The Age of Mega-Regionals – TPP and Regulatory Autonomy in International Economic Law

Discrimination or legitimate government regulation? Striking a balance in the TPP

Richard Braddock[*]

Draft: 15 May 2016

Abstract

The obligation of National Treatment is a key protection against discrimination of foreign investors. However, the fact that a foreign investor is treated differently or adversely affected by government regulation does not necessarily establish a breach. Tribunals have recognised that national treatment does not prevent governments from regulating in the public interest, even where this has a detrimental effect on an investment. The key question is how to distinguish between illegitimate discrimination on one hand, and legitimate government regulation on the other. This presentation examines how the Trans-Pacific Partnership Agreement seeks to clarify this distinction and provide greater certainty to the government parties in the context of recent arbitral interpretations of national treatment.

1. Introduction

Discussions around the potential risks of investor-State dispute settlement (ISDS) for legitimate government regulation often focus on the obligations of fair and equitable treatment and expropriation. Attempts to refine and clarify investment obligations – including to introduce safeguards for regulatory autonomy – have tended to focus on these two obligations.[1] Given that they are by a good margin the most commonly invoked obligations in ISDS claims this is understandable.[2] In contrast there has been considerably

[*] Partner, Lexbridge Lawyers.

[1] See for example the *North American Free Trade Agreement* (entry into force 1 January 2004) (*NAFTA*), the *Korea-Australia Free Trade Agreement* (entry into fore 12 December 2014), the *EU-Canada Comprehensive Economic and Trade Agreement* (text released following completion of the legal review on 29 February 2016).

[2] According to the *UNCTAD Investment Dispute Settlement Navigator* there have been 392 cases alleging a breach of expropriation (317 of these alleging indirect expropriation) and 347 cases alleging a breach of fair and equitable treatment or the minimum standard of treatments. <http://investmentpolicyhub.unctad.org/ISDS/FilterByBreaches>, accessed 10 May 2016.

less focus on attempts to refine or clarify the national treatment obligation in investment agreements. The Trans-Pacific Partnership Agreement (TPP) is an exception. In the TPP the parties took a novel approach to provide more guidance on the interpretation of the national treatment obligation and its relationship to legitimate government regulation. This paper will review the interpretation of the national treatment obligation and its implications for regulatory autonomy focusing on ISDS cases brought under the North-American Free Trade Agreement (NAFTA). It will then explore how the TPP parties responded to some of the arbitral interpretations of national treatment and the implications of the TPP approach.

2. Overview of national treatment claims

Like fair and equitable treatment and expropriation, the national treatment obligation has implications for the regulatory autonomy of governments. Government measures can offend national treatment when they discriminate against foreign investors or investments not only on their face, but also in their effect in practice.[3] Examples include a regulatory approval process (for example, for a mine) where more onerous requirements are imposed on a foreign investor[4], or where a domestic policy (such as a tax rebate) is implemented in a way which disproportionately favours domestic over foreign investors so as to give them a competitive advantage.[5]

In contrast to the obligations of fair and equitable treatment and expropriation, governments have been less active in seeking to clarify the national treatment obligation and its relationship to legitimate government regulation. This lack of attention may be due to the relatively lower rates of claims alleging a breach of national treatment. In relation to all known ISDS disputes, there have been far less claims of national treatment breaches (and a lower rate of success) than either expropriation or fair and equitable treatment.[6]

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[3] See *Marvin Roy Feldman Karpa v United Mexican States (Award) (*NAFTA Chapter 11 tribunal, 16 December 2002*)* (*Feldman v Mexico)* [166]; *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc. v. The United Mexican States (Award)* (NAFTA Chapter 11 tribunal, 21 November 2007*)* (*ADM v Mexico)* [193].

[4] For example *William Ralph Clayton, William Richard Clayton, Douglas Clayton, Daniel Clayton and Bilcon of Delaware, Inc. v Canada (Award*), (NAFTA Chapter 11 tribunal, 17 March 2015) (*Bilcon v Canada).*

[5] See *Feldman v Mexico*.

[6] *UNCTAD Investment Dispute Settlement Navigator: there have been 98 cases alleging a breach of national treatment. In 8 of these cases the investor's claim was upheld. <http://investmentpolicyhub.unctad.org/ISDS/FilterByBreaches>, accessed 10 May 2016.*

However if we focus on the North-American Free Trade Agreement (NAFTA) we get a different picture of the potential risks of national treatment in terms of potential ISDS claims. Under NAFTA there have been more successful claims of national treatment breaches than any other obligation. There have been six successful claims of a breach of national treatment[7] compared to five successful claims of a breach of fair and equitable treatment / minimum standard of treatment[8] and only one successful claim of expropriation.[9]

One might question the merit of focusing on NAFTA when it is only one of the thousands of investment agreements in force. But there are several reasons why cases decided under NAFTA are particularly appropriate in examining the impact of the national treatment obligation on regulatory autonomy, and the approaches taken to address this, in context of the TPP. First, the language of the NAFTA national treatment obligation is substantively identical to the equivalent TPP obligation which is not the case with the majority of existing agreements. Second, six of the eight cases where national treatment claims have been successful were brought under NAFTA. Third, in a Drafters' Note associated with the TPP, the TPP parties have specifically referred to the approach of NAFTA tribunals in interpreting national treatment and have confirmed their intention that the TPP obligation should be interpreted consistently with this.

3. Elements of the national treatment obligation: what conduct will breach national treatment?

For the reasons outlined above, in examining the interpretation of national treatment, this paper will focus on NAFTA cases. Leaving aside the innovative elaborations in the TPP, the language of the obligation and the core elements are substantially identical to NAFTA. As such, it is reasonable to expect that the national treatment obligation would be interpreted in a similar way to the equivalent NAFTA obligation. The national treatment obligation in both the TPP and NAFTA refer to the treatment of both investors and investments, however as the

[7] *S.D. Myers Inc. v Canada (Partial Award) (NAFTA Chapter 11 tribunal, 13 November 2000) (SD Myers v Canada); Feldman v Mexico; ADM v Mexico; Corn Products International Inc. v United Mexican States (Decision on Responsibility) (NAFTA Chapter 11 tribunal, 15 January 2008) (Corn Products v Mexico); Cargill Inc. v United Mexican States (Award) (NAFTA Chapter 11 tribunal, 18 September 2009) (Cargill v Mexico); Bilcon v Canada.*

[8] *Metalclad Corporation v The United Mexican States (Award) (NAFTA Chapter 11 tribunal, 30 August 2000) (Metalclad v Mexico); SD Myers v Canada; Pope & Talbot Inc. v Canada (Award on Merits of Phase 2) (NAFTA Chapter 11 tribunal, 10 April 2001) (Pope & Talbot v Canada); Cargill v Mexico; Bilcon v Canada.*

[9] *Metalclad v Mexico.*

distinction is not important for the focus of this paper we will focus on the treatment of investors.

Paragraph 1 of the TPP national treatment obligation provides:

> Each Party shall accord to investors of another Party treatment no less favourable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory.[10]

The equivalent NAFTA paragraph provides:

> Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.[11]

The structure of the national treatment obligation in both the TPP and NAFTA sets out the three key elements which an investor must prove to establish a breach of national treatment:

1) that the Party has accorded treatment with respect to the establishment, acquisition, … operation, and sale .. of investments;

2) that the investor is *in like circumstances* with comparable domestic investors; and

3) that the Party treats the foreign investor *less favourably* than it treats the relevant domestic investors.[12]

One immediate observation is that while national treatment is generally described as an obligation of non-discrimination, the language of the national treatment article does not explicitly refer to discrimination at all. The language is more qualified, referring to 'less favourable' treatment 'in like circumstances'. Further, less favourable treatment of a foreign investor, as compared to domestic investors, may not breach national treatment where it is not 'in like circumstances'.

While each of the elements of national treatment is important, this paper focuses on the concept of 'like circumstances' as it is this concept which is key in drawing a distinction

[10] *Trans-Pacific Partnership Agreement* (signed 4 February 2016) (*TPP*) art 9.4.1 (footnotes omitted).
[11] NAFTA art 1102.1.
[12] See *Universal Parcel Service of America Inc. v Canada* (*Award on the Merits*), (NAFTA Chapter 11 tribunal, 24 May 2007) (*UPS v Canada*) [83].

between legitimate government regulation on one hand and improper discrimination against investors (amount to a breach of national treatment) on the other.

4. 'Like circumstances'

The approach of NAFTA tribunals confirm that the determination of whether treatment of investors is accorded 'in like circumstances' is a fact-specific exercise. The meaning of 'circumstances' depends on the context and facts of each case.[13] Whether treatment is accorded in 'like circumstances' requires an examination of the surrounding factual situation in its entirety.[14]

Circumstances that have been found by a number of NAFTA tribunals to be particularly relevant in determining whether treatment has been accorded in like circumstances include whether the foreign investor is in the same business or economic sector as a comparable domestic investor[15], and whether foreign and domestic investors are subject to the same legal and regulatory regime.[16]

Of most relevance to the focus of this paper, the concept of 'like circumstances' has generally been interpreted by NAFTA tribunals to mean that *reasonable* differences in treatment of foreign and domestic investors – where these are reasonably or plausibly connected with legitimate (non-discriminatory) policy goals – will not breach national treatment.[17] In this way, the 'like circumstances' concept has acted as a mechanism for tribunals to consider the relevance of legitimate public welfare objectives in determining alleged breaches of national treatment.

While tribunals have characterised the distinction in different ways and the reasoning is not uniform, there is a reasonably consistent thread through the NAFTA awards that differences in the treatment of foreign and domestic investors will not breach national treatment where they are justified by reference to reasonable policy objectives.

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[13] *Apotex Holdings Inc. & Apotex Inc. v United States (Award) (NAFTA Chapter 11 tribunal, 25 August 2014) (Apotex v US) [8.42]; Pope & Talbot v Canada [75]*.
[14] *ADM v Mexico [197]; Pope & Talbot v Canada [75]*.
[15] *SD Myers v Canada [250]; ADM v Mexico [198]; Corn Products v Mexico [120]*.
[16] *Apotex v US [8.42, 8.54]; Grand River Enterprises Six Nations, Ltd., et al. v United States (Award) (NAFTA Chapter 11 tribunal, 12 January 2011) (Grand River v US) [166-167]*.
[17] See *SD Myers v Canada* [250]; *Pope & Talbot v Canada* [79]; *Feldman v Mexico* [170]; *GAMI Investments Inc. v United Mexican States* (Final Award) (NAFTA Chapter 11 tribunal, 15 November 2004) (*GAMI v Mexico*) [114]; *Cargill v Mexico* [206]; *Bilcon v Canada* [723].

In one of the earliest NAFTA cases, *SD Myers v Canada*, the tribunal found that:

> The assessment of "like circumstances" must also take into account circumstances that would justify governmental regulations that treat them differently in order to protect the public interest.[18]

Similarly, in *Pope & Talbot v Canada* the tribunal found:

> focusing on the like circumstances question … will require addressing any difference in treatment, demanding that it be justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments.[19]

The *Feldman v Mexico* tribunal found:

> In the investment context, the concept of discrimination has been defined to imply unreasonable distinctions between foreign and domestic investors in like circumstances[20]

The *GAMI v Mexico* tribunal found:

> The arbitrators are satisfied that a reason exists for the measure which was not itself discriminatory. That measure was plausibly connected with a legitimate goal of policy … and was applied neither in a discriminatory manner nor as a disguised barrier to equal opportunity.[21]

In *Cargill v Mexico*, the tribunal surveyed the approach of earlier NAFTA tribunals and found that:

> in both GAMI and Pope & Talbot, "like circumstances" was determined by reference to the rationale for the measure that was being challenged. It was not a determination of "like circumstances" in the abstract. The distinction between those affected by the measure and those who were not affected by the measure could be understood in light of the rationale for the measure and its policy objective.[22]

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[18] *SD Myers v Canada [250]*.
[19] *Pope & Talbot v Canada [79]*.
[20] *Feldman v Mexico [170]*.
[21] *GAMI v Mexico [114]*.
[22] *Cargill v Mexico [206]*.

Finally, in the recent *Bilcon v Canada* award, the tribunal reviewed the approach taken by previous tribunals to the interpretation of "like circumstances" and found that this approach:

> would seem to provide legally appropriate latitude for host states, even in the absence of an equivalent of Article XX of the GATT, to pursue reasonable and non-discriminatory domestic policy objectives through appropriate measures even when there is an incidental and reasonably unavoidable burden on foreign enterprises.[23]

5. Results of NAFTA cases alleging a breach of national treatment

NAFTA tribunals have recognised the importance of legitimate regulatory objectives in determining whether or not a difference in treatment is "in like circumstances". The next question is whether this approach, and the concept of "like circumstances' – which is at the core of both the NAFTA and TPP national treatment obligations – has been effective in protecting legitimate government regulation? To answer this question it is necessary to examine the relevant cases.

There have been eighteen NAFTA cases were an alleged breach of national treatment has been determined by a tribunal. Of these, tribunals have found a breach of national treatment in six cases.[24]

The early NAFTA case of *SD Myers v Canada*[25] is perhaps the most controversial. The claim arose out of a Canadian ban on the export of PCB waste. PCB is a persistent organic pollutant which is banned and regulated under international environmental conventions. SD Myers, a US company, alleged the export ban violated national treatment. The tribunal upheld the claim finding that it was intended to favour Canadian waste disposal businesses over foreign businesses. The tribunal recognised the legitimate goal underlying the measure (to support and maintain domestic capacity to process PCB) however it found that the ban was not justified by environmental concerns as there were a number of legitimate alternatives (such as subsidies).

Based on the evidence, the *SD Myers* tribunal formed the view that the export ban had a protectionist intent.[26] While the cases always turn on their facts, it is difficult to reconcile

[23] *Bilcon v Canada [723]*.
[24] See n7.
[25] *SD Myers v Canada.*
[26] *SD Myers v Canada [162]*.

this case with the general approach of NAFTA tribunals to interpreting the meaning of 'like circumstances' as it does seem that there was a plausible connection between the export ban and a legitimate public welfare objective despite the availability of potential alternatives to achieve the objective.

Feldman v Mexico[27] was concerned with a Mexican law that provided tax refunds to exporters. The investor owned a local company which exported cigarettes and alleged discrimination as his company had been denied tax rebates which other Mexican exporters had been granted. On the facts available the tribunal upheld this claim.

The next three cases, *ADM v Mexico,*[28] *Corn Products v Mexico,*[29] and *Cargill v Mexico,* [30] involved challenges to the same measure – Mexico's adoption of a tax on beverages sweetened high fructose corn syrup (HFCS). The tax applied only to beverages sweetened with HCFS and not beverages sweetened with sugar. The HCFS industry was controlled by US investors and the sugar industry was primarily controlled by domestic investors. In each of these cases the tribunal found that the tax was intended to protect the domestic sugar industry and to damage the US producers and suppliers of HFCS. The tribunals found that the tax was intended to put pressure on the US in the context of a broader dispute related to sugar.

Each of *Feldman* and the three corn syrup cases were decided on the basis of the facts before the tribunal, and it is not possible to examine them in detail in this paper. However at a high level, it is understandable how a tribunal could have reached a finding of a breach of national treatment in each of these cases and they do not seem inconsistent with the principle that reasonable differences in treatment of foreign investors – where these are plausibly connected with legitimate policy goals – will not breach national treatment.

In the recent *Bilcon v Canada*[31] case, the dispute concerned a proposed quarry and marine terminal in Nova Scotia which – after an extensive environmental assessment ('EA') process – was ultimately denied. The investor claimed that it had been treated less favourably than

[27] *Feldman v Mexico.*
[28] *ADM v Mexico.*
[29] *Corn Products v Mexico.*
[30] *Cargill v Mexico.*
[31] *Bilcon v Canada*

comparable domestic investors in the EA process. A majority upheld the claim, finding that the process for Bilcon had failed to meet the standard required under Canadian law – in particular the requirement to consider the potential to mitigate adverse effects of the project – in contrast to comparable domestic investors. The tribunal did not explicitly consider whether the different treatment was based on nationality, however it did examine a number of Canadian projects which it considered sufficiently similar for the purposes of national treatment and found they had been treated more favourably (in like circumstances).[32] The tribunal also found that there was no justification for the less favourable treatment accorded to *Bilcon*.[33] In a controversial finding, the tribunal held that after the claimant had established that it had been accorded less favourable treatment in like circumstances, the burden shifted to the respondent (Canada) to establish that the measure was nonetheless not inconsistent with national treatment (because the treatment was justified as the measure was in pursuance of reasonable and non-discriminatory policy objectives).[34]

Bilcon has generated significant controversy, partly due to a strong dissent by one of the arbitrators and criticism of the decision by the NAFTA parties. The main source of the controversy was the finding on the minimum standard of treatment, however the tribunal's approach to interpreting the national treatment obligation has also drawn criticism. In submissions to the tribunal in the *Mesa Power v Canada* case, each of the NAFTA parties criticised the *Bilcon* tribunal's approach to interpreting national treatment. The US and Canada criticised the tribunal's approach on two primary grounds: (i) that national treatment protects only against *nationality-based* discrimination and the tribunal's approach to interpreting 'like circumstances' was not consistent with this; and (ii) that the tribunal improperly shifted the burden of proof to the respondent to establish that the less favourable treatment of the investor was justified. Mexico only raised the latter of these points in its submission to the *Mesa* tribunal, however it has previously argued that national treatment protects only against nationality-based discrimination, and this is the consistent interpretation of all three NAFTA parties.[35] As discussed later in this paper, both of these concerns are addressed in the approach to national treatment in the TPP.

[32] Ibid [694-696].
[33] Ibid [724].
[34] Ibid [723].
[35] See *In the Matter of an Arbitration under Chapter Eleven of the NAFTA Between: Mesa Power Group, LLC and Government of Canada*: *Government of Canada Observations on the Award on Jurisdiction and Merits* in *William Ralph Clayton, William Richard Clayton, Douglas Clayton, Daniel Clayton and Bilcon of Delaware, Inc. v. Canada* (May 14, 2015); *In the Arbitration under Chapter Eleven of the NAFTA: Mesa Power Group,*

6. National treatment and nationality-based discrimination

The consistent interpretation of the parties to NAFTA is that national treatment protects only against nationality-based discrimination.[36] Some NAFTA tribunals have explicitly characterised national treatment as prohibiting only *nationality-based* discrimination.[37] Others have not been so explicit, and at least one case has rejected an argument that national treatment is limited to nationality-based discrimination.[38] This leads to the question: what does nationality-based discrimination mean in the national treatment context?

In *Pope & Talbot v Canada* the tribunal rejected the argument that national treatment was limited to discrimination on the basis of nationality. However this appears to have been based on a view that this would mean national treatment was limited to measures which were discriminatory on their face (de jure) and would exclude de facto national treatment claims:

> the Tribunal believes that the approach proposed by the NAFTA Parties [that National Treatment prohibits treatment that discriminates on the basis of the foreign investment's nationality] would tend to excuse discrimination that is not facially directed at foreign owned investments.[39]

In this regard the NAFTA awards are consistent in finding that national treatment covers both de jure and de facto discrimination.[40] However, the NAFTA parties and other tribunals have not characterised nationality-based discrimination in the national treatment context as being limited to de jure discrimination. Rather, they have focused on the reasonableness of any less favourable treatment accorded to foreign investors, taking into account all of the relevant circumstances. The *ADM v Mexico* tribunal characterised it as follows:

LLC and Government of Canada: *Second Submission of Mexico Pursuant to NAFTA Article 1128* (12 June 2015); *In the Arbitration under Chapter Eleven of the NAFTA: Mesa Power Group, LLC and Government of Canada*: *Second Submission of the United States* (12 June 2015).

[36] See above n 35.

[37] *ADM v Mexico* [193, 205]; see also *Loewen Group, Inc. and Raymond L. Loewen v. United States of America (Award)* (NAFTA Chapter 11 tribunal, 26 June 2003) [139]*;* (less explicitly) *Apotex v US* [8.56].

[38] The tribunal in *Pope & Talbot* rejected the argument that national treatment was limited to discrimination on the basis of nationality. However this appears to have been based on a belief that this interpretation would mean national treatment was limited to measures which were discriminatory on their face (de jure). See *Pope & Talbot v Canada* [79].

[39] *Pope & Talbot v Canada* [79].

[40] See *SD Myers v Canada* [252]; *Feldman v Mexico* [166]; *ADM v Mexico* [196]; *Corn Products v Mexico* [140].

> Article 1102 prohibits treatment which discriminates on the basis of the foreign investor's nationality. Nationality discrimination is established by showing that a foreign investor has unreasonably been treated less favorably than domestic investors in like circumstances.[41]

In other words, nationality-based discrimination will be established where there is less favourable treatment of a foreign investor which is like a comparable domestic investor in all relevant respects and there is no reasonable justification for that difference. If there is no other reasonable justification for the different treatment, then it will be deemed to be based on nationality. Characterised this way, the general approach of NAFTA tribunals (outlined above) could be seen as being consistent with the scope of national treatment being limited to nationality-based discrimination.

After rejecting the argument that national treatment is limited to nationality-based discrimination (as it understood the principle) the tribunal in *Pope & Talbot* found that:

> A formulation focusing on the like circumstances question, on the other hand, will require addressing *any* difference in treatment, demanding that it be justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments. That is, once a difference in treatment between a domestic and a foreign-owned investment *is* discerned, the question becomes, are they in like circumstances? It is in answering that question that the issue of discrimination may arise.[42]

This approach is consistent with national treatment being limited to nationality-based discrimination in the manner characterised by the *ADM* tribunal. For the purposes of this paper, the primary importance of this is that a difference in treatment which is justified by a legitimate policy objective or rationale would not amount to nationality-based discrimination and therefore would not be in breach of national treatment.

[41] *ADM v Mexico* [193, 205].
[42] *Pope & Talbot v Canada* [79].

7. TPP approach to National Treatment

As outlined above, the text of the national treatment obligation in the TPP is almost identical to the equivalent NAFTA obligation. However the TPP text includes two additional elements: a footnote which elaborates on the meaning of 'like circumstances' (the 'Footnote'); and a Drafters' Note on Interpretation of 'In Like Circumstances' (the 'Drafters' Note'). Together, these can be seen as a response by the TPP parties to the concerns raised in some of the NAFTA national treatment cases, in particular *SD Myers, Pope & Talbot* and *Bilcon*. In the context of this paper, these additional elements increase the parties' certainty that appropriate consideration will be given to any relevant legitimate public welfare objectives in determining whether treatment is 'in like circumstances'.

The Footnote, which appears in both the national treatment and Most-Favoured-Nation Treatment Articles, provides:

> For greater certainty, whether treatment is accorded in "like circumstances" under Article 9.4 (National Treatment) or Article 9.5 (Most-Favoured-Nation Treatment) depends on the totality of the circumstances, including whether the relevant treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives.

The Drafters' Note is not part of the TPP treaty itself but has been published in association with the text of the treaty.[43] The Drafters' Note confirms the shared intent of the TPP Parties that tribunals follow a certain approach in interpreting the concept of 'like circumstances'. It refers to the approach of a number of NAFTA tribunals and key principles for the interpretation of 'like circumstances'. For the purposes of this paper the key elements are:

- the claimant bears the burden to prove that the respondent failed to accord to the claimant treatment no less favourable than it accords, in like circumstances, to its own investors;

- national treatment does not prohibit all measures that result in differential treatment but rather measures that treat investors less favourably on the basis of their nationality;

[43] *Drafters' Note on Interpretation of "In Like Circumstances" Under Article 9.4 (National Treatment) and Article 9.5 (Most-Favoured-Nation Treatment).*
<https://tpp.mfat.govt.nz/assets/docs/Interpretation%20of%20In%20Like%20Circumstances.pdf>

- examination of whether treatment is 'in like circumstances' is a fact-specific inquiry requiring consideration of the totality of the circumstances including competition in the relevant business or economic sectors, the applicable legal and regulatory frameworks, and whether the differential treatment is based on legitimate public welfare objectives;

- NAFTA tribunals have held that investors or investments that are 'in like circumstances' based on the totality of the circumstances have been discriminated against based on their nationality; and

- NAFTA tribunals have accepted distinctions in treatment between investors or investments that are plausibly connected to legitimate public welfare objectives.

8. What is the status of the Drafters' Note?

The Drafters' Note is not a part of the treaty text. Rather it is an instrument associated with the treaty. Henckels, while welcoming the additional clarity resulting from the Drafters' Note, observed that its legal significance is not clear.[44] This paper seeks to further explore the legal significance of the Drafters' Note.

While not part of the treaty text, the Drafters' Note is part of the context of the treaty, and in particular, the context of the national treatment obligation. In accordance with the general rule of treaty interpretation, as reflected in Article 31 of *Vienna Convention on the Law of Treaties* (Vienna Convention)[45] the terms of a treaty must be interpreted in accordance with their ordinary meaning in their context. Article 31(2) of the Vienna Convention sets out what comprises the context for the purposes of interpreting a treaty. This includes, as set out in sub-paragraph (a) of Article 31(2) 'any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty'.[46] In the author's view the Drafters' Note falls within this category of instruments. The Drafters' Note was made between all of the TPP Parties in connection with the conclusion of the treaty. An 'agreement' referred to in Article 31(2)(a) does not need to be a treaty in itself and in this regard the term 'agreement' is used in contrast to 'treaty' in the Vienna Convention. Aust

[44] Caroline Henckels, '*Protecting regulatory autonomy through greater precision in investment treaties: the TPP, CETA and TTIP*' (2016) [17-18] <http://ssrn.com/abstract=2721523>.
[45] *Vienna Convention on the Law of Treaties* (1969) (*Vienna Convention*).
[46] Vienna Convention, art 31(2)(a).

notes that what is important is that the agreement is a clear expression of the intention of the parties[47] and the Drafters' Note unambiguously expresses the intention of the TPP parties in relation to how the national treatment obligation should be interpreted.

Proceeding on the basis that the Drafters' Note is part of the context of the national treatment obligation, it follows that the national treatment obligation, including the like circumstances Footnote, must be interpreted by reference to, and consistently with, the approach set out in the Drafters' Note.

As a matter of practice, in the event of an ISDS dispute it would be reasonable to expect a respondent government to argue that the national treatment obligation must be interpreted consistently with the Drafters' Note. Beyond this, there are a couple of mechanisms available to the TPP parties to seek to ensure that tribunals interpret the national treatment obligation consistently with the Drafters' Note. First, in the event of an ISDS dispute, all non-disputing Parties have the ability to make a submission to a tribunal on the interpretation of the agreement, including the proper interpretation of the national treatment obligation.[48] Second, if the parties have concerns that tribunals were failing to interpret national treatment consistently with their intention as set out in the Drafters' Note they could issue a joint interpretation of national treatment which reflected the same approach. Under Article 9.25.3 of the Investment Chapter, this interpretation would then be binding on any tribunal interpreting national treatment.[49]

9. What are the implications of the Footnote and Drafters' Note?

As Henckels notes, the TPP Footnote and the Drafters' Note set out the Parties' intentions with respect to the interpretation of 'like circumstances' with far greater clarity than other agreements.[50] In doing so, they expressly direct tribunals to approach the interpretation of the national treatment obligation, and in particular, the concept of like circumstances, in a manner which recognises the importance of legitimate public welfare objectives. We will now examine the impact of the Footnote and Drafters' Note in more detail.

[47] Anthony Aust, *Modern Treaty Law and Practice* (Cambridge University Press, 2nd ed, 2007) [236].
[48] TPP art 9.23.2.
[49] TPP art 9.25.3.
[50] Caroline Henckels, n44 [18].

Implications of the Footnote

As extracted above, the Footnote to the national treatment Article provides:

> For greater certainty, whether treatment is accorded in "like circumstances" … depends on the totality of the circumstances, including whether the relevant treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives.

In broad terms, the Footnote reflects the general approach of NAFTA tribunals in interpreting the concept of 'like circumstances'. Even if this was its only function there would be value in this approach. It would be reasonable to expect TPP tribunals to take a consistent approach to the majority of NAFTA tribunals when interpreting the same concept, however setting out this elaboration of like circumstances explicitly in the treaty text delivers a greater degree of certainty for the Parties. It addresses the concern raised by the finding in the *SD Myers* case – that the tribunal did not give due weight to the relevance of legitimate public welfare objectives.

In the author's view there is an additional benefit associated with the Footnote. While recognising that the determination of 'like circumstances' depends on the totality of the circumstances, it refers specifically to just one of these circumstances, 'whether the relevant treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives'. As such, the Parties have highlighted the importance of this factor and ensure that any tribunal *must* consider whether the treatment does distinguish between investors on the basis of legitimate public welfare objectives. The Footnote does not explicitly state the result if the answer to this question is positive, however when interpreted in the context of the Drafters' Note (discussed further below), it would support a conclusion that the treatment did not amount to a breach of national treatment.

Implications of the Drafters' Note

As outlined above, the Drafters' Note elaborates in some detail how the concept of 'in like circumstances' should be interpreted. It directly addresses concerns that have been raised by the cases of *SD Myers*; *Pope & Talbot* and most recently, *Bilcon*. It expressly confirms the shared intent of the TPP parties, that tribunals interpreting 'like circumstances' follow the approach as set out in the Footnote and Drafters' Note. In doing so it delivers greater

certainty to the parties that tribunals will give appropriate consideration to the relevance of legitimate regulatory objectives in determining whether treatment is in 'like circumstances'.

First, the Drafters' Note confirms that the burden in establishing each of the elements of national treatment rests with the claimant. This responds to the *Bilcon* tribunal's finding that the respondent government bears the burden of establishing a measure found to be *prima facie* inconsistent with national treatment was nonetheless justified by reference to legitimate policy objectives.

Second, the Drafters' Note confirms that national treatment prohibits measures that treat investors less favourably on the *basis of their nationality*. This element responds to concerns raised by the *SD Myers* case and also the concerns of the NAFTA parties that the *Bilcon* tribunal failed to interpret national treatment in this way. If a difference in treatment is reasonably justified by reference to a legitimate policy rationale then it is not a difference on the basis of nationality.

Third, the Drafters' Note states that NAFTA tribunals have accepted distinctions in treatment between investors or investments that are plausibly connected to legitimate public welfare objectives and states the intention of the parties that any TPP tribunal follows this approach. Stating that NAFTA tribunals have *accepted* such distinctions, in context, must mean that distinctions 'plausibly connected to legitimate public welfare objectives' have not been found to be 'in like circumstances' and therefore not in breach of national treatment. This is supported by the extracts of NAFTA cases referred to in the Drafters' Note, in particular *GAMI*[51] and *Pope & Talbot*.[52] This aspect of the Drafters' Note is particularly useful as context for interpreting the Footnote in relation to protecting legitimate government regulation. It supports an argument that treatment which 'distinguishes … on the basis of legitimate public welfare objectives', as the Footnote provides, would not be less favourable treatment 'in like circumstances' and therefore not in breach of national treatment.

The language of the Drafters' Note: 'distinctions *plausibly connected* to legitimate public welfare objectives' is broader than the language in the Footnote which refers to distinctions '*on the basis* of legitimate public welfare objectives'. As part of the context, the Drafters' Note informs the interpretation of the Footnote including the strength of the relationship or connection between any difference in treatment and legitimate public welfare objectives. If

[51] *GAMI v Mexico* [111-115].
[52] *Pope & Talbot v Canada* [78-79].

differences in treatment which are 'plausibly connected' to legitimate public welfare objectives have been found not in breach of national treatment, then differences which are 'based on' the same objectives would be less likely to be so.

In contrast to the Footnote which refers only to legitimate public welfare objectives, the Drafters' Note enumerates a broader range of factors which have been found by tribunals to be part of the 'totality of circumstances' relevant to whether treatment is 'in like circumstances'. These include competition in the relevant business or economic sectors, and the applicable legal and regulatory frameworks. This confirms that there are a range of reasons why investors or investments may or may not be 'in like circumstances' and that it will always be a fact-specific question. In the author's view this broader reference in the Drafters' Note does not detract from the prominence given to the role of legitimate public welfare objectives in the Footnote but simply reflects certain circumstances factors which have been identified as being important by previous tribunals.

10. Conclusion

The TPP national treatment obligation owes much to the equivalent NAFTA obligation, in particular the concept of 'like circumstances'. The approach of NAFTA tribunals has in general (although not uniformly) supported an interpretation of 'like circumstances' which recognises that different treatment of a foreign investor will not be in breach of national treatment where the difference is plausibly or reasonably connected with legitimate policy objectives. Some NAFTA tribunals have found that discrimination in the national treatment context is limited to discrimination based on nationality. Other NAFTA tribunals have not explicitly recognised this principle, and one has rejected it. However, if nationality-based discrimination is characterised as being established where a foreign investor has unreasonably been treated less favourably than domestic investors in all relevant (like) circumstances, then the general approach of NAFTA tribunals is consistent with this. The importance of this principle from the perspective of safeguarding regulatory autonomy is that a difference in treatment which is based on, or plausibly connected with, legitimate public welfare objectives, would not be unreasonable, and therefore not in breach of national treatment. The TPP national treatment obligation responds to the concerns raised in some of the NAFTA cases. Through the Footnote and Drafters' Note, the TPP elaborates on the approach to interpreting the concept of 'like circumstances' and clearly expresses the

intention of the Parties that any tribunal must follow this approach. In doing so, the TPP delivers greater certainty to the parties and ensures that tribunals give appropriate consideration to the relevance of legitimate public welfare objectives in determining an alleged breach of national treatment.