAFTA).

These investment and free trade treaties grant broad new rights to multinational corporations. The content of the investment treaties usually include provisions granting "adequate compensation" if an investment is directly or indirectly "expropriated," prohibitions against enacting currency controls, guarantees to provide "full protection and security" and "fair and equitable treatment" to an investment, and, most importantly, access to direct remedies in international tribunals such as ICSID to address claims of violations of any of these rights (see Box 1 for more details). Although ICSID is the most commonly used dispute resolution mechanism, there are other international tribunals and rules used to resolve these claims such as UNCITRAL (United Nations Commission on International Trade Law) and the ICC (International Chamber of Commerce).

ICSID, and the investment and free trade treaties that give it life, provide grandiose new powers to multinational corporations and essentially privatize certain aspects of our international legal system. In past centuries, international conflicts were resolved through state-to-state mechanisms. Today, as University of Minnesota professor and former arbitration lawyer Susan Franck puts it, multinational corporations can act like "private attorney generals" and sue sovereign states directly for monetary compensation.³¹ Corporate power has become elevated to the height of sovereign state power.

"These [treaties] are signed without any knowledge of their implications. And when you are hit by the first investor-state arbitration you realize what these words mean."

*- Makhdoom Ali Khan,
Pakistan's Attorney General*

Box 1

Most Controversial Elements of Investor Protection Agreements

With only small variations, the following rules are typically found in bilateral investment treaties and in all trade agreements signed by the United States since 1993, with the exception of the 2004 U.S.-Australia Free Trade Agreement. The Australian government refused to accept investor-state dispute resolution.

1. Investor-State Dispute Resolution

Private foreign investors can bypass domestic courts to sue governments directly in international tribunals.

2. Restrictions on "Indirect" Expropriation

Whereas expropriation in the past applied to physical takings of property, current rules also protect investors from "indirect" expropriation, interpreted to mean regulations and other government actions that significantly reduce the value of a foreign investment. Hence, corporations can sue over environmental, health, and other public interest laws developed through a democratic process. While the tribunals cannot force a government to repeal such laws, the threat of massive damages awards can put a "chilling effect" on responsible policy-making.

3. Vague "Fair and Equitable Treatment" Standards

These terms have no definable meaning and are inherently subjective, allowing arbitrators to apply their own interpretations to government actions in countries with diverse histories, cultures and values systems.

4. National Treatment and Most Favored Nation Treatment

Governments must treat foreign investors and their investments at least as favorably as domestic investors and those from any third country. While this is touted as a basic principle of fairness, it strips the power of governments to pursue national development strategies used in the past by nearly every successful economy. Moreover, a regulatory action that applies to all corporations but has a disproportionate impact on a foreign investor could be targeted as a national treatment violation.

5. Ban on Capital Controls

Governments are banned from applying restrictions on the flows of capital, even though such controls helped some countries escape the worst of the global financial crisis of the late-1990s.³⁰ Even the IMF has stopped demanding that governments lift controls on capital flows.

6. Limits on Performance Requirements

Governments must surrender the authority to require that foreign investors use a certain percentage of local inputs in production, transfer technology, and other conditions used in the past as responsible economic development tools.

It is important to place this all in historical perspective. During the 1960s and 1970s, many developing countries pursued "import substitution industrialization" by giving protections to domestic industry. Foreign investors were subjected to a variety of domestic government regulations such as tariff protection, domestic content requirements, capital controls or controls on repatriation and other rules to help ensure that the investment provided some benefits to the host country.³² However, investors became increasingly resistant to such constraints on their behavior and began devising new strategies to protect their profits. Today many of these same domestic regulations could provide cause for multi-million dollar investor lawsuits. The development of BITs and free trade treaties, and the hundreds of ICSID cases that they have spawned, are part of a new era of growing international corporate power where investment flows have become increasingly directed towards satisfying international shareholders and global production demands.

Longstanding principles of international relations have fallen by the wayside. In Latin America, for example, the history of foreign interference gave rise to the Calvo Doctrine, which gave domestic courts final jurisdiction in disputes with foreign investors. This prevented rich country investors from undermining the sovereignty of weaker countries by seeking international arbitration or legal remedies in their home country. During much of the twentieth century various formulations of the Calvo Doctrine found its way into many constitutions, treaties, statutes, and contracts around the world.³³

The founding of ICSID was an initial step in overturning the long history of the Calvo Doctrine. The ICSID Convention does not require investors to exhaust domestic remedies before filing an ICSID claim, nor is there any role for domestic court review of the compensation award or at any prior point in the process.³⁴ ICSID provides multinational

Today, as University of Minnesota professor and former arbitration lawyer Susan Franck puts it, multinational corporations can act like “private attorney generals” and sue sovereign states directly for monetary compensation.

corporations (investors) with a new international body to help protect their profitability on foreign shores. It is an institutionalized and internationally sanctioned mechanism to place the same pressures on governments that were previously achieved through diplomacy, gunboat and otherwise.

World Bank and ICSID

ICSID is not an independent organization. It is part of the World Bank Group, from which it receives financial support. The president of the World Bank, currently former U.S. Defense Department official Paul Wolfowitz, chairs the Administrative Council of ICSID and the Bank’s Legal Vice-President is ICSID’s Secretary General.³⁵ The chair of the Administrative Council has a variety of powers and duties at ICSID. He designates up to ten people each to the panels of conciliators and arbitrators. When the parties in a dispute fail to agree, or for any other reason fail to appoint conciliators or arbitrators to a tribunal, the chair of the Administrative Council has the authority to intervene and make the selection himself.³⁶ World Bank presidents have often participated in such selection processes, including in the notorious Bechtel v. Bolivia case. The chair of

Global 500 Corporations Take on the Little Guys

In defending against investor-state cases, national governments often must compete against deep-pocketed corporations with high-powered legal teams and strong political ties. Corporations that rank in the top 500 globally make up more than 20 percent of all ICSID claims. In seven pending ICSID cases, the claimant’s corporate revenues exceed the GDP of the defending country. (For a list of all Global 500 corporations that have filed such cases, see Appendix.)

Claimant	Parent Corporation	2005 revenues (\$000)	Defending Country	2005 GDP (\$000)
Shell Brands International AG and Shell Nicaragua S.A.	Royal Dutch Shell	306,731,000	Nicaragua	4,911,046
Togo Electricite	Suez	52,742,900	Togo	2,202,788
Chevron Block Twelve & Chevron Blocks Thirteen and Fourteen	Chevron	189,481,000	Bangladesh	59,957,930
BP America Production Company and others	BP	267,600,000	Argentina	183,309,400
Mobil Exploration and Development Inc. Suc. Argentina and Mobil Argentina S.A.	Exxon Mobil	339,938,000	Argentina	183,309,400
DaimlerChrysler Services AG	DaimlerChrysler	186,106,000	Argentina	183,309,400
Pan American Energy LLC and BP Argentina Exploration Company	BP	267,600,000	Argentina	183,309,400

Sources: Corporate revenues, Fortune, July 31, 2006; GDP, World Bank WDI Online

the Administrative Council may also appoint members to ad hoc committees (such as ones that consider annulment) and considers proposals to disqualify a conciliator or arbitrator.³⁷

Many civil society groups argue that this relationship with the World Bank is completely inappropriate for an arbitration tribunal that, in order to have any credibility, should need to maintain itself as a neutral, impartial and objective dispute resolution mechanism.

Basic assumptions of the World Bank underlie the founding of ICSID. The key assumption is that promoting increased flows of international investment will contribute to “development” and the Bank’s stated poverty reduction goals. Therefore, the reasoning goes, promoting “development” requires setting an attractive investment climate, i.e. one that provides for the security and protection of the private investor. Investor rights are not balanced with investor responsibilities. A more balanced approach would assess investor performance by reviewing compliance with basic environmental, health and safety regulations essential to safeguarding rights of local communities and workers. A more balanced approach could also promote policies encouraging investor responsibilities to local communities or the local economy. Examples of these type of policies include local content regulations, controls on repatriation of profits, local employment or local investment requirements, responsibilities to pay local taxes, or price controls on basic services. Unfortunately, such requirements are viewed as impeding the creation of a “conducive investment climate” and can be considered a breach of bilateral investment treaties and a cause for arbitration claims.

The conflicts of interest inherent in the World Bank’s role within ICSID are mammoth. For example, the World Bank takes positions and influences the development of bilateral investment treaties among their client governments.

The conflicts of interest inherent in the World Bank’s role within ICSID are mammoth. For example, the World Bank takes positions and influences the development of bilateral investment treaties among their client governments. For example, during the 2006 negotiations for a BIT between the United States and Pakistan, World Bank and Asian Development Bank officials reportedly put pressure on Pakistan to adopt the dispute resolution mechanism preferred by the United States, that is the ICSID mechanism, rather than UNCITRAL.³⁸ The most important operational conflicts of interest between the World Bank Group and ICSID fall into five main categories.

1. Investors that bring claims to ICSID may also be clients of the World Bank. The investor may have received a loan from the World Bank’s private sector window, called the International Finance Corporation (IFC). In fact, the IFC has played a key role in promoting the use of the ICSID mechanism through its loan agreements.
2. The government respondents to the claim are also likely to be clients, often severely indebted clients, of the World Bank, placing them in a position beholden to the World Bank and subject to a wide range of lending conditions.
3. The World Bank quite regularly plays a role in designing institutional, legal and regulatory reforms that facilitate the privatization process. The Bank may be directly or indirectly involved with the host country government in the development of concession contracts with foreign investors that carry out the privatization process. Some of these concession contracts will later become the topic of investment disputes.
4. The World Bank’s IFC may also be a shareholder in companies that bring ICSID claims.
5. The investor may also have purchased guarantees from the World Bank’s Multilateral Investment Guarantee Agency (MIGA). MIGA provides political risk insurance for investors. The guarantees aim to protect investors from currency transfer risk, expropriation, breach of contract and other issues.

Given these fundamental conflicts-of-interest imbedded in the structure and operation of ICSID, it should not be considered an independent, neutral or impartial body for the resolution of international investment disputes.

Investor-State Disputes as Blackmail

Powerful corporations often enlist the support of home country officials as well as international financial institutions to pressure governments to resolve their investor-state suits. Examples:

- The Bush administration broke off free trade negotiations with Ecuador after U.S.-based Occidental Petroleum filed an ICSID claim related to the Ecuadorian government’s cancellation of a contract.³⁹
- The IMF advised Ecuador in September 2006 to increase its accumulation of reserves to prepare for a possible ruling against the country in the \$1 billion ICSID claim by Occidental Petroleum.⁴⁰
- World Bank and IMF debt relief to The Gambia was delayed for several years pending the outcome of an ICSID claim filed by the Swiss company Alimenta. The Gambian government had seized property belonging to the global groundnut trader on allegations of money laundering.⁴¹
- The U.S. Ambassador to Mexico allegedly made threats to Mexico’s Commerce Secretary and a Mexican state governor that he would put Mexico on a blacklist to slow investments to that country if it did not reverse actions that had prompted U.S.-based Metalclad to file a NAFTA investor lawsuit against the country (for more on Metalclad v. Mexico, see Section III).⁴²

The United States and other rich nations have often used trade, aid and debt as levers to exert power over less powerful countries. The current regime of excessive investor protections gives them one more means of influence.

Once corporations have filed investor-state suits, they can use them for leverage over host country governments. The Suez company Aguas Argentinas used its \$1.7 billion ICSID suit to pressure the Argentine government for concessions in the renegotiation of a contract to run the Buenos Aires water system. This probably delayed the government’s termination of the contract by several years.⁴³ The Suez concession contract in Cordoba, Argentina has a similar history (see interview with activists involved in that case in Box 2).



Box 2
Who Controls the World Bank?

Major decisions at the World Bank are made by the 24 executive directors. The five largest shareholding countries appoint their Executive Directors. These are the United States, Japan, Germany, France and UK. Other countries are grouped together, usually in regional groupings, and elect one country to represent them. Voting power of the executive directors is determined by the capital subscription of the countries they represent with the larger shareholders having the greatest percentage of the votes. The five largest shareholding countries have the following percentage of the vote:

United States.....	16.41%
Japan.....	7.87%
Germany.....	4.49%
France.....	4.31%
United Kingdom.....	4.31%

Investor-State Arbitration: Privatization of Public International Law?

Corporations have often preferred arbitration over the public judicial system for resolving disputes for a number of reasons. Sometimes it is quicker and cheaper, with less red-tape and bureaucracy. It is also a system of dispute resolution that is primarily controlled by the disputing parties themselves. In the public judicial system model, a judge must follow applicable law and the binding decisions of appellate courts, whereas with arbitration the disputing parties themselves have much more control over the resolution process.⁴⁴ There is no accountability to the public, no consistency or coherence in decision-making and no appeals process. Because the arbitration model has removed itself from many of the checks and balances of a public judicial system model, many have argued that it is a form of privatization of the judicial system. As stated by scholar Susan D. Franck, it “places the enforcement of public international law rights in the hands of private individuals and corporations.”⁴⁵

Three reasons why the arbitration model is inappropriate for resolving investor-state disputes:

1. **These are not private commercial disputes, rather they involve broad public welfare issues.** The majority of investor-state claims today involve companies that provide basic public services such as electricity or water, or companies that extract, process and transport vital natural resources such as oil, gas and mining operations.⁴⁶ The business of these companies is vitally related to public welfare, the environ-

ment, and national security. It is no longer appropriate for such cases to be resolved in a quasi-privatized commercial arbitration dispute system. Most of these cases would be more appropriately decided in public judicial system models because they are cases that involve the balancing of private and public welfare issues and often engage important topics of public policy such as regulation to protect the environment and public health, taxpayer, fiscal and budgetary issues, and access to basic public services.

2. The arbitration model lacks public accountability, transparency and citizen participation. The system of commercial arbitration is not an appropriate mechanism to resolve investor-state disputes because this system was not designed to provide public accountability, transparency, or citizen participation. In fact, the system was designed to intentionally shield the hearings from the public eye. As explained by law

professor Edward Brunet, “The desire for secrecy can be a prime determinant in selecting arbitration. Often one or more party to an arbitration agreement has an interest in avoiding a public trial with unwanted adverse publicity.”⁴⁷ As noted in Section V on Transparency and Participation, there are very few cases where citizen’s groups have been allowed to submit an amicus brief or even attend a hearing, much less gain access to court documents or provide testimony to the proceedings.

3. There is no separation between the role of judge and lawyer. In the public judicial system model, no practicing lawyer is permitted to be a member of the judiciary as well. However, in the arbitration system there is little distinction between the two roles. Lawyers or arbitrators also serve the role of judges when they serve on arbitration panels or tribunals. This creates both the perception of conflict of interest

Box 3

Suez v. Argentina: A Civil Society Perspective

Interview with Gustavo Spedele and Luis Bazan of the Comision Popular por la Recuperacion del Agua, Cordoba, Argentina

Water privatizations have collapsed across Argentina and most of the companies have fled. However, one of the last strongholds of the French multinational, Suez, is in Cordoba, Argentina. In Cordoba the state legislature recently approved a revised privatization contract after the company demanded the deal in exchange for dropping an ICSID case.

How do big multinationals like Suez use the threat of an ICSID case to pressure governments to do their bidding?

ICSID is used like a “boogie man” by governments to justify their acceptance of ruinous deals for taxpayers and the state. In Cordoba the only argument used by vice-governor Shiaretti (advised by Roberto Chama, a consultant for the Inter-American Development Bank) to defend the passage of the deal with SUEZ-ROGGIO was that, “when the new law is approved the ICSID case will be withdrawn; this was the agreement because the Cordoba people cannot continue with this sword of Damocles over our heads.” In summary, the deal had to be signed because otherwise the ICSID lawsuit would have to be paid.

Using the case of Aguas Cordobesas as an example, explain exactly what benefits Suez demanded and what they won when the state legislature approved the new contract. Suez promised to terminate the ICSID case after the new contract was approved. Did this happen?

Suez demanded a pardon for all of the debts it owed to the province including back taxes it owed, fines for contractual non-compliance, and investments. They denied they had an obligation to make investments to improve the service. Rather the state and taxpayers had to assume responsibility for the financing through a fund that is managed by SUEZ-ROGGIO. They demanded that consumer water rates be increased over 500% or the government would compensate the company for losses through direct or indirect subsidies. They wanted the government to pay their creditors including \$40 million owed to the European Investment Bank that was not used for investment in services but rather for financial negotiations. There was also a clause that stated that, until the contract ended in 27 years, the government guaranteed the rate of earnings of the company, and under any contingency that altered this rate the company would be compensated.

and/or an actual conflict of interest. Lawyers or arbitrators should not serve as advocates one day and as judges on another. As judges they create decisions that aid their clients or clients in a future potential situation. Thus in the arbitration system it is well understood that parties to arbitrations choose their arbitrators because of their known leanings.⁴⁸ The concept of a neutral, objective judiciary does not exist in such a system.

The system of commercial arbitration was not designed to provide public accountability, transparency, or citizen participation, and intentionally shields hearings from the public eye.

The legislature approved most of these conditions in the new contract including the pardon of the debts, massive consumer rate increases especially after 2008 and the installation of new water meters, annual subsidies for SUEZ-ROGGIO of about 25 million Argentine pesos, and a reduction in the powers of the regulatory agency, to name a few of the measures. While the current ICSID case has been suspended, this is not as relevant as the fact that the new contract requires that the government, until the contract expires in 2027, approve within 90 days all rate revisions claimed by the company. If rate revisions are not approved in 90 days this implies the immediate termination of the contract due to breach by the state and permits SUEZ-ROGGIO to file new claims with ICSID. In addition to this, the contract establishes the possibility that, while the current ICSID claim in the name of Aguas Cordobesas is discontinued, individual shareholders among the consortium that previously made up Aguas Cordobesas could continue with the ICSID claim.

Describe the police repression that the people in Cordoba suffered when they protested the deal being made in the legislature. Why was the police repression so harsh?

The repression launched December 29, 2006, minutes after the approval by the legislature of the new contract, was the only response the government found to face the growing popular mobilization challenging the massive and perpetual water rate hikes proposed by SUEZ-ROGGIO. The popular outcry produced a profound crisis of government that caused the fall of the minister of public works, the state controller, and the head of ERSEP (the public services regulatory agency). The media and political analysts attributed the repression to the fact that this was the last opportunity before the 2007 elections that the government had to fulfill its promises to the corporations. Therefore, they passed the contract package and paid the price by using the police to repress the popular mobilization. This meant more than 50 people were wounded, either beaten or hit by rubber bullets and 10 were jailed. The order to attack a peaceful demonstration was given by the vice-governor Schiaretti. The repression was also an attempt to quell our enthusiasm for organizing a popular consultation on water privatization and to discourage our process of building a broad multisector coalition in defense of water and life.

What will this new contract deal with Roggio/Suez mean for the people of Cordoba? How will it affect access to clean and affordable water?

A basic principle of water, sanitation and public health is the requirement of universal access for all, including access to sufficient quantity and quality of water without cut-offs and stoppages. With the passage of this contract the basic principle of universal access to water for all will be in constant risk until 2027 for the people of Cordoba, Argentina. SUEZ-ROGGIO will be left able to impose their will and their main objective will be the maximizing of profits.

III. Ten Egregious Investor-State Cases

This section highlights ten of the most controversial investor-state cases. They were not selected based on financial impact alone. As noted in the “key findings,” the largest known damage award ever paid in an investor-state case was the Slovak Republic’s \$877 million to the Czech bank CSOB. That case related to the government’s failure to cover losses associated with non-performing loans after the private CSOB took over a government-owned bank.⁴⁹ The biggest damages claim so far is in the pending case brought by the British-based Group Menatep, which is demanding \$28.3 billion from the Russian government to compensate for stock losses associated with the government’s takeover of the Yukos oil company.⁵⁰

While not the largest in dollar terms, the ten highlighted cases effectively illustrate how corporations and wealthy private investors have used investor-state disputes to:

- attack environmental and other public interest regulations;
- punish governments for acting according to the will of their people; and
- guarantee profits despite shoddy performance.

These examples, which include both pending and concluded suits, also illustrate how such cases have an impact on countries large and small, and in many parts of the world.

Cases Related to Environmental Regulations:

Note: All three of these cases have been filed under the investment protections of the North American Free Trade Agreement (NAFTA), which was promoted as a vehicle for strengthening environmental protections in Mexico, the United States, and Canada.

1. V.G. Gallo v. Canada Government Faces \$355 million Suit After Blocking Unpopular Garbage Project

American investor Vito G. Gallo filed notice in 2006 that he intends to sue Canada over an environmental regulation which blocked a project to create a garbage mega-dump out of an abandoned open-pit iron mine. Gallo, whose company owns the mine, is using NAFTA rules to demand \$355.1 million in damages for an action he charges was “tantamount to expropriation.”⁵¹

The plan was to transport garbage 370 miles (600 kilometers) from the city of Toronto to the former Adams Mine

Timiskaming Chief Carol

McBride said the Toronto

government would become “toxic criminals” if they shipped urban garbage to native lands.

in northern Ontario. First proposed in 1989, the project faced fierce opposition, culminating in the largest act of civil disobedience in Ontario history. Environmentalists charged that the technology to be used to contain the waste in the former mine was untested, and there would be a high risk of groundwater contamination.⁵² The mine is located on traditional territory of the Timiskaming First Nation, a member of the Algonquin indigenous tribe. Timiskaming Chief Carol McBride said the Toronto government would become “toxic criminals” if they shipped urban garbage to native lands.⁵³ Farmers in communities downstream from the mine were also concerned about potential dangers for their crops and livestock.

A conservative provincial government ignored these concerns and gave the project the green light in the late-1990s. However, a diverse citizens’ alliance managed to stall progress through a series of protests, including a railroad blockade that involved hundreds of people and lasted nearly a week.⁵⁴ Peter Di Gangi, Director of the Algonquin Nation Secretariat, said that while there has been friction between the Algonquins and others in the area over land rights, there was virtual unanimity in opposition to the mega-dump. “The farmers and the environmentalists and others from the local area were right there with us on this one, and in fact, we made it clear that if the government didn’t take action, things would just escalate, through more civil disobedience or through the courts.”

After provincial power shifted to the Liberal Party in 2003, the government passed a regulation that killed the plan. The Ontario government offered compensation to investors, but it was not enough for Gallo. Charlie Angus, who fought the project as a community activist and now represents the area as a member of the Canadian Parliament, is outraged that “a numbered company, registered in Ontario, can appeal to the unaccountable NAFTA process for compensation over a municipal project that was rejected by Provincial authorities.” Angus is particularly angry that Gallo could use his status as a U.S. citizen to file the NAFTA suit, even though the company that owns the mine is based in Canada.

This is only the latest of several NAFTA lawsuits targeting Canada’s environmental and public health standards. In 1996, U.S.-based Ethyl Corp. threatened to file the first NAFTA investor-state lawsuit over a Canadian ban on trade in the fuel additive MMT. The Canadian Parliament had adopted the ban because MMT was a suspected neurotoxin and also damages car exhaust systems. Ethyl, the sole producer of MMT, demanded more than \$250 million in compensation, charging that Canada had violated NAFTA protections against discrimination, performance requirements, and expropriation.⁵⁵

The Canadian government responded by repealing the ban, paying the company \$13 million for costs and lost profits while the ban was in place, and issuing an official apology.⁵⁶ According to the Canadian Centre for Policy Alternatives, while MMT was eventually phased out by gas companies under pressure from automakers, Canada’s repeal of the ban caused Canadians to be exposed to MMT-laced gasoline for six additional years.⁵⁷

2. Glamis Gold Ltd. v. United States Targeting Sacred Native Lands for Profit

Canadian gold mining company Glamis Gold filed a suit against the U.S. government in 2003, demanding at least \$50 million in compensation for regulations enacted to protect the environment and indigenous communities from the impacts of open-pit mining.⁵

Glamis filed the lawsuit under the North American Free Trade Agreement over an action to block an extremely controversial mining project in Southern California. Among the many opponents are members of the Quechan Indian Nation, a 3,000-member tribe whose sacred ancestral lands

The Quechan Nation has had to rely primarily on the Bush Administration to defend its interests – despite their opposing positions on the mining project and the fact that under U.S. law, the tribe is a sovereign nation.



Railroad blockade to stop mega-dump. Photo courtesy of the Algonquin Nation Secretariat.

would be severely affected. According to a submission filed on behalf of the Quechan, “the mine would be so damaging to the historic resources that the Tribal members’ ability to practice their sacred traditions as a living part of their community life and development would be lost.”⁵⁹

Environmental groups have also been extremely critical, charging that the company’s proposed “Imperial Mine” would destroy a largely pristine area adjacent to a designated desert wilderness area and require massive amounts of water from the desert groundwater aquifer.⁶⁰ In March 2006, the Sierra Club brought together members of the Quechan people with Mayan Indians who are fighting attempts by Glamis to mine indigenous lands in Guatemala.

When the Bush Administration gave the green light to the project in 2001 (reversing the federal government’s previous opposition but not approving the mine), the State of California took action to limit its negative impacts. The new regulations require that craters created by all new open-pit metallic mining operations be backfilled and that the landscape in the area be re-contoured once mining operations have been completed. Glamis claims that compliance would be so costly that the regulations have essentially destroyed the value of its investments. The company charges that these actions are a violation of NAFTA’s prohibition on expropriation and “fair and equitable” treatment protections.⁶¹

The Glamis case, which is ongoing, reveals how indigenous rights can be threatened by international investor protections. Since the federal government is the official respondent in such suits, the Quechan Nation, while submitting its own amicus briefs, has had to rely primarily on the Bush Administration to defend its interests – despite their opposing positions on the mining project and the fact that under U.S. law, the tribe is a sovereign nation.

3. Metalclad v. Mexico **Court Ruled Environmental Laws are “Expropriation”**

In 1993, U.S.-based Metalclad Corporation purchased a Mexican company that operated a notorious waste site in the central Mexican state of San Luis Potosí. After many years of problems associated with the site, including contamination of a nearby reservoir, local authorities had closed and sealed the existing waste dump. Metalclad officials presented themselves as heroes who would use cutting-edge technology in operating an improved and expanded site, making it a great success story of the North American Free Trade Agreement.

In the book *Confronting Globalization: Economic Integration and Popular Resistance in Mexico*, Fernando Bejarano González provides a detailed account of Metalclad’s efforts to push through the controversial project in the face of strong opposition from local and state authorities, environmental and social organizations, and local residents.⁶²

According to Bejarano, who worked for Greenpeace-Mexico at the time, state environmental officials had warned Metalclad from the beginning not to invest in the site, because studies had shown that it was not geo-hydrologically sound for waste management. Moreover, an environmental audit had shown that the risk of explosion was extremely high because of shoddy containment of the existing 20,000 plus tons of toxic waste on the site.⁶³ The company ignored these warnings, however, and announced plans to receive 30,000 tons of toxic waste annually over 25 years.⁶⁴

In response, several municipal administrations sent letters to state and federal authorities, expressing their opposition to reopening the dump. Local residents protested a public “grand opening” of the site, while Greenpeace and other national and local environmental and social organizations formed an alliance to demand that the site be cleaned up and then remain closed.

While the Mexican federal government supported the project, Metalclad never received a municipal construction permit. After years of wrangling, the state issued a decree in 1997 declaring the area a natural reserve for the preservation of endangered cacti, effectively blocking the project.⁶⁵

Metalclad retaliated by filing a lawsuit under NAFTA, demanding \$130 million in compensation for damages and lost future earnings. The company successfully argued before an ICSID tribunal that Mexico had violated NAFTA protections of fair treatment and against “expropriation.” Mexico then appealed to the British Columbia Supreme Court in Canada (where the NAFTA tribunal had deliberated). That court threw out some of the tribunal’s findings, but agreed that the creation of the protected natural area

was “tantamount to expropriation” and awarded the company about \$15.5 million.⁶⁶

According to Bejarano, “the case has grave repercussions for the future of democracy and municipal and state sovereignty, not only in Mexico, but in the United States, Canada, and all of Latin America.”

Cases Related to Natural Resource Control:

4. Piero Foresti, Laura De Carli and others v. South Africa **European Investors Target Black Empowerment Measure**

While the international divestment movement played a key role in ending Apartheid, some foreign investors are attacking a South African government effort to redress historical racial injustices. In January 2007, a group of European investors filed an ICSID lawsuit over a law designed to promote greater participation of blacks in the South African mining sector.

The target of the suit is the 2004 Mineral and Petroleum Resources Development Act (MPRDA), which requires all mining companies to achieve criteria in keeping with the country’s “Black Economic Empowerment” agenda. Specifically, black ownership in mining companies must be at least 26 percent by the year 2014 and blacks must make up 40 percent of management. The Act also sets additional non-quantitative goals, such as in skills training.⁶⁷

The MPRDA aims to improve racial equity in a sector that lags behind other South African industries. A study by an executive search group found that in 2005, 18 percent

The British Columbia Supreme Court in Canada agreed that the creation of the protected natural area was “tantamount to expropriation” and awarded the company about \$15.5 million.

of top managers in the mining industry were black, compared to 23 percent in the overall economy. In professional middle management, 27 percent were black in the mining sector, compared to 53 percent overall.⁶⁸ (Whites make up nine percent of the South African population.)

The investors are Italian nationals who own granite production companies in South Africa. Listed as “Piero Foresti, Laura De Carli and others” on the ICSID web site, they charge that the MPRDA violates protections against expropriation and discrimination in the Italy-South Africa bilateral investment treaty. According to Investment Treaty News, these investors have also charged violations of an agreement between South Africa and Belgium and Luxembourg through their Luxembourg-based holding company, Finstone.⁶⁹

This case has disturbing implications for other governments committed to expanding opportunities for historically disadvantaged peoples and promoting international human rights.

As Luke Eric Peterson points out in Investment Treaty News, “To date, investment arbitrations have scarcely wrestled with such thorny legal questions – and the relevant investment treaties offer no guidance as to whether human rights considerations ought to mitigate potential claims for breach of an investment treaty.”⁷⁰

5. Occidental Petroleum Corporation v. Ecuador Using ICSID Claims as Legalized Blackmail

On May 15, 2006, Ecuador’s Minister of Energy announced the cancellation of Occidental Petroleum Corporation’s operating contract in an area of the country where it was extracting more than 100,000 barrels of oil daily, approximately 7% of Occidental’s global oil production.⁷¹ Occidental immediately retaliated by filing a billion dollar ICSID claim.

Occidental Petroleum (Oxy) has been active in Ecuador for more than two decades, first providing contractual services to Petroecuador, the state-owned corporation, and then in 1999 becoming a direct contractor and undertaking its own drilling operation in an area called Block 15.⁷² Local and international environmental and indigenous organizations have accused the U.S.-based company of numerous human rights abuses and widespread environmental devastation in Ecuador (see Box 4 for details).

As in other parts of the Andean region, an indigenous renaissance has taken place in Ecuador during the last ten years that has included massive mobilizations which have brought down successive presidencies. A central demand has been to grant indigenous peoples control over their

“The relevant investment treaties offer no guidance as to whether human rights considerations ought to mitigate potential claims for breach of an investment treaty.”

*- Luke Eric Peterson in
Investment Treaty News*

land and natural resources and the benefits generated from them. Most specifically, this has translated into a demand that the Ecuadorian government end the exploitation of oil reserves, including the cancellation of the Occidental contract.⁷³

Oxy and the Ecuadorian government also have a long history of legal conflict. In 2004, Oxy was awarded \$75 million in a BIT case over the Ecuadorian government’s refusal to give the company Value-Added Tax refunds.⁷⁴ This outcome was criticized by numerous lawyers as having “strayed too far” in its national-treatment analysis.⁷⁵ “The potential breadth of the award is somewhat disconcerting” stated the American Journal of International Law.⁷⁶

Shortly after this controversial ruling, Petroecuador accused Oxy of improperly transferring a share of Ecuadorian production to a Canadian company. The Energy Minister investigated and concluded that the action was a breach of Occidental’s contract with Petroecuador, setting the legal stage for canceling the contract.⁷⁷ Meanwhile, civil society demands to cancel Oxy’s contract again reached a heightened pitch. This time, it appears, the government felt they had more to lose by holding on to the contract than by canceling it.

To support Occidental, the U.S. government suspended free trade negotiations with Ecuador.⁷⁸ The U.S. Trade Representative (USTR) demanded an immediate clarification as to whether Ecuador “intends to fully compensate the company as required under our Bilateral Investment Treaty.”⁷⁹ State Department official Charles Shapiro stated that legal



Photo courtesy of Patricio Realpe, from the archives of CONAIE.

Ecuador’s new President Rafael Correa stated that Ecuador was under no obligation to accept ICSID arbitration because the company’s illegal actions caused the contract termination... Correa warned that the people will be in the streets if the ICSID case moves forward.

recourse against the contract cancellation “certainly would be supported by the State Department.”⁸⁰

The IMF also entered the fray by suggesting that Ecuador should immediately begin to accumulate reserves to pay off a possible ruling against the country by the ICSID tribunal.⁸¹ Ecuador’s Attorney General Jose Borja responded by accusing the IMF of “hateful partiality in favor of interests that have seriously hurt” the country.⁸²

Ecuador’s new President Rafael Correa stated that Ecuador was under no obligation to accept ICSID arbitration because the company’s illegal actions caused the contract termination. He contends that under these circumstances the BIT would give Oxy access to Ecuadorian courts but not to international arbitration.⁸³ Correa warned that the people will be in the streets if the ICSID case moves forward. He also claims that the ICSID Executive Secretary has committed an irregularity by posting the registration of Oxy’s claim because the claim has not yet been accepted by the Ecuadorian government.⁸⁴

The outcome of this case will be an important barometer of the ability of the ICSID system to respond to a direct challenge to its legitimacy, and to investor-state lawsuits more generally.

**6. RSM Production v. Grenada
Litigious American Oil Tycoon Uses ICSID to Slam Tiny Grenada**

In 2005, U.S.-based RSM Production filed an ICSID suit demanding damages related to an oil exploration contract with the tiny Caribbean nation of Grenada (population 106,000). Jack Grynberg, President of RSM parent company Grynberg Petroleum, is known as a “professional plaintiff” who has made almost as much money through lawsuits as he has through energy contracts.⁸⁶

His most ambitious legal crusade was against 73 U.S. natural gas companies he accused of underreporting their production on federal lands. Although a U.S. District Court judge accused Grynberg of “odious tactics” when he dismissed the cases in 2006, Grynberg is planning an appeal.⁸⁷

On the international front, Grenada is only one of Grynberg’s many targets. In 2005 alone, Grynberg initiated a suit against Israel for refusing the company a license for offshore natural gas exploration and threatened an ICSID case against the Central African Republic over an oil deal. Despite the fact that the company had abandoned work in the African country in 2003, the ICSID threat pressured the government to grant a three-year contract extension.⁸⁸

The Grenada case is highly complex. In 1996, RSM obtained the country’s first ever concession for offshore oil exploration. According to the government, within 14 days of signing the contract, RSM invoked the force majeure clause, which relieves a party of its obligations in the case of an unexpected and disruptive event. In this instance, RSM claimed it could not do any work because of unresolved boundary disputes.⁸⁹

The government argues that RSM always knew about these issues and that the vast majority of the offshore area covered by the contract was nowhere near the disputed bound-

aries. Officials also complain that while they were attempting to resolve maritime boundaries with Trinidad & Tobago and Venezuela, Grynberg undercut their efforts by starting litigation against both countries.⁹⁰

The Grenadian government finally terminated the contract in 2004, after eight years had gone by without RSM beginning the work. In retaliation, RSM filed an ICSID complaint for undisclosed damages. Then in 2006, Grynberg turned up the heat by filing a case in a U.S. court charging Grenada's Energy Minister with attempted bribery. Ten years after obtaining the contract, Grynberg argued that the real reason work had never been done was because of obstruction and harassment by the Minister after the oilman refused to pay him off. Grynberg demanded \$500 million in the bribery case – more than Grenada's total 2006 GDP of \$408 million.⁹¹

In January 2007, Grynberg abruptly offered to drop the bribery suit and the ICSID claim and apologize to the Energy Minister, if the Grenada government agreed to let RSM sell a controlling interest in the contract to a “potential partner.”⁹² As of this publication, the matter remained unresolved.

Cases Related to Services Privatization:

7. Azurix v. Argentina Protecting Investor Profit While Ignoring the Public Right to Affordable Water

In July 2006 an ICSID tribunal determined that Argentina should pay \$165.2 million to Azurix, the water division of the scandalous Enron Corporation which has become a symbol of willful fraud and corruption. Azurix had claimed \$565 million in compensation from the government of Argentina although the ICSID tribunal decided to award them less than a third of this amount.⁹³

The water privatization project began when, in 1999, Azurix agreed to pay \$438 million for the exclusive right to provide water and sanitation services to the Argentine Province of Buenos Aires for 30 years. Relations with the government were rocky from the start, as officials refused to let the company raise water rates as high as they wanted. Then in April 2000 further controversy erupted when an algae outbreak led provincial officials to warn citizens that they should boil their water before consuming it, prompting some customers to refuse to pay for the water. Azurix blamed Argentine government officials for the situation, which they said was caused by years of disinvestment.⁹⁴ In October 2001, shortly after parent company Enron announced it would break-up Azurix and sell its assets, the company withdrew its contract in Argentina, accusing the provincial government of “serious breaches” and filing a compensation claim with ICSID.⁹⁵

Azurix claimed that the government's actions subjected them to expropriation without compensation. They also argued that Argentina had violated vaguely worded clauses in a U.S.-Argentina BIT that require “fair and equitable treatment” and “full protection and security.” Argentina argued that their regulatory measures were taken in pursuit of important public interests -- ensuring that citizens have access to essential public services such as clean, safe, affordable water. The Argentine government distinguished between “legitimate regulation and confiscatory regulation.” However, the ICSID tribunal concluded that “the issue is not so much whether the measure concerned is legitimate and serves a public purpose, but whether it is a measure that, being legitimate and serving a public purpose, should give rise to a compensation claim.”⁹⁶

In the end, the ICSID tribunal decided that the actions of the Argentine government did not rise to the level of an expropriation but rather there were breaches of the “fair and equitable treatment” and “full protection and security”

The Azurix tribunal interpreted “fair and equitable” treatment to be not merely a negative obligation to refrain from bad faith, but a positive obligation to facilitate the success of the foreign investor. The result is that if governments decide to serve the public good rather than narrow corporate interests, they must be ready to pay a high price.

clauses of the BIT. The tribunal acknowledged that some recent U.S. investment agreements limited the concept of “full protection and security” to physical police protection required under customary international law. Nevertheless, the tribunal was of the view that this clause did not have a merely physical protective component, but further required that host governments ensure the “stability afforded by a secure investment environment.” Regarding fair and equitable treatment, the tribunal stated that: “(t)he standard of conduct agreed by the parties to a BIT presuppose a favorable disposition toward foreign investment, in fact, a proactive behavior of the State to encourage and protect it.”⁹⁷

The Azurix tribunal interpreted “fair and equitable” treatment to be not merely a negative obligation to refrain from bad faith, but a positive obligation to facilitate the success of the foreign investor. The result is that if governments decide to serve the public good rather than narrow corporate interests, they must be ready to pay a high price.

8. Eureka v. Poland Government Responds to Growing Public Opposition to Privatization and Gets Hit with 1.5 billion Euro Case

In 1999, the Polish government partially privatized the

Box 4

Occidental Petroleum v. Ecuador: A Civil Society Perspective

Interview with Alexandra Almeida of Accion Ecologica in Ecuador

Why is there such anger felt by so many citizens in Ecuador toward Occidental Petroleum and the \$1 billion lawsuit they filed against the Ecuadorian government?

It is absolutely clear to all the citizens of Ecuador that the U.S. company Occidental Petroleum violated the laws of Ecuador, including the Hydrocarbon Law, the concession contract they signed with the government as well as human rights, social rights and environmental laws during their operations. Due to this history, there was a broad mobilization across many sectors of society pressuring the government to terminate the contract with Occidental. On this topic there was a national consensus. There was practically no Ecuadorian citizen that supported Occidental...well, except the Ecuadorians that worked for the company. For Ecuadorians the exit of Occidental was an act of justice. The case symbolized Ecuadorian sovereignty and dignity and because of this it is intolerable that Occidental has dared to bring a claim against the country in international arbitration.

Explain a little about the history of Occidental Petroleum’s activities in Ecuador.

Occidental Petroleum operated in what was known as Block 15 in the Amazon rainforest of Ecuador. An initial contract for operations between Occidental and the government was signed in 1985 and was modified over the years to provide more benefits to the company and fewer to the state. For example on May 18, 1993, Petroecuador (the state oil company) and Occidental signed a contract for the exploration of Camp Limoncocha that provided subsidies to Occidental and cheated the state oil company out of \$70.7 million.

Occidental has systematically violated Ecuadorian laws, for example:

1. The company was fined on six occasions for surpassing the extraction limits, which leads to the overexploitation of the wells;
2. The company invested less than the contract required;
3. The company did not provide information, as the law requires, on the opening of new wells, in the final report on the perforation operations (in 14 instances);
4. The company did not provide information on the transfer of crude oil as required;
5. It did not submit a report on its financial state or its inventories as is required by law.

In total, the state attorney submitted a list of 34 instances where Occidental violated the law. This merited the suspension of the company and the cancellation of the contract. Every day the company extracted and overexploited the wells extracting approximately 100,000 barrels of petroleum each day that should be part of the national budget.



country's largest insurance company, PZU, by selling 30 percent of shares to Dutch-based Eureko. What the company was really interested in was majority control, and so the government also promised to hold an initial public offering for PZU by the end of 2001.⁹⁸

In the meantime, the Polish public became increasingly skeptical about financial services privatization. The privatization of social security in 1999 had had some disastrous results – high administrative costs, abysmal returns during the first few years, and widespread corruption.⁹⁹ In 2005, the Polish government estimated that 18 percent of accounts were bogus, the result of sales agents forging docu-

ments to earn commissions.¹⁰⁰ There were also concerns about rising foreign ownership of the domestic banking sector (today about 70 percent is in foreign hands).¹⁰¹

As a result of the rising opposition and shifts in political power, the government dropped the plan to complete PZU's privatization. In response, Eureko filed a claim before the International Court of Arbitration, charging violations of the "fair and equitable" treatment and other standards of a Dutch-Polish investment treaty. That court accepted the case -- despite the fact that the privatization agreement stipulated that Polish courts would have jurisdiction in disputes between shareholders. In August 2005, the arbitra-

Additionally the company has been accused of:

- Operating in protected indigenous areas. Its operation affects four protected areas: Limoncocha, Panachocha, Yasuni and Cuyabeno.
- Lying to communities when negotiating its operating conditions and at the same time secretly proceeding with the expropriation of their territories (Judith Kimerling. Report: "Practices of the Oil Companies. The case of Occidental". Quito, June 2003)
- Spilling toxic waters into the Napo River in the zone of El Eden. (The complaint was made by the director of Yasuni National Park and by the commune of El Eden in August 2004).
- Using child labor to clean toxic materials in the zone of Jivino in 1991 (Amazonias por la Vida. Quito, 1993, page 37).
- The Eden Yuturi - Lake Agrio pipeline operating without an environmental permit for more than two years.
- Building a secret road near Yasuni National Park in the wilderness area in the Kichwas Indians territory (Servicio de Noticias Ambientales, February 16, 2005).
- Allowing leakages for more than six months in the secondary tubing in Block 15 of the pipeline that Occidental used. (Complaint made by the town of Limoncocha).
- Entering territory that belonged to indigenous communities without authorization in order to build platforms and paths. (Complaint made by the Commune of Kichwas from El Eden and Samona Yuturi on August 2003 and March 2004).
- Using violence that included threats, denunciations, and torture in January 2002 during the construction of the Eden – Agrio Lake pipeline that will be connected to OCP (Alerta Verde, Number 125, May 2003).⁸⁵

How is the new government of Rafael Correa approaching the issue of the Occidental Petroleum case?

According to statements made by Rafael Correa during his campaign, the Occidental case has already been judged and does not merit any type of arbitration. The problem is that the position of the previous government with respect to this case was one that tacitly accepted the arbitration, although they had not given their written consent as ICSID requested. Now the new government is trying to reject what the previous government did.

What actions do you think the government can take to avoid such lawsuits in the future?

Unfortunately these investor-state arbitration cases are increasingly frequent. It is a form of privatizing the system of justice and they have mechanisms that sometimes make it impossible not to fall into these lawsuits, because they are the basis of the bilateral investment treaties which almost every country has signed. I think that a strategy to avoid these lawsuits will require more than just one country but rather the coordination of all Latin American countries to establish mechanisms to free ourselves from these threats that are harming all of our countries.

tion court ruled in Eureko’s favor, prompting the company to demand a minimum of 1.5 billion euros (\$1.97 billion) in damages.¹⁰²

Since then, the Polish government has failed to obtain an annulment but is continuing to fight the ruling and has filed a countersuit. As Deputy Treasury Minister Pawel Szalamacha said recently, “Most decisions concerning finance are made outside Poland’s borders. Such a privatization should not be continued.”¹⁰³

**9. Bechtel v. Bolivia
U.S. Corporation Demanded \$50 million After Provoking Social Unrest**

In the late 1990s, the World Bank forced Bolivia to privatize the public water system of its third-largest city, Cochabamba, by threatening to withhold debt relief and other development assistance. In a process with just one bidder, U.S.-based Bechtel was granted a 40-year lease to take over Cochabamba’s water through a subsidiary called Aguas del Tunari.¹⁰⁴

Within weeks of taking over the water system, Aguas del Tunari imposed rate hikes on local water users of more than 50 percent on average, according to the Cochabamba-based Democracy Center. Families living on the local minimum wage of \$60 per month were billed up to 25 percent of their monthly income.¹⁰⁵ The rate hikes sparked massive citywide protests that the Bolivian government sought to end by declaring a state of martial law and deploying thousands of soldiers and police. More than a hundred people were injured and one 17-year-old boy was killed.¹⁰⁶ In April 2000, as anti-Bechtel protests continued to grow, the company’s managers abandoned the project after the government warned that it could not guarantee their safety.

Aguas del Tunari retaliated by filing an ICSID claim for compensation and lost profits under a Dutch-Bolivia bilat-



Protesters in Cochabamba, Bolivia.

eral investment treaty. At the time there was no such pact between the United States and Bolivia, and so although Bechtel is a U.S. corporation, it established a post office box presence in the Netherlands.¹⁰⁷ Even the Dutch government was ambivalent about whether the corporate shell created by Bechtel should be entitled to take advantage of the treaty, but the ICSID tribunal accepted jurisdiction anyway.

Bolivian “Water Warriors” joined forces with supporters in the United States and elsewhere to pressure Bechtel to drop the lawsuit. In San Francisco, activists occupied the lobby of the corporate headquarters, while the City Council passed a resolution criticizing the company’s legal action. Earth Justice, along with a Center for International Environmental Law and Friends of the Earth, drafted a legal petition on behalf of Bolivian civil society leaders demanding that they be allowed to participate in the lawsuit proceedings. The Democracy Center helped organize a sophisticated international media strategy and, along with the Institute for Policy Studies, helped coordinate a citizen sign-on letter in support of the legal petition that was endorsed by people in more than 40 countries.¹⁰⁸

Battered by several years of bad publicity, Bechtel settled the \$50 million lawsuit for a symbolic amount of about 30 cents on January 19, 2006.¹⁰⁹

Case Related to Emergency Protections in Economic Crisis

**10. CMS Gas Transmission Company v. Argentina
Argentina Challenges Decision and Calls for Annulment**

In May 2005, an ICSID tribunal decided against Argentina and awarded \$133.2 million plus interest to CMS Gas Transmission Company. The case has tremendous importance for Argentina due to its unfortunate status as the country with more than 30 ICSID cases filed against it – approximately one third of all pending ICSID claims. The CMS decision could have significant implications for the other Argentine cases. Like many of the other cases, the CMS case relates to government actions in 2002 in response to a financial meltdown that had caused severe social, economic, and political crisis.

CMS argued, and the ICSID panel agreed, that the Argentine government violated its privatization arrangement with the company when it froze utility rates in early 2002, as part of the Economic Emergency Law.¹¹⁴ By keeping rates constant in peso terms, the government aimed to protect Argentine consumers from runaway inflation. During this period the international value of the peso, which had been pegged to the U.S. dollar, plunged by 70 percent. CMS

demanded compensation for massive revenue losses caused by the rate freeze.¹¹⁵

The Argentine government countered that the Economic Emergency Law was fair since the domestic component of the utilities' cost structure was also considerably reduced as a result of the devaluation. The government also argued that the entire economy had been "pesoized," meaning that all transactions were conducted in pesos and thus foreign-owned utilities were treated no differently than domestic firms.¹¹⁶

CMS argued that it had borrowed in dollars to invest in Argentina and needed to be paid back in dollars. The Argentine government responded that the privatization contract did not give CMS a guaranteed right of profit or a guarantee that tariffs would be tied to the dollar. And, besides, the government faced a national emergency. Customary international law has long recognized the "necessity defense," which allows a government to take actions in response to a crisis that might otherwise violate international obligations. Nevertheless, the ICSID panel ruled that the government's action constituted a denial of "fair and equitable treatment" for CMS under the U.S.-Argentine BIT.¹¹⁷ A year and a half later, another ICSID tribunal came to a different conclusion in the case of LG&E against Argentina, despite the fact that the government's "necessity defense" relied on the same economic crisis.¹¹⁸

Argentina's Minister of Justice, Horacio Rosatti, was sharply critical of the CMS decision. Reflecting on the case from the point of view of Argentine sovereignty, he said it is obvious to every Argentine citizen that an issue regarding consumer rates for public utility services should not be decided by the World Bank's ICSID tribunal. He also pointed out the problem of conflict of interest due to the fact that CMS has a \$200 million loan from the World Bank.¹¹⁹

Argentine Government's Strategy

The Argentine government has a multi-level strategy to challenge the ICSID cases. One approach has been to broaden the possibility of local judicial review of arbitral awards. An important Argentine Supreme court decision, *Jose Cartellone Construcciones vs. Hidroelectrica Norpatagonia S.A.*, upheld that when matters of public policy are involved, local courts may review the reasonableness, fairness, and constitutionality of an arbitral award.¹²⁰ The Argentine prosecutor argued in a hearing of the CMS case that bilateral treaties do not supercede the Argentine national constitution and that a company engaged in the rendering of public services cannot impose a limitation on the sovereign right of the government to change consumer rates. In 2004 the Argentine government sent a draft bill to Congress establishing a new legal framework for the concession of public services that would subject such contracts to local



The headquarters of Aguas Argentinas (Suez) in Buenos Aires used to be the National Palace. Banners condemn the hikes in consumer water rates. Photo courtesy of Sara Grusky.

law and courts eliminating the possibility of submitting disputes to outside sources.¹²¹

Immediately following the ICSID tribunal's award to CMS of \$133.2 million, the Argentine government filed an application requesting the annulment of the award. In addition, the opposition ARI party in Argentina introduced two bills into Congress, one calling for the cancellation of all BITs and the other for the cancellation of Argentina's signatory status to the treaty that establishes ICSID as a valid international court for investment disputes. Argentina sought annulment on the grounds that the ICSID tribunal manifestly exceeded its powers and that the award had failed to adequately state the reasons on which it was based. Argentina also requested that the payment of the award be stayed until a decision was made on the annulment application. In September 2006, the ICSID Committee agreed that Argentina did not have to pay the award until there was a decision on the application for annulment.¹²²

This case will be widely watched because of its implications for all the other pending Argentine cases. The majority of the pending Argentine cases involve other energy-related companies that were privatized in the 1990s (19 are gas and electric companies, seven are water companies, and five are communications companies) and most of them were also subjected to the emergency restrictions. The total cost of the pending claims is not publicly available information due to the secrecy that surrounds ICSID tribunals, but estimates are around \$30 billion.

IV. Corporate Claims in Support of Investor Protections

Despite mounting public criticism, global corporations have continued to lobby hard for expanded investor protections through trade agreements and investment treaties. The most powerful pressure comes from well-funded and politically connected U.S. business associations, such as the U.S. Council for International Business, the National Association of Manufacturers, and the National Foreign Trade Council. The following section analyzes some of these business groups' key arguments.¹²³

CORPORATE CLAIM #1: “Strong investor protections help developing countries attract additional foreign investment.”

REALITY: Granting excessive protections to foreign investors does not guarantee more foreign direct investment and cripples governments' ability to ensure that investment supports national goals.

A recent Tufts University study on Latin America and the Caribbean found that signing bilateral investment treaties with the United States had no effect on investment flows.¹²⁴ What investors appeared to care more about was whether countries had big domestic markets with educated workforces and could serve as export platforms. China and Brazil are prime examples. Between 1990 and 2001, they were the world's largest recipients of foreign direct investment, even though they have not signed any investment agreements with the United States.

The Tufts study reinforced the findings of previous research. In 2003, a World Bank paper found that countries that signed investment treaties were no more likely to attract additional investment than countries that did not. The author also emphasized the costs of such agreements to host governments in terms of lost policy choices and potentially expensive damages claims. “If there is little apparent benefit, the case to ratify new agreements – at least under terms that are extremely favorable to the investor – is harder to make,” she wrote.¹²⁵

Box 5

Biwater v Tanzania: A Civil Society Perspective

Background on the Case:

In 2005, the government of Tanzania canceled a water privatization deal with British-based Biwater, just two years into a ten-year contract. The controversial contract had excluded the poorest neighborhoods from service.¹¹⁰ Biwater responded to the cancellation by filing a claim with ICSID.

The case has received significant publicity, especially in Britain, where the newspaper *The Observer* ran the headline “UK water giant to sue debt-laden Tanzania.”¹¹¹ Biwater complained to ICSID that the Tanzanian government's release of documents had stoked media and NGO scrutiny and criticism and asked for a ruling that the parties be barred from disclosing correspondence exchanged between them and refrain from disclosing copies of pleadings to third parties.

The Tanzanian government opposed these moves by Biwater and argued for greater transparency in the conduct of the case. However, the tribunal ruled that in the absence of agreement between the parties they should refrain from disclosing minutes, records, documents produced by the opposing party, witness statements, expert reports and correspondence between the parties.¹¹² While many of the documents will remain secret, the tribunal did agree to accept an amicus curiae brief from affected civil society organizations.¹¹³ The case is scheduled to be heard in April 2007.

Interview with Mussa Billegeya, (Tanzania Association of NGOs- TANGO)

How do Tanzanians feel about the ICSID case that the British company Biwater has filed against the government for US\$25 million?

It isn't clear for many Tanzanians what exactly happened beyond the failure of the water company. Most people in Tanzania don't know anything about ICSID. They might know about World Bank conditionalities and trade agreements – this is something we in Tanzania have grown used



Informal water vendors pull small carts with jugs full of water.

One 2005 study by Harvard researchers did find a correlation between U.S. investment flows and investment treaties, but another by two Yale University researchers that used a much larger sample and a longer time period found that developing countries overall did not experience such benefits.¹²⁶

Tying the Hands of Government

While there is no strong evidence that extreme investor protections attract additional investment, it is clear that they cripple governments' power to ensure that the investment they do get supports national goals. For example, prohibitions on "performance requirements" limit governments' authority to maximize the social, economic and environmental benefits of investments. Such rules under NAFTA have meant that the Mexican government may not demand that the thousands of foreign-owned factories along the U.S.-Mexico border use a certain level of domestic inputs in order to ensure a "multiplier effect," or broader benefits for the economy. In 2000, the Mexican

government reported that domestic content of maquiladora production was only 3.5 percent.

Most recent U.S. trade and investment treaties also protect foreign investors from controls on capital such as the ones that have been used successfully to insulate countries to some extent from the devastating impacts of financial crisis. Even the International Monetary Fund broke with its traditional opposition to capital controls in 2000 and issued a report that found that controls used by Chile, Brazil and Colombia had been useful. Since then, IMF officials have supported at least limited use of capital controls in countries such as Tunisia, Russia, and Argentina.

The UN Economic Commission on Latin America and the Caribbean has also been sharply critical of the "more is better" approach to attracting foreign direct investment. One study concluded that as a result of unregulated investment policies, "countries often find that they have assumed obligations which, further down the road, will place limitations on their own development programs."¹²⁷

to – and exploited by. We know that the international financial and trade systems don't work in our favor. But, when Tanzanians hear about the Biwater case in ICSID they feel that it's part of the global operation that works against poor countries, that works against their sovereignty. While most people do not know about the specifics of the case, they know it's part of the system working against poor countries.

What is Biwater trying to achieve?

After Biwater defaulted on the contract – I remember in one of their press releases from 2005 – they said that the government of Tanzania took the property from them. They said that the government cancelled the contract. Biwater is trying to tell the world that it's a political move by the government against their company. What they really wanted is to win the support of the outside world, and present the case as if they did a good job in Tanzania. Their story is that the government was at fault, not Biwater. They want money that they claim they lost when the contract was cancelled. But the real story for Tanzanians and residents in Dar es Salaam is quite different.

What happened when Biwater took over the water system in Dar es Salaam?

The water system was leased to a consortium, led by Biwater, in 2003. The intention was to improve the system. But Biwater never performed well under the terms of the contract. They were supposed to increase revenue, but they couldn't collect the water fees. They didn't even pay the lease fee to the government. They owed around US\$ 3.5 million to the government in 2005. They did not contribute to a collection fund that was meant for the poorest people. They were doing almost none of what they were supposed to do. Biwater was supposed to inject \$8.5 million of capital but they fell far short of that.

What did it mean to people in Dar es Salaam?

All the local NGOs had spoken out against the privatization before it even happened. Everyone on the ground had spoken out against it. There was no evidence that water privatization was going to work. But there was nothing we could do. It was part of the conditions from the World Bank. People didn't feel that the project belonged to them. For most of the people absolutely nothing changed. It seemed like a waste of money. Many people were only getting water 1-2 times a month. I remember that there was a large outbreak of water borne diseases as people couldn't access clean water. Now that the system has been returned to the public there's more oversight and regulation. And more people are getting water.

History has shown that foreign investment can play a positive role when it creates dignified jobs and is consistent with democratically determined national development and environmental goals. Nearly every successful economy (including the United States) has developed by lifting barriers to investment only gradually and selectively.

CORPORATE CLAIM #2: “Strong investment protections ...foster democratic principles and policies”

REALITY: Extreme investor protections undermine, rather than promote democracy.

These rules give foreign investors the right to attack public interest laws, regulations, and other governmental acts developed through democratic processes, merely because their profits might be adversely affected. Moreover, decisions regarding investor-state claims are made by non-elected, unaccountable “experts” who are not subject to standard judicial ethics rules.

According to Professor David Schneiderman of Georgetown University, “These are lawyers drawn from the international trade and investment law bar. They are not ordinarily well-versed in human rights, environmental law, or the social impact of legal rulings. These are matters one might expect judges in national high courts to have some familiarity or concern with. They are not matters considered relevant to international investment law or the qualifications of arbitrators (who also may act as legal counsel in another case).”¹²⁸

Governments that are parties to such agreements have to weigh the value of new public interest regulations against the threat of an expensive corporate lawsuit. In the United States, the National Conference of State Legislatures has raised serious concerns about the threat posed by inves-

tor protections to democracy. In a letter submitted to the U.S. Trade Representative, NCSL stated, “Provisions in the FTAA draft text providing for an investor-state dispute settlement mechanism (a private right of action) in investment-related disputes are very troubling in light of recent experience under the NAFTA. In particular, NCSL is concerned about this mechanism being used to bring unreasonable challenges to state sovereignty.”¹²⁹

CORPORATE CLAIM #3: “Foreign investment by U.S. companies complements their activities in the United States.... The payoff is better, higher-paying jobs and a higher standard of living in the United States.”

REALITY: There is no guarantee that the benefits of U.S. foreign investment rebound to U.S. workers.

The corporate groups make the sweeping statement that U.S. foreign investment promotes “greater productivity, research and development, investment in physical capital and new technology.”¹³⁰ One letter points out that “over 40 percent of large company exports go to their foreign affiliates. For small companies, the figure is nearly 20 percent. These exports support more than \$2 trillion in sales of our foreign affiliates abroad.”¹³¹

The suggestion here appears to be that U.S. corporations that invest abroad in order to take advantage of cheaper labor or closer proximity to foreign consumers increase their profits and then automatically channel these profits into better wages for U.S. workers and better technology for U.S. factories. The record over the past 15 years does not support such a claim. Between 1990 and 2004, U.S. foreign direct investment skyrocketed from \$31 billion to \$222 billion.¹³² However, U.S. workers received little of the benefits of the explosion of U.S. foreign investment. As more and more U.S. firms transferred production overseas, the number of Americans employed in manufacturing has declined sharply, from 18 million in 1989 to only 14.2 million last year.¹³³ Meanwhile, the growth jobs in the U.S. economy are overwhelmingly in the service sector, where wage levels are much lower on average than in manufacturing.

CORPORATE CLAIM #4: “The investor-state provisions neither undermine nor interfere with environmental, health, and safety laws that are applied in an even-handed and non-discriminatory manner.”

REALITY: Investor protections do make public interest laws vulnerable to corporate attacks.

Many investor-state lawsuits have targeted environmental, health, and safety regulations, with foreign investors

In 2003, a World Bank paper found that countries that signed investment treaties were no more likely to attract additional investment than countries that did not.

As a result of unregulated investment policies, “countries often find that they have assumed obligations which, further down the road, will place limitations on their own development programs.”

- UN Economic Commission on Latin America and the Caribbean

arguing that these measures diminished the value of their investment. In two widely publicized NAFTA cases, arbitration panels ruled in favor of the investor. These include the Metalclad case, in which a Mexican municipality denied a permit for a hazardous waste facility, and the S.D. Myers case, regarding Canada’s ban of exports of toxic PCB wastes.

For the business groups’ claim to be true, the governments in these cases would have had to have applied laws in an unfair and discriminatory manner. However, it must be understood that when these groups speak of fairness, they are referring strictly to the governments’ treatment of the foreign investor, not their treatment of potentially affected communities, workers, or natural resources. The arbitration panels that handle these cases do not judge the public interest merits of the governmental acts that are the target of the lawsuits. The overriding goal is to promote investor rights, not environmental sustainability or other social interests.

In the case of Metalclad, the judges found that Mexico had “expropriated” the firm’s property when the state declared an area that includes the landfill site to be an ecological reserve.¹³⁴ The test for expropriation was focused narrowly on whether Metalclad’s property rights had been affected. The proceedings did not address the question of whether it was fair to force Mexico to pay a company not to expose the local community to potentially hazardous toxic waste. The



Photo courtesy of Indymedia Ecuador.

government lost and Mexico was ordered to pay about \$15 million in damages (*see page 12 for more details*).

In the S.D. Myers case, Canada’s offense was that it banned PCB exports for a 16-month period in the mid-1990s. U.S.-based S.D. Myers wanted to import the waste for disposal at its U.S. facilities. The Canadian government argued that the ban was part of its commitment under the Basel Convention, an international treaty that obliges countries to take care of their own waste treatment problems rather than dump them on neighbors.¹³⁵ The tribunal found that the action was discriminatory because it gave Canadian waste disposal companies an advantage over S.D. Myers. By awarding damages to S.D. Myers, the tribunal signaled that under NAFTA, corporate profits are more important than international environmental treaties.

Defenders of these investor protections often point out that arbitral panels can force a country to pay damages but can’t force them to repeal a law. While this may be true, the reality is that when forced to choose between a steep damages claim and repealing the law, many governments are likely to opt for the latter.

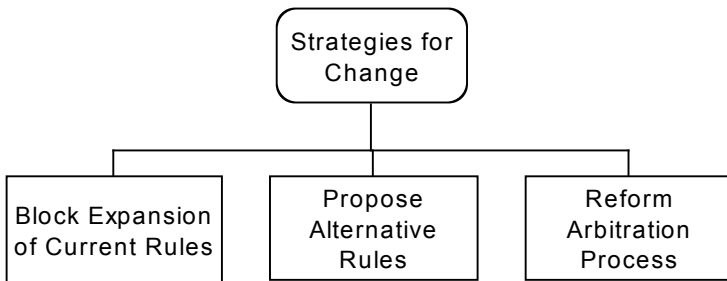
“We know the rules are rigged. Why should we play?”

- Jim Shultz, the Democracy Center (Cochabamba, Bolivia)

V. Strategies for Challenging Excessive Investor Powers

There appears to be broad agreement among many civil society organizations, development professionals, academics, southern governments, and legal experts that the current international investment law regime is not working well, is not a level playing field and does not provide fair, neutral and objective resolution mechanisms. However, while there seems to be wide consensus on the need for change, the nature of the needed reforms is hotly contested.

Many civil society groups argue for the complete dissolution of the current international investment law regime. As Jim Shultz, of the Democracy Center in Cochabamba, Bolivia, puts it, “We know the rules are rigged. Why should we play?” Instead, many of these groups call for the construction of alternative rules focused on the responsibilities of international investors to ensure sustainable development and enhance environmental, labor, and human rights protections. Others believe the system is not so deeply flawed as to be beyond repair or reform. This section lays out some of the key strategies for change, including halting new investor protections and proposing new substantive rules, as well as more modest efforts to reform the process of international arbitration.



A. Block Expansion of Current Rules

Developing country governments worked as a bloc to keep investor protections off the agenda for the current round of World Trade Organization negotiations. Brazil’s strong opposition to the U.S. investment model contributed to the failed talks for a hemispheric trade pact. In Ecuador and Bolivia, citizen concerns about investment rules were a factor in the election of leaders who are opposed to negotiating free trade agreements with the United States.

Despite these setbacks, the Bush administration has pushed ahead by including extreme investor protections in several new regional and bilateral free trade agreements and investment treaties. Their ability to do this may change, however, as a result of the shift in power in the U.S. Congress. New Democratic leaders have promised to reform U.S. trade policy, starting with Peru and Colombia trade

pacts that, as of this writing, have been negotiated but not ratified.

However, key Democrats appear to be focused primarily on strengthening the labor rights language in the agreements, rather than pursuing a broad overhaul that would include a new approach on investment. U.S. environmental, labor, and other groups are working with international allies to ensure that concerns about investment rules are not overlooked in the debate over bilateral trade pacts. They are also planning to mount a major campaign to prevent the renewal of “fast track” or “trade promotion” authority, which allows the U.S. Executive Branch to negotiate new trade agreements that must pass Congress on an up or down vote, without amendment, and with limited time for debate. The current fast track expires in July 2007. At a January 2007 conference, representatives of 10 major fair trade coalitions and labor and environmental groups discussed plans to block the old, anti-democratic fast track and propose new guidelines for the Executive Branch that would include a prohibition against any deals that include excessive investor protections.

B. Propose Alternative Rules Broad New Agendas on Trade and Investment

The Bolivian government, in response to a request from the Bush Administration, has proposed guidelines for a “fair and productive cooperation treaty with the United States” that welcomes international trade and investment, as long as it does not undermine the national government’s authority to pursue its own development strategies. The plan differs from the U.S. trade model in many ways. For example it would allow governments to guarantee access to affordable general medicines, ban the patenting of plants and animals, and maintain programs that favor local producers. With regard to investment, it would preserve the right to require foreign investors to transfer technologies and use local inputs and labor. It also rejects investor-state dispute settlement and instead would require foreign investors to resolve disputes through national mechanisms.¹³⁶

The Bolivian proposal has similarities with the Bolivarian Alternative for Latin America and the Caribbean (or ALBA, in Spanish), developed by the Venezuelan government as an alternative to the proposed Free Trade Area of the Americas. That proposal also would allow governments to put performance requirements on foreign investment and prevent corporations from undermining public interest regulations.¹³⁷

The political shift in the U.S. Congress may open some opportunities for pursuing positive alternative approaches that eliminate the most excessive investor protections.

However, Bolivia and most other countries in the hemisphere are already locked into bilateral investment treaties, which are extremely difficult to withdraw from (see Box 6). Among their options:

- Governments that share strong criticism of the current rules (e.g., Argentina, Ecuador and Bolivia) could negotiate new investment agreements with each other that serve as positive models.
- They could give notice of intent to withdraw from investment treaties. Since this would be perceived as financially risky, another approach would be to form country blocs to demand that the U.S. government (and also, perhaps, European governments) renegotiate existing deals. As Alexandra Almeida of Accion Ecologica in Ecuador stated in Box 4 of this report, “I think that a strategy to avoid these lawsuits will require more than just one country but rather the coordination of all Latin American countries to establish mechanisms to free ourselves from these threats that are harming all of our countries.”

Investment Models that Promote Sustainable Development

The Canadian-based International Institute for Sustainable Development has led a consultative effort to develop a more balanced set of investment rules.¹³⁸ The model is innova-

“Allowing corporations to bypass domestic courts is not going to strengthen them. They need to be tested and if they fail, then, and only then, should investors have recourse to an international tribunal.”

- David Waskow, Friends of the Earth

tive in that it would require investors to abide by various internationally recognized labor, environmental and human rights standards, as well as perform environmental and social impact assessments of their potential investments. Violations of any of the agreement’s obligations could result in the investor losing the right to use the dispute settlement mechanism. Anti-corruption provisions would apply to investors as well as home and host states. The model agreement also encourages home states (which tend to be richer nations) to provide assistance to developing countries to facilitate foreign investment, including help with technology transfer, insurance programs, and capacity building.

The IISD model would require foreign investors to exhaust domestic remedies before taking disputes to international tribunals. However, this is waived when domestic judicial or administrative processes are found to lack independence or timeliness.

According to IISD’s Howard Mann, a number of developing countries are looking carefully at the model agreement, with a view to incorporating provisions into bilateral treaties. It is being used as a model for at least two regions in the negotiations between the EU and former European colony countries to form so-called Economic Partnership Agreements. The OECD Investment Committee is also reviewing the model.

The IISD model has been sharply criticized by some in the business community. William A. Reinsch, President of the National Foreign Trade Council, charged that the requirement to exhaust domestic remedies would create a formidable hurdle since, in his words, “the domestic judicial system in many developing countries is corrupt, inefficient, and/or inexperienced.” Moreover, he argued that “it is not a corporation’s responsibility to act as a shadow government, as it would have to under this model agreement.”¹³⁹

The strongest critics of current investor protections have not been particularly enthusiastic about the IISD model either. According to Mary Bottari, who has written extensively on investor-state issues for Public Citizen’s Global Trade Watch, “IISD’s Model is an attempt to create a ‘kinder, gentler’ version of the same bad rules. It not only preserves the investor-state dispute resolution process, but it even preserves an investor’s ability to challenge a government’s application of performance requirements which are key tools used by developing countries to leverage economic development.”¹⁴⁰ The model also fails to give private citizens any significant new powers. The model document merely requires that each government set up a national contact point for investigating and seeking to resolve concerns raised by individuals or civil society groups about investor conduct.

Proposals of U.S. Environmental Groups

In January 2007, U.S. environmental groups submitted recommendations to the new, Democratic-controlled Congress on a range of trade issues, including investment. They stated that investment disputes should be addressed on a government-to-government basis. If, however, an investor-state mechanism was inevitable, investors should have to exhaust domestic remedies. According to David Waskow of Friends of the Earth, the lead drafter of the recommendations, “I realize there are concerns over domestic courts, but allowing corporations to bypass domestic courts is not going to strengthen them. They need to be tested and if they fail, then, and only then, should investors have recourse to an international tribunal.”¹⁴¹

The environmental groups also recommended that investors should be prohibited from filing suits over government decisions regarding natural resource issues. Moreover, any deal should give private citizens the same rights for enforcement and remedies as corporations.¹⁴²

Strip Investor-State Dispute Rules -- Revive the “Calvo Doctrine”

The 2004 U.S.-Australia Free Trade Agreement does not include investor-state dispute resolution, due to the Australian government’s resistance. While free trade critics would have preferred no agreement at all, the omission of this extreme investor privilege set an important precedent by allowing domestic courts to have the final jurisdiction in investor disputes. Governments that are currently engaged in trade negotiations with the United States should consider taking the same position as the Australian government. Those that already have U.S. trade agreements could also build on the Australia precedent by requesting that their deals be re-negotiated to exclude the investor-state provision.

Ronald J. Daniels, Provost of the University of Pennsylvania, offers a compelling argument for reviving the Calvo doctrine, which subjects foreign investors to the same laws and courts as domestic investors. Essentially, he argues that if foreign investors lost the privilege of taking disputes to international tribunals, they would have a greater interest in allying with “often voiceless” citizens in developing countries who are fighting for good rule of law reforms against entrenched political elites. The current BIT legal regime, Daniels says, “constitutes a legal enclave of sorts, where many of the risks of legal and political failure that confront domestic investors generally are substantially lessened or, indeed, eradicated, for foreign investors.” This, Daniels argues, “inflicts a double whammy on law reform efforts in developing states, first by dulling the interest of foreign investors in building good domestic rule of law institutions and then by encouraging foreign investors to devise alternative institutional arrangements that are in-

imical to the development of sound regulatory institutions and policies.”¹⁴³

Others have suggested that some provisions of the agreements could be narrowed in scope or more clearly defined. Christian Leathley, who specializes in international arbitration with the law firm WilmerHale, cited the vague “fair and equitable treatment” standards included in most agreements as particularly problematic. “The rulings on this have become a one-way street in favor of the investor with no ability for the state to push back,” Leathley said.¹⁴⁴

C. Reform the Arbitration Process

After 18 months of consultation with representatives from governments, lawyers, businesses and civil society, ICSID made some limited changes to its arbitration rules in April 2006. Most of these related to transparency and participation. The new rules allow third parties to attend oral hearings, but only if none of the parties to the proceedings object. They also establish procedures that allow a tribunal to accept amicus briefs, even if the parties object. However, the decision on whether to accept the submission must consider whether the nonparty has a “significant interest” in the proceeding and other criteria that are open to wide interpretation. In addition, the new rules require ICSID to publish excerpts of the awards that reveal the tribunal’s legal reasoning. The old rules left this up to ICSID’s discretion.¹⁴⁵

ICSID had already begun to open up a bit prior to the April 2006 reform. In 2005, an ICSID tribunal agreed to accept amicus briefs submitted by NGOs in a dispute concerning the Buenos Aires water and sewage system, despite opposition from the foreign investors (Suez and Vivendi (see Box 7)).¹⁴⁶ However, while there have been some steps forward,

“The rulings on this [‘fair and equitable treatment’ standard] have become a one-way street in favor of the investor with no ability for the state to push back.”

- Christian Leathley, international arbitration specialist

many civil society organizations argue that ICSID's changes do not go far enough. The following are additional proposals for changing the arbitration process.

Further Increase Transparency and Participation

The decisions on these cases can have tremendous impacts on public health, the environment, access to basic public services and overall quality of life. Civil society organizations have argued that in cases where there is a clear public interest, tribunals should be obliged to ensure open hearings, document disclosure and acceptance of amicus briefs. Some have called for ICSID to go even further to ensure the participation of affected citizen groups. For example, Earthjustice Legal Defense Fund submitted a petition in 2002 on behalf of Bolivian civil society organizations and leaders requesting that they be allowed to participate in the proceedings of the Bechtel v. Bolivia "Water War" case. Specifically, they requested that the tribunal members travel to Bolivia to receive public testimony, in addition to opening hearings to the public and releasing all documents.¹⁴⁷ The petition was rejected. In the Vivendi/Suez case, while the tribunal agreed to accept amicus briefs, it did not agree to the NGOs' demands to open hearings to the public and disclose all documents produced in the arbitration (see Box 7).

Civil society organizations have argued that in cases where there is a clear public interest, tribunals should be obliged to ensure open hearings, document disclosure and acceptance of amicus briefs.

Box 6 Straitjacket BITs

Bilateral investment treaties (BITs) are designed to be extremely difficult to break. The 2001 U.S.-Bolivia treaty is typical. After the initial 10 years, either Party can give one year's written notice of intent to terminate the treaty. However, the treaties' protections must continue to apply to all covered investments for another 10 years. Hence, the treaty is designed to lock in both countries' commitments at least until the year 2022.

Free trade agreements typically have less onerous termination clauses. NAFTA, for example, requires only six months' notice. However, many governments would fear provoking a "trade war," making withdrawal from a comprehensive trade pact practically impossible.

Create an appeals process

Thus far, ICSID has rejected proposals for the creation of an appeals mechanism. Under the current system, a losing party may ask for the annulment of an award by an ad hoc Committee, but only for narrow reasons, such as the tribunal was improperly constituted, manifestly exceeded its powers, or was corrupt. This means that there is virtually no recourse for rulings that are flawed or inconsistent. According to Susan Franck, a lawyer and professor who specializes in international arbitration, the utility of the system "will not be fully realized until an appellate court is created which permits the correction of legal errors, which might otherwise inappropriately bankrupt developing nations, stifle legitimate regulatory activity, or deprive private investors of their legitimate expectations."¹⁵⁴ Some have proposed a common appeals body that would handle not only ICSID, but also awards by UNCITRAL and other international arbitration tribunals.¹⁵⁵

De-Link ICSID from the World Bank

ICSID will lack credibility as long as it maintains close formal ties to the World Bank. If such an investment arbitration mechanism is indeed necessary, it should re-establish itself as an independent body with international governmental control outside the existing World Bank system.

Box 7

Do Citizens Have a Voice in ICSID Tribunals?

The case of Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal S.A. v. Argentina

By Jimena Garrote of the Centro de Estudios Legales (CELS), Argentina¹⁴⁸

In 2003, despite the fact that they were undergoing contract renegotiations with the Argentine government, the water company Aguas Argentinas S.A. (their major shareholder is the French conglomerate Suez) filed an ICSID case against the government. The company charged that the government's Emergency Economic Law that froze consumer water rates during the Argentine peso crisis was a form of expropriation by default and demanded financial compensation from the government of Argentina for the supposed damage this caused to its investment.

As noted by many human rights organizations, there is a close relationship between access to potable water and sanitation services (in this case provided by the claimant) and the ability to exercise other basic human rights such as the right to an adequate standard of living, and the right to a decent and dignified standard of housing and health. There was a broad public interest in this case and in the renegotiation of the contract, in part because the entry of a new Argentine government opened greater possibilities for the participation of citizen's organizations. This enabled a group of civil society organizations, including the Centro de Estudios Legales (CELS), to present a petition seeking participation as *amicus curiae* (friend of the court).¹⁴⁹ The petition presented by CELS and four other civil society organizations challenged the secrecy of the proceedings by claiming that when investor-state cases addressed questions of broad public interest the request for confidentiality should not be admissible. The petition goes on to state:

The government's decisions questioned by Aguas Argentinas S.A. involve general economic measures adopted by the Argentine government to face a sizable economic crisis. The scope and application of such measures, albeit involving consequences to the complainant and to all the economic activities conducted in Argentina, also determine the way in which inhabitants have access to and enjoy the essential public service of drinking water and sanitation.¹⁵⁰

The petition also states:

It is clear that the final decision adopted as a result of this process will have a substantial impact on the ability of the inhabitants of Buenos Aires City and Greater Buenos Aires to access indispensable basic services of water and sanitation. It is also equally clear that this process and the resulting decisions should not be conducted in secrecy, without civil society participation, particularly of those who are directly affected.¹⁵¹

The petition challenged as a potential conflict of interest the close existing relationship between ICSID and other institutions that form part of the World Bank Group such as the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC). The IBRD has played a key role in the design of the regulatory framework for the privatized public services in Argentina and the IFC held a percentage of Aguas Argentinas equity shares.

The *amicus curiae* petition was unanimously admitted by the arbitration tribunal of ICSID following consultation with all the parties in the case. The Argentine government was firmly in favor of the participation of civil society organizations while the shareholders of Aguas Argentinas were in opposition and claimed that "the public and institutional importance of the case did not exist."¹⁵²

The Tribunal concluded that:

This case is not simply a contract dispute between private parties where nonparties attempting to intervene as friends of the court might be seen as officious intermeddlers. The factor that gives this case particular public interest is that the investment dispute centers around the water and sewage systems of a large metropolitan area, the

city of Buenos Aires and surrounding municipalities. Those systems provide basic public services to millions of people and as a result may raise a variety of complex public and international law questions, including human rights considerations. Any decision rendered in this case, whether in favor of the Claimants or the Respondent, has the potential to affect the operation of those systems and the public they serve.¹⁵³

This decision was without precedent in the history of ICSID due to its recognition of the public interest that permeates the case and due to the fact that civil society will be given a voice through the submission of an amicus curiae brief. However, despite the fact that the tribunal endorsed greater transparency in cases where there is a broad public interest, the tribunal rejected the request of civil society organizations to open the hearing of the case to the public. That request was denied expressly due to opposition from Aguas Argentinas.

VI. Conclusion

There is strong evidence that the current system of international investor protections has granted excessive powers to global corporations. In a growing body of cases, powerful firms have exploited these rules to undermine democratic processes, often at the expense of vulnerable communities and the environment. On the other hand, there is scant evidence that agreeing to these deals brings strong benefits

for national economies. Policymakers should carefully review this record and fully weigh the risks before signing any deals that expand this flawed and unbalanced system. At the same time, policymakers and civil society groups should build consensus around strategies to challenge existing investor protection and to advance an alternative set of rules that would allow democratic governments to play responsible roles in ensuring that foreign investment supports social and environmental goals.

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Appendix: ICSID Cases in which Claimant Ranks among Global 500 (as of February 2007)

Concluded Cases

Claimant	Parent	Defending country
Alcoa Minerals of Jamaica, Inc	Alcoa	Jamaica
Kaiser Bauxite Company	Alcoa	Jamaica
Reynolds Jamaica Mines Limited and Reynolds Metals Company	Alcoa	Jamaica
Cargill	Cargill**	Poland
AGIP S.p.A.	ENI	People's Republic of the Congo
Azurix Corp.	Enron*	Argentina
Mobil Oil Corporation and others	Exxon Mobil	New Zealand
Mobil Argentina S.A.	Exxon Mobil	Argentina
France Telecom S.A.	France Telecom	Argentina
IBM World Trade Corp	IBM	Ecuador
Motorola Credit Corporation, Inc.	Motorola	Turkey
Siemens A.G.	Siemens	Argentina
Togo Electricite	Suez	Togo

Pending

Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc.	ADM	Mexico
Wintershall Aktiengesellschaft	BASF	Argentina
BP America Production Company and others	BP	Argentina
Pan American Energy LLC and BP Argentina Exploration Company	BP	Argentina
Cargill, Incorporated	Cargill**	Mexico
Cemex Asia Holdings Ltd	Cemex	Indonesia
Chevron Block Twelve & Chevron Blocks Thirteen and Fourteen	Chevron	Bangladesh
DaimlerChrysler Services AG	DaimlerChrysler	Argentina
Duke Energy Electroquil Partners and Electroquil S.A.	Duke Energy	Ecuador

Claimant	Parent	Defending country
Duke Energy International Peru Investments No. 1 Ltd	Duke Energy	Peru
Aguaytia Energy, LLC	Duke Energy	Peru
LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc.	E.On	Argentina
EDF International S.A., SAUR International S.A. and Leon Participaciones Argentinas S.A.	Électricité De France	Argentina
EDF (Services) Limited	Électricité De France	Romania
Enersis S.A. and others	ENI	Argentina
Saipem S.p.A.	ENI	Bangladesh
Mobil Exploration and Development Inc. Suc. Argentina and Mobil Argentina S.A.	Exxon Mobil	Argentina
Metalpar S.A. and Buen Aire S.A.	Itaúsa	Argentina
Rumeli Telekom A.S. and Telsim Mobil Telekomunikasyon Hizmetleri A.S.	Motorola	Kazakhstan
Occidental Petroleum Corporation and Occidental Exploration and Production Company	Occidental	Ecuador
Repsol YPF Ecuador S.A.	Repsol YPF	Ecuador
Shell Brands International AG and Shell Nicaragua S.A.	Royal Dutch Shell	Nicaragua
TSA Spectrum de Argentina, S.A.	RWE	Argentina
Biwater Gauff (Tanzania) Limited	Saint-Gobain	Tanzania
Suez, Sociedad General de Aguas de Barcelona S.A. and Interagua Servicios Integrales de Agua S.A.	Suez	Argentina
Aguas Cordobesas S.A., Suez, and Sociedad General de Aguas de Barcelona S.A.	Suez	Argentina
Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal S.A.	Suez	Argentina
Togo Electricite	Suez (Elyo)	Togo
Telefonica S.A.	Telefonica	Argentina
Total S.A.	Total Group	Argentina
Compania de Aguas del Aconquija S.A. and Vivendi Universal	Vivendi	Argentina

Source: Fortune magazine, July 24, 2006 (ranked by revenues)

*was in the Global 500 at the time of the filing.

**a privately held corporation, but revenues would put it in the Global 500.

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