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Secret TPP Investment Chapter Unveiled: It's Worse than We Thought

Analysis of Specific TPP Investment Provisions and Their Threats to the Public Interest: Scope of ISDS Challenges Expanded, Promised Procedural Reforms Absent

After nearly six years of Trans-Pacific Partnership (TPP) negotiations under conditions of extreme secrecy, the Obama administration has only now released the text after it has been finalized and it is too late to make any needed changes. The final TPP investment chapter provides stark warnings about the dangers of "trade" negotiations occurring without press, public or policymaker oversight. The TPP would elevate individual foreign corporations to equal status with the 12 sovereign governments signing the deal text. It would empower foreign firms to privately enforce new foreign investor rights set forth in the pact by directly "suing" signatory governments in extrajudicial investor-state dispute settlement (ISDS) tribunals over domestic policies that have withstood domestic court review and that apply equally to domestic and foreign firms. Before tribunals comprised of three private sector attorneys, foreign firms and the foreign subsidiaries of U.S. firms could demand U.S. taxpayer compensation for domestic financial, health, environmental, land use and other policies and government actions they claim undermine their new TPP privileges, such as the "right" to a regulatory framework that conforms to the "expectations" they had when they established their investment.

- **Contrary to administration claims that the TPP's investment chapter would somehow limit the uses and abuses of the controversial investor-state dispute settlement regime, much of the text replicates, often word-for-word, the most provocative terms found in past U.S. ISDS-enforced agreements.** Indeed, many fixes and safeguards that were included in a 2012 leaked version of the draft TPP Investment Chapter text have been eliminated.

- **Contrary to Fast Track negotiating objectives, the TPP would grant foreign firms greater rights that domestic firms enjoy under U.S. law and in U.S. courts.** One class of interests – foreign firms – could **skirt U.S. domestic laws and courts** to challenge U.S. federal, state and local decisions and policies on grounds not available in U.S. law and do so before extrajudicial tribunals authorized to order payment of unlimited sums of taxpayer dollars. Such compensation orders could include the "expected future profits" a tribunal surmises that an investor would have earned in the absence of the public policy it is attacking.

- **The TPP would expand U.S. ISDS liability by widening the scope of domestic policies and government actions that could be challenged**. ***<u>For the first time in any U.S. free trade pact</u>*:**

  - **The provision used in most successful investor compensation demands would be extended to challenges of financial regulatory policies.** The TPP would extend the "minimum standard of treatment" obligation to the TPP Financial Services Chapter's terms, allowing financial firms to challenge policies as violating investors' "expectations" of how they should be treated. The "safeguard" that the U.S. Trade Representative (USTR) claims would protect such policies repeats an ambiguously written World Trade Organization (WTO) provision that has not been accorded significant deference in the past.

- **Pharmaceutical firms could use the TPP to demand cash compensation for claimed violations of WTO rules on creation, limitation or revocation of intellectual property rights**. Currently, WTO rules are not privately enforceable by investors.

- **With Japanese, Australian and other firms newly empowered to launch ISDS attacks against the United States, the TPP would *double* U.S. ISDS exposure. More than 1,000 additional corporations in TPP nations, which own more than 9,200 subsidiaries here, could newly launch ISDS cases against the U.S. government.** About 1,300 foreign firms with about 9,500 U.S. subsidiaries are so empowered under ALL existing U.S. investor-state-enforced pacts. Most of these are with developing nations with few investors here. (That is why until the TPP the United States has managed largely to dodge ISDS attacks to date.) The TPP would subject U.S. policies and taxpayers to an unprecedented increase in ISDS liability at a time when the types of policies being attacked and the number of ISDS case are surging. Just 50 known ISDS cases were launched in the regime's first three decades combined while about 50 claims were launched in *each* of the last four years.

- **The TPP also would newly empower more than 5,000 U.S. corporations to launch ISDS cases against other signatory governments on behalf of their more than 19,000 subsidiaries in those countries.** (These are firms not already directly covered by an ISDS-enforced pact between the United States and other TPP governments.)

- **U.S. negotiators succeeded in pressuring other TPP nations to empower foreign investors to bring certain sensitive contract disputes with TPP signatory governments to ISDS tribunals, instead of resolving such matters in domestic courts.** This includes disputes with the federal government about natural resource concessions, government procurement projects for construction of infrastructure projects and contracts relating to the operation of utilities.

- **TPP ISDS tribunals would not meet standards of transparency, consistency or due process common to TPP countries' domestic legal systems or provide fair, independent or balanced venues for resolving disputes**. (Section B) ***Contrary to claims that the process was "reformed":***

  - **TPP tribunals would still be staffed by three private sector attorneys that would be allowed to rotate between acting as "judges" and as advocates for investors** launching cases. Such dual roles would be deemed unethical in most legal systems.

  - **The TPP text has no requirement for tribunalists to be independent or impartial.** Rather, the text relies on the existing, weak impartiality rules set by the arbitration venues themselves.

  - **The text does not include new conflict of interest rules for tribunalists.** TPP negotiators punted a so-called "Code of Conduct" for ISDS arbitrators to a side agreement to be created and put in place by the TPP countries before the pact goes into effect (Article 9.21.6), *which at the soonest would be two years after it is signed*. Whether such rules will be effective with respect to tribunalists' direct conflicts of interest is an open question. It seems improbable that Congress and the public will get to evaluate the rules and how enforceable they will be before votes to approve the pact. However, even if the Code of Conduct were to stop the outrageous practice of lawyers with direct financial interests in the companies and issues involved being allowed to serve as "judges," the TPP text does not address the bias inherent in the ISDS system and underlying the business model of lawyers engaged in this field: ISDS tribunalists have a structural incentive to concoct fanciful interpretations of foreign investors' rights and order compensation to increase the number of investors interested in launching new cases and enhance the likelihood of being selected for future tribunals.

  - **There is no system of outside appeal on the merits of a decision. Nor is an appellate body established within the TPP to constrain the enormous discretion on the merits and amounts of compensation**. The text retains full discretion for the tribunal to determine how much a government must pay the firm in taxpayer funds. This can include claims for the "expected future profits" the tribunal surmises would have earned in the absence of the public policy under attack. ISDS tribunals have ordered more than $3.5 billion in compensation under existing U.S. pacts alone for toxics bans, land-use policies, financial stability measures, forestry rules, water services, economic development policies, mining restrictions and more. More than $34 billion remain in pending claims under U.S. pacts.

  - **Even when governments win, under TPP rules they can be ordered to pay for the tribunal's costs and legal fees, which average $8 million per case.**

  - **The provisions on expedited dismissal of "frivolous" cases replicate the language included in U.S. pacts since the George W. Bush administration with respect to the speed at which such claims must be heard and tribunals' authority to order claimants to pay costs if a case is dismissed.** The only new provision makes explicit a factor (that a claim is "manifestly without legal merit") that is inherent in the underlying standard for expedited dismissal that is included in past U.S. pacts and the TPP: that "a claim submitted is not a claim for which an award in favour of the claimant may be made…"

- **TPP does not include the promised "reforms" of the substantive foreign investor rights underlying egregious past rulings.**

  - **The TPP retains the "Minimum Standard of Treatment" and "Indirect Expropriation" language from past U.S. pacts that grants foreign investors "rights"** to not have expectations frustrated by a change in government policy. Under the TPP, it does not matter if the changed policy came in response to a new financial crisis or health discovery or environmental catastrophe, *or if it applies to domestic and foreign firms alike.*

  - **There are no new safeguards that limit ISDS tribunals' discretion to issue ever-expanding interpretations of governments' obligations to investors and order compensation on that basis.** The text reveals virtually identical "limiting" annexes and terms that were included in U.S. pacts since the 2005 Central America Free Trade Agreement (CAFTA) that have failed to rein in ISDS tribunals. CAFTA tribunals have simply ignored these provisions now replicated in the TPP. As with past pacts, in the TPP such tribunal conduct is not subject to appeal.

  - **The TPP includes an overreaching definition of "investment" that would extend the coverage of the TPP's expansive substantive investor rights far beyond "real property," permitting ISDS attacks over government actions and policies related to financial instruments, intellectual property, regulatory permits and more.** Proposals to narrow the definition of "investment," and thus the scope of policies subject to challenge, that were included in an earlier version of the text that leaked have been eliminated.

- **The lack of robust "denial of benefits" provisions would allow firms from non-TPP countries and firms with no real investments to exploit the extraordinary TPP ISDS privileges.** This includes firms from non-TPP countries that have been incorporated in a TPP signatory country. Thus, for instance, one of the many Chinese state-owned corporations in Vietnam and Malaysia (that also have U.S. investments), could "sue" the U.S. government under this text. Language limiting investors to those that have "substantial business activities" is not defined, and tribunals have been willing to consider very minimal investments in host states as conferring nationality for the sake of gaining treaty protections.

- **Proposals to extend even the TPP's weak general exceptions for environmental and health policies to the Investment Chapter were rejected**. Instead of real safeguards to stop attacks on countries' environmental, health and other regulatory objectives, the TPP text reveals that the same self-cancelling provision included in past U.S. pacts is replicated, although with more types of policies listed. The construct of the provision, which limits the rule of construction to only environmental and other policies that already are consistent with the agreement makes the measure meaningless – a safeguard is only needed to protect policies that would otherwise violate the agreement's rules. The relevant provision (Article 9.15) reads "Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure **otherwise consistent** with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental, health or other regulatory objectives." (emphasis added)

- **The final TPP text even eliminates some limited safeguards included in an earlier leaked version that would have protected certain public interest policies in several TPP countries from ISDS challenges.** These include Canada's policies to promote Canadian culture, Malaysia's government procurement measures (after three years of the TPP going into effect), and Australia's public health policies to ensure access to affordable medicines. With the deletion of these safeguards in the final TPP text, foreign firms would be free to ask extrajudicial tribunals to order government compensation for these sensitive policies.

- **The only meaningful new ISDS safeguard included in the final TPP text is a carve-out for tobacco-related public health measures that allows countries to elect to remove such policies from being subject to ISDS challenges, either in advance or once a policy is attacked**. Leading health groups, pro-free-trade former New York City mayor Michael Bloomberg and TPP countries like Malaysia had pushed for years for even more expansive provisions. These proposals would have prevented all TPP challenges to tobacco-related health policies, including those brought by other governments and would have excluded tariff cuts on unprocessed tobacco and tobacco products that would result in the TPP lowering the price of cigarettes. The final tobacco provision makes clear that government-to-government challenges to tobacco control measures are allowed as is tariff elimination on tobacco and tobacco products. But even with these unfortunate limitations, the final provision is considerably better than past ISDS tobacco control exception proposals. It provides an example of how a meaningful trade pact safeguard against ISDS attacks could be structured. That said, because the TPP's Investment Chapter includes a Most Favored Nations provision, a tobacco company could demand the better investor rights provided in other ISDS-enforced investment agreements the regulating country has enacted. (Indeed, the TPP tobacco language was motivated in part by various subsidiaries of Phillip Morris using the ISDS clauses of various countries' ISDS-enforced agreements to attack Australian and Uruguayan tobacco control policies.) However, even with those not insignificant caveats, this real carve-out from ISDS liability for various forms of health-related tobacco control policies makes apparent how ineffective and meaningless the chapter's language advertised by the White House as protecting other health policies and the environment actually is (Article 9.15). The tobacco provision also begs the question why only tobacco control policies are excluded from ISDS attacks, given no other provision of the Investment Chapter nor the TPP's General Exceptions Chapter provides any meaningful safeguard or effective exception to stop ISDS attacks on other public health measures, from toxins bans to patent policies to pollution cleanup requirements. (For more on the TPP's tobacco-related provisions, see the text analysis from Action on Smoking and Health.)

The TPP's expansion of the ISDS regime would come amid a surge in ISDS cases against public interest policies. Rather than being an option of last resort, corporations' use of ISDS is surging, with an ever-expanding range of policies and government actions coming under attack, with few claims involving actual expropriation. While treaties with ISDS provisions have existed since the 1960s, just 50 known cases were launched in the regime's first three decades combined. In contrast, foreign investors launched at least 50 ISDS claims *each year* from 2011 through 2013, and another 42 claims in 2014. The ostensible goal of the ISDS system was to provide foreign investors a means to obtain compensation if a government expropriated their factory or land and the domestic court system did not provide for compensation. Over time, both the rules and their interpretation have been dramatically expanded – a problem that the final TPP shows the TPP would exacerbate.

Foreign corporations have used these claims to attack tobacco, climate, financial, mining, medicine, energy, pollution, water, labor, toxins, development and other non-trade domestic policies. Under U.S. "free trade" agreements (FTAs) alone, foreign firms have already pocketed more than $440 million in taxpayer money via investor-state cases. This includes cases against natural resource policies, environmental protections, health and safety measures, economic development policies and more. ISDS tribunals have ordered more than $3.6 billion in compensation to investors under all U.S. FTAs and Bilateral Investment Treaties (BITs). More than $34 billion remains in pending ISDS claims under these pacts, nearly all of which relate to environmental, energy, financial regulation, public health, land use and transportation policies. Even when governments win cases, they are often ordered to pay for a share of the tribunal's costs. Given that the costs just for defending a challenged policy in an ISDS case total $8 million on average, the mere filing of a case can create a chilling effect on government policymaking, even if the government expects to win.

Detailed Textual Analysis

This analysis of the released TPP investment text provides a guided tour of this chapter's many provisions that literally replicate the terms of past U.S. agreements. This includes language providing foreign investors various substantive and procedural rights that extend beyond those provided to domestic firms under domestic law, and the same "safeguard" language that has failed to function effectively in past pacts. This analysis also spotlights differences between earlier leaked versions of this chapter (from 2012 and 2015) and this final text, including the elimination of various reform and safeguard proposals found in the earlier versions.

TPP Text Establishes Procedural Rights Available Only to Foreign Investors

- **Foreign investors alone would be granted access to extrajudicial tribunals staffed by private sector lawyers who rotate between acting as "judges" and representing corporations in cases against governments, posing major conflicts of interest.** The text includes provisions that submit

TPP signatory countries to the jurisdiction of World Bank and United Nations arbitral tribunals. These tribunals, staffed by private sector attorneys (Article 9.21), are empowered to order governments to pay investors compensation for what the attorneys deem to be violations of the TPP's investor rights. The tribunals lack public accountability and standard judicial ethics rules. The lawyers rotate between roles as "judges" in disputes brought by investors against governments, and as advocates for investors against governments, in a manner that would be deemed unethical for judges in most domestic legal systems.

The TPP text itself has no requirement for tribunalists to be independent or impartial and instead refers to weak impartiality rules set by the arbitration venues themselves. In the 48-year history of the World Bank arbitration regime, which is most commonly used, tribunalists have only been disqualified in four of 41 challenges of exhibited bias or conflicts of interest. Rulings by tribunalists with specific conflicts of interest have been allowed to stand. A tribunalist ruling that Argentina had to pay Vivendi Universal $105 million for reversing a failed water privatization served on the board of a bank that was an investor in Vivendi. The tribunalist did not disclose the conflict, much less recuse herself, but Argentina's effort to annul the ruling was dismissed. While the text promises that a Code of Conduct for investment arbitrators will be released before the TPP goes into effect (Article 9.21.6), the final TPP text does not give the public or Congress any enforceable reform commitments to compare against domestic best practices.

However, a deeper conflict of interest is inherent in the "business model" underlying the ISDS system. The corporation initiating a case chooses the venue and selects one of the "judges". The defending government chooses another, and those two select the third (Article 9.21). Since only foreign investors can launch cases and also select one of the tribunalists, ISDS tribunalists have a structural incentive to concoct fanciful interpretations of investors' rights and order that they be compensated for breaches of obligations to which governments never agreed. Lawyers that do so while serving as a tribunalist in one ISDS case can increase the number of investors interested in launching new cases and enhance the chance investors will select him or her for future tribunals.

There are no requirements to follow precedent. And, there is no right of appeal on the merits of a decision. Under the World Bank rules, governments can turn to another tribunal of three private sector attorneys to seek annulment of a ruling for limited procedural errors. But annulments are extremely rare. The final TPP text, like past U.S. FTAs, includes no meaningful internal appeals mechanism for ISDS rulings. And the text provides for no additional rights of appeal to an outside court or other body. It only includes a reference to the possibility that one day such an appeals mechanism could be created "under other institutional arrangements" (Article 9.22.11). But the final TPP text is even weaker on this front than the investment chapters of existing FTAs, which state that were an ISDS appellate body to be created one day by the signatory governments, the governments "shall strive to reach an agreement that would have such appellate body review awards." The TPP text only states that, in the hypothetical scenario that such an appellate mechanism would someday be created by some unnamed party, the signatory governments "shall consider whether awards … should be subject to that appellate mechanism" (Article 9.22.11).

- **Foreign tribunals would be empowered to order governments to pay unlimited cash compensation out of national treasuries**. The text provides tribunals with discretion to determine the amount of compensation governments must pay investors (Article 9.28.1) and also the allocation of costs (Article 9.28.3), such as the tribunalists' fees. Even when governments win ISDS cases, they waste scarce budgetary resources defending national policies against these corporate attacks, as $8 million in taxpayer funds must be used in an average ISDS case to pay large hourly fees for the tribunals and legal costs. An earlier leaked version of the TPP Investment Chapter included a proposed provision to standardize hourly fees for tribunalists at the lower end of the range of fees currently paid (about $375 per hour, compared to the $700 per hour that some tribunalists receive). But that restriction on tribunalist fees has been scrapped in the final text.

- **An overreaching definition of "investment" has been agreed by all parties that would extend the coverage of the TPP's expansive substantive investor rights far beyond "real property," permitting ISDS attacks over government actions and policies related to financial instruments, intellectual property, regulatory permits and more.** The definition of "investment" in the text is: "every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk" (Article 9.1). The text goes on to enumerate as examples: regulatory permits; intellectual property rights; financial instruments such as stocks and derivatives; "construction, management, production, concession, revenue-sharing, and other similar contracts;" and "licenses, authorizations, permits, and similar rights conferred pursuant to domestic law."

  The chapter's new rights and protections would extend to investments already existing before the TPP. It would permit compensation claims even over failed attempts to make an investment, with the low standard to qualify for attempting to invest being "concrete action or actions to make an investment, such as channeling resources or capital in order to set up a business, or applying for a permit or license." The expansive definitions allow attacks on a vast array of non-discriminatory domestic policies and government actions from health and land use policies to construction permits and financial regulation. Proposals in a 2012 leaked version that would have banned ISDS attacks related to government procurement, subsidies or government grants were struck from the final text.

- **Under pressure from U.S. negotiators, the final text expands the scope of matters that are subject to investor-state enforcement to also include government contracts with foreign investors for natural resource concessions, construction projects and more**. The final TPP text gives foreign investors greater rights than domestic investors with respect to disputes relating to procurement contracts with the signatory governments, contracts for natural resource concessions on land controlled by the national government and contracts to operate utilities (Articles 9.1 and 9.18(1)(a)(i)(C)). The U.S. government pushed for the TPP to establish a right for foreign investors to bring disputes over such contracts to ISDS tribunals rather than domestic courts despite years of strong opposition from other TPP countries, which apparently caved to the U.S. demands. As a result, the TPP would allow disputes over such contract matters between foreign firms and governments to be resolved in ISDS tribunals rather than requiring foreign firms to use the same domestic laws and courts to which domestic firms could bring such disputes.

  Specifically, ISDS enforcement would be extended to cover "written agreement[s]... between an authority at the central level of government of a Party and a covered investment or an investor of another Party… that grants rights to the covered investment or investor: (a) with respect to natural resources that a national authority controls, such as oil, natural gas, rare earth minerals, timber, gold, iron ore and other similar resources, including for their exploration, extraction, refining, transportation, distribution, or sale; (b) to supply services on behalf of the Party for consumption by the general public for: power generation or distribution, water treatment or distribution, telecommunications or other similar services supplied on behalf of the Party for consumption by the general public…; or (c) to undertake infrastructure projects, such as the construction of roads, bridges, canals, dams, or pipelines…"

- **An overreaching definition of "investor" and lack of robust "denial of benefits" provisions would allow firms from non-TPP countries and firms with no real investments to exploit the extraordinary privileges the TPP would establish for foreign investors.** The text includes an overreaching definition of "investor" as a person or legal entity that makes an investment as defined in the pact (Article 9.1). **This includes firms from non-TPP countries that have incorporated in a TPP signatory country.** Thus, for instance, one of the many Chinese state-owned corporations in Vietnam and Malaysia, TPP countries, could "sue" the U.S. government in a foreign tribunal to demand compensation under this text. Additionally, the text's broad definition of an "investor" could allow firms that have made no real investment in a country to drag governments through costly foreign tribunal proceedings. Existing U.S. trade deals include terms whereby an investor that is not native to a nation in the pact can be denied the benefits of the deal. The ostensible goal is to discourage "free riding" and "treaty shopping" by multinational firms. To counter abusive nationality planning, the pacts state that the benefits of the deal can be denied to investors if they are owned or controlled by investors outside of the trade pact signatory countries and they also have no "substantial business activities" in the claimed home nation (or in any signatory country beyond the host country). However, such "denial of benefits" terms are not particularly robust, since even having a staff person or two and a minor paper trail in the claimed home country can pass the "substantial business activities" threshold. These low thresholds are replicated in the TPP text, allowing Chinese or German investors (for instance) to channel investments through TPP nations in order to obtain the extraordinary TPP foreign investor protections and access the private enforcement regime (Article 9.14).

- **The TPP text does include one new provision aimed at limiting who can launch ISDS cases. This provision is intended to prevent an individual investor from launching an ISDS claim against their own home country**. In existing ISDS cases, individuals have launched such claims by setting up business activities in another country covered by an ISDS-enforced agreement and then acquiring "investments" back in their home country as a "foreign investor." The TPP language states that if an investor "is a natural person, who is a permanent resident of a Party, and a national of another Party, that natural person may not submit a claim to arbitration against that latter Party" (Article 9.1). But this provision only applies to "natural persons." Thus the prohibited individual could evade this limitation by incorporating a business in another TPP country, use that corporation to establish an "investment" back in their home country, and then use the corporation's newly-acquired "foreign investor" status to launch an ISDS claim against their home government.

- **Claims already decided in domestic courts can be re-litigated in ISDS tribunals for all but four TPP countries.** An annex in the TPP investment text states that if a foreign investor pursues a case in the domestic courts of Chile, Peru, Mexico or Vietnam over a government measure claimed as a violation of a foreign investor right, the investor cannot then launch an ISDS case against the government for that same claim under the TPP (Annex 9-J). It would appear that for all other TPP countries, foreign investors are welcome to pursue claims before domestic courts and, if they lose, re-litigate the case before an ISDS tribunal. Indeed, the final TPP investment chapter eliminates a proposed provision from an earlier leaked version that would have required foreign investors in all TPP countries to choose between pursuing claims before domestic courts or ISDS tribunals.

- **The TPP would grant foreign investors procedural rights that are not available to domestic firms to "sue" governments outside of national court systems, unconstrained by the rights and obligations of countries' constitutions, laws and domestic court procedures** (Section 9-B). The portion of the text that enumerates the private ISDS enforcement system largely replicates word-for-word the provisions of past U.S. ISDS agreements. However, foreign investors would be granted even more time to launch an ISDS case**.** While existing U.S. FTAs already allow foreign investors to initiate ISDS cases up to three years after the investor became aware of the alleged violation of their special foreign investor rights, the TPP text would expand that timeframe by another six months (Article 9.20.1). This final text also abandons a proposal in the 2012 leaked text that would have required a foreign investor to pursue domestic legal avenues before launching an ISDS case. This "exhaustion" requirement would have obliged investors to pursue domestic administrative review before launching an investor-state case. Exhaustion of domestic remedies is a fundamental principle of international law.

  What could be the justification for foreign investors to pursue claims against a nation outside of that nation's judicial system? The track record of ISDS cases reveals a clear answer: to try to obtain greater rights than those provided under national law and through domestic courts. Many of the TPP countries have strong domestic legal systems. For example, New Zealand, Australia, Singapore and Canada are all ranked by the World Bank as performing better than the United States with regard to adherence to rule of law. Yet, in a manner opposed by conservative and liberal jurists and policymakers alike, the private "investor-state" enforcement system included in the TPP text would empower foreign investors and corporations to skirt domestic courts and laws and "sue" governments in foreign tribunals, demanding cash compensation from national treasuries for domestic policies that they claim undermine their new investor rights. This would expand an alarming two-track system of justice that privileges foreign corporations in myriad ways relative to governments, domestic businesses and non-governmental organizations.

  The recent surge in ISDS cases has intensified opposition from legal scholars. An April 2015 letter signed by leading legal experts, including Harvard law professor and Obama mentor Laurence Tribe, strongly criticizes the TPP's proposed inclusion of ISDS, warning: "ISDS weakens the rule of law by removing the procedural protections of the legal system and using a system of adjudication with limited accountability and review. It is antithetical to the fair, public, and effective legal system that all Americans expect and deserve." A March 2015 letter signed by 139 U.S. law professors urges congressional leaders and the administration "to protect the rule of law and our nation's sovereignty by ensuring ISDS is not included" in the TPP, stating; "ISDS threatens domestic sovereignty by empowering foreign corporations to bypass domestic court systems and privately enforce terms of a trade agreement." A May 2012 letter signed by former judges, law professors and other prominent lawyers from TPP nations warns: "the foreign investor protections included in some recent Free Trade Agreements (FTA) and Bilateral Investment Treaties (BIT) and their enforcement through Investor-State arbitration should not be replicated in the TPP. We base this conclusion on concerns about how the expansion of this regime threatens to undermine the justice systems in our various countries and fundamentally shift the balance of power between investors, states and other affected parties in a manner that undermines fair resolution of legal disputes."

TPP Text Establishes Substantive Rights Available Only to Foreign Investors

- **The TPP investment text shows that foreign investors would be able to demand compensation if new policies that apply to domestic and foreign firms alike undermine their "expectations"**

of how they should be treated. This includes a right to claim damages for government actions (such as new environmental, health or financial policies) that reduce the value of a foreign firm's investment (Article 9.7 and Annex 9-B on indirect expropriation) or that go against the expected level of regulatory scrutiny that an investor might have had when dealing with a previous government (Article 9.6 on minimum standard of treatment). After a series of alarming ISDS rulings based on language replicated in the TPP text, annexes were added to U.S. FTAs starting with the 2005 CAFTA with language aimed at defining what sorts of government action should be considered an "indirect expropriation" or a violation of the "minimum standard of treatment" guarantee given to foreign investors. However, ISDS tribunals already have ignored these provisions in cases brought under recent U.S. FTAs that included the so-called safeguards now being touted with respect to the TPP, and instead have continued to develop their own broad interpretations of foreign investors' rights to rule against governments and order compensation to investors. The TPP text largely replicates these failed annexes, meaning that ISDS tribunals would maintain enormous discretion to order a government to pay a foreign investor merely because the government improved a regulatory policy applying to both domestic and foreign firms. Indeed, the inclusion of the language from past FTAs on a guaranteed minimum standard of treatment for foreign investors and the right to compensation for indirect expropriation directly contradicts the assurances TPP governments have given to legislators and public interest advocates that the pact would safeguard regulatory sovereignty.

- **The provision used in most successful investor compensation demands would be extended to challenges of financial regulatory policies.** The most successful (and controversial) basis for investors' challenges of government policies in past agreements is alleged violations of the guaranteed "minimum standard of treatment" (MST) for investors or the closely linked "fair and equitable treatment" (FET) provision. The TPP would be the first U.S. trade pact to empower foreign financial firms to use the open-ended MST and FET provisions to challenge domestic financial regulations before ISDS tribunals. Previous U.S. FTAs have shielded financial regulations from these most-used and most-abused of foreign investor claims. By newly allowing foreign banks to use these broad rights to attack financial regulations, the TPP would spell an unprecedented ISDS threat to U.S. financial stability measures.

  The TPP text regarding the MST and FET obligations largely replicates the language found in previous ISDS agreements on which tribunals have relied to issue some of the most alarming ISDS rulings to date (Article 9.6). Tribunals have often broadly interpreted these terms, effectively fabricating new obligations for governments that do not exist in the actual text of ISDS agreements. Of the 29 known ISDS cases under U.S. trade and investment agreements in which the foreign investor has "won," 76 percent (22) have found MST or FET violations. (In contrast, only seven have found national treatment violations, five have found expropriation violations and three have found performance requirement violations. Some cases found violations of multiple rules.)

  While some of the FET violations involved "denials of justice" as that term has long been understood under customary international law (e.g. lack of due process), some tribunals have found FET violations for government regulatory actions that simply contradicted what investors' argued were their "reasonable expectations." For instance, in an *Occidental Exploration and Production Co. v. Ecuador* case under the U.S.-Ecuador BIT, a tribunal ruled that the reasonable expectations requirement means that "there is certainly an obligation not to alter the legal and business environment in which the investment has been made." In defending itself against an investor-state challenge that tried to invoke this sweeping interpretation, the U.S. government argued, "[I]f States were prohibited from regulating in any manner that frustrated expectations – or had to compensate for any diminution in profit – they would lose the power to regulate." There is no right to compensation in U.S. law merely because a government policy changes after the establishment of an investment in a way that may affect a business operating here.

The TPP includes nothing to forestall these extreme interpretations. Instead, the text merely replicates an annex contained in recent U.S. FTAs that states that the relevant standard under customary international law that is intended for the MST provision is one that "results from a general and consistent practice of States that they follow from a sense of legal obligation" (Annex 9-A). This circular language has failed to fix the problem. Though this annex was first included in CAFTA, in two of the first investor-state cases brought under CAFTA – *Railroad Development Corporation (RDC) v. Guatemala* and *TECO Guatemala Holdings v. Guatemala* – the tribunals simply ignored the annex's attempt to narrow the definition of "minimum standard of treatment" with a requirement that tribunals examine the *actual* practice of nations. Instead, the *RDC* and *TECO* tribunals both relied on an expansive interpretation of the standard concocted by a previous ISDS tribunal, which included an obligation to honor investors' expectations. On that basis, both tribunals ruled that Guatemala had violated the expanded obligation, and ordered the government to pay millions. The TPP fails to remedy this severe flaw, leaving uncertainty and unpredictability that invites investors to launch more ISDS attacks against public interest policies.

- **Foreign investors would be allowed to use claims of "indirect expropriation" to demand government payments for regulatory costs all firms operating in a country must meet.** Under domestic and international law, governments' obligation to compensate for expropriation has typically applied to the physical taking of real property, such as when a government expropriates a house to make way for a highway. But the TPP annex on expropriation, as in past U.S. FTAs, makes clear that foreign investors can launch claims of indirect expropriation when the government has not actually taken ownership or control of an investment. The final text would provide investors with a right to demand compensation for "indirect" expropriation (Article 9.7 and Annex 9-B), which can be and has been interpreted by ISDS tribunals to mean regulations and other government actions that merely *reduce* the value of a foreign investment. This definition of indirect expropriation cannot be justified as reflecting the general practice of states, given that the dominant practice of nations is to provide for compensation only when the government has actually acquired an asset or permanently destroyed all of its value, not merely when the value of an asset has been adversely affected by regulatory measures.

  Moreover, the right to compensation for indirect expropriation in the text applies to much wider categories of property than those to which similar rights apply in U.S. law. To the limited extent that indirect expropriation compensation is permitted in U.S. law, it has generally been held that the requirement of compensation for "regulatory takings" under the Fifth Amendment of the U.S. Constitution primarily applies to regulations affecting *real* property (i.e. land). However, the broad provisions of the TPP investment chapter, like existing FTAs, enable foreign investors to claim "indirect expropriation" if government regulations implicate their personal property, intellectual property rights, financial instruments, government permits, money, minority shareholdings or other forms of non-real-estate property.

  An earlier leaked version of the TPP investment chapter included a proposed provision that attempted to safeguard public interest regulations from indirect expropriation claims, stating, "non-discriminatory regulatory actions … that are designed and applied to achieve legitimate public welfare objectives, such as the protection of public health, safety and the environment do not constitute indirect expropriation." Instead, the final TPP investment chapter, like past U.S. FTAs, includes a clause containing a loophole that undermines this attempted safeguard. It states that non-discriminatory health, safety, environmental and other public interest regulations could indeed be challenged as indirect expropriations "in rare circumstances" (Annex 9-B). The loophole would grant ISDS tribunals discretion to determine when such non-discriminatory public interest policies constitute an indirect expropriation. The final text also eliminated, in favor of terms granting tribunals ample discretion over the meaning of indirect expropriation, an alternative provision that would have explicitly restricted indirect expropriation claims to instances when a government "deprivation of the investor's property" is "(a) either severe or for an indefinite period; and (b) disproportionate to the public purpose."

- **Foreign corporations could be newly empowered to privately enforce public agreements concerning intellectual property in ISDS challenges to government policies that ensure access to affordable medicines.** Unlike past U.S. FTAs, the TPP investment text could empower foreign investors to claim that government policies that ensure access to affordable medicines constitute TPP-prohibited "expropriations" of intellectual property rights if deemed to violate the terms of the WTO's Trade-Related Aspects of Intellectual Property Rights (TRIPS) agreement (Article 9.7.5). WTO rules can only be enforced when one government formally challenges another government before a WTO tribunal. There is no right in the WTO for a corporation to directly challenge sovereign governments. But with this new provision in the TPP investment text, individual firms could be empowered to privately enforce the terms of the WTO's monopoly protections for pharmaceutical firms, and directly challenge governments for alleged violations of these protections. In addition, the signatory governments of TRIPS, including TPP governments, deliberately included ambiguous language in TRIPS to grant flexibility to each government to interpret the terms in line with domestic priorities. But the TPP investment text could empower the three private lawyers of ISDS tribunals, which have a clear track record of interpreting vague terms broadly to favor foreign investors, to impose their binding interpretation of TRIPS' intentionally flexible terms on the very governments that negotiated those terms. This move, which risks making TRIPS obligations enforceable via ISDS, could restrict governments' policy space to ensure access to affordable medicines.

- **Domestic policies that apply equally to domestic and foreign firms could be challenged by foreign investors under the TPP.** The TPP text would allow investors to claim that government actions (such as new environmental, health or financial laws) violate "national treatment" or "most favored nation" rules, ostensibly intended to prohibit discriminatory treatment, even when the laws are facially neutral and lawmakers did not intend to harm foreign investors (Articles 9.4 and 9.5). Such claims could be used if a foreign investor's own business model resulted in the firm experiencing a slightly higher burden in complying with a non-discriminatory law. For example, a government's carbon emission controls could disproportionately impact foreign investors if most domestic energy firms used less carbon-intensive sources of energy than their foreign-owned counterparts. While a footnote in the text suggests that differences in treatment of foreign investors may be allowed "on the basis of legitimate public welfare objectives," the ISDS tribunal would have full discretion to judge whether a government's public welfare objectives are "legitimate" and whether the alleged difference in treatment of foreign investors owes to those objectives.

- **Policies to create domestic jobs, support domestic businesses or foster economic development would be subject to foreign investors' demands for compensation.** The TPP investment chapter, like past U.S. FTAs, would empower foreign firms to demand compensation from governments for "performance requirements" imposed on domestic and foreign firms alike (Article 9.9). Foreign firms would be able to challenge policies used by many governments to support local job creation and business growth (for example, by requiring firms to purchase inputs from domestic businesses). (While Article 9.9.4 allows requirements to employ local workers, this does not extend to so-called backward linkages, like purchasing locally made inputs.) In a recent ISDS case brought against Canada under the North American Free Trade Agreement (NAFTA), a tribunal ruled that Canada's non-discriminatory requirement for oil companies to contribute to research and development in one of the country's poorest provinces violated such "performance requirement" provisions. The TPP text goes even further than past U.S. FTAs in listing additional performance requirements that can be challenged.

- **Most TPP countries have decided to expose decisions regarding the approval of foreign investments to ISDS challenge.** An annex in the text states that a government's decision, done in accordance with domestic laws, on whether to approve a given foreign investment in its territory shall not be subject to ISDS enforcement (Annex 9-H). But the annex only applies to four of the 12 TPP countries (Australia, Canada, Mexico and New Zealand). A separate annex (Annex 9-F) also contains some protections for Chile's foreign investment laws. For the remaining countries, the TPP text would apparently empower foreign firms to challenge such decisions before ISDS tribunals. In the United States, for example, the Committee on Foreign Investment in the United States (CFIUS) reviews planned foreign investments to determine whether they pose threats to national security. CFIUS has the authority to recommend to the president that investments deemed as threatening not be authorized. In cases where the president acts on such recommendations, the TPP text would appear to empower foreign firms to retaliate by asking foreign tribunals to order taxpayer compensation. While the TPP includes a national security exception clause, the provision removes a critical footnote included in the last four U.S. FTAs that specified that it was up to a government, not an ISDS tribunal, to determine when a challenged measure was necessary for the protection of the nation's essential security interests. The TPP's removal of that footnote, which a bipartisan bloc of members of Congress fought for, means that three lawyers on an ISDS tribunal – not the government of the United States – would have the authority to determine what constitutes the essential security interests of the United States. Under the weakened TPP provision, if the U.S. president decided not to allow a foreign investment after CFIUS determined it posed a threat to national security, an ISDS tribunal would be empowered to second-guess the U.S. government with respect to what constitutes an essential security interest of the United States and order compensation to the foreign firm with U.S. taxpayers' money.

- **Foreign corporations could demand compensation for capital controls and other macro-prudential financial regulations that promote financial stability.** Like past U.S. FTAs, the TPP text requires that governments "shall permit all transfers relating to a covered investment to be made freely and without delay into and out of its territory" (Article 9.8). This obligation restricts the use of capital controls or financial transaction taxes, even as the International Monetary Fund (IMF), many prominent economists and world leaders have shifted from opposing capital controls to officially endorsing them as a legitimate policy tool for preventing or mitigating financial crises.

  In July 2015, the four Democrats in the House of Representatives with the highest authority on matters of trade and finance – the ranking members of the House Financial Services Committee, the House Ways and Means Committee and the trade subcommittees of both – sent a letter to the Obama administration to warn against the TPP's threat to capital controls. They concluded, "With what we know today about the dangers of volatile, short-term capital movements, we hope the Administration will avoid showing the world that there are times when those who *remember* the past are also bound to relive it, especially when it is likely to come at enormous economic and human cost." In a December 2014 letter to the administration, Senator Elizabeth Warren (D-Mass.), member of the Senate Banking Committee, and Sens. Tammy Baldwin (D-Wis.) and Edward Markey (D-Mass.) urged the administration to not replicate in the TPP terms from past U.S. FTAs "that could limit the ability of the government to use capital controls." In another letter that same month led by Congresswoman Maxine Waters (D-Calif.), the ranking member of the House Financial Services Committee, leading House Democrats made clear to the administration their opposition to the inclusion of such restrictions on capital controls in pending trade deals.

In February of that year, U.S. Federal Reserve economists backed capital controls in a study finding they "can lead to a significant welfare improvement." And in a February 2012 letter signed by more than 100 prominent economists, including Jagdish Bhagwati of Columbia University, former IMF officials Olivier Jeanne of Johns Hopkins University and Arvind Subramanian (formerly of the Peterson Institute for International Economics, now chief economic adviser to the government of India), demanded that such provisions be excluded from the TPP, stating, "The U.S. government's rigid opposition to capital controls does not reflect the global norm." This followed a January 2011 letter to the Obama administration signed by more than 250 economists, including Nobel laureate Joseph Stiglitz, Harvard economics professors Ricardo Hausmann and Dani Rodrik (formerly at Harvard University, now at the Institute for Advanced Study), and José Antonio Ocampo (a former executive secretary of the UN Economic Commission on Latin America and the Caribbean, and Colombia's former Minister of Finance), noting that past U.S. FTAs and BITs "strictly limit the ability of our trading partners to deploy capital controls." Yet, the final TPP text would replicate the past U.S. template, defying the post-financial crisis consensus that policy space for capital controls must be preserved.

Ineffective Exceptions and Limitations

- **Broad-based concerns about the TPP's ban on the use of capital controls resulted in a new "temporary safeguard" provision despite years of U.S. opposition. But the actual provision ultimately agreed would not adequately protect governments' ability to regulate speculative and destabilizing flows of capital.** In contrast to past U.S. FTAs, the final text includes a "temporary safeguard" to allow the use of limited types of capital controls, subject to a litany of conditions, that would otherwise violate the expansive obligations of the Investment Chapter's free transfers provisions (Article 29.3). Unfortunately, the provision largely replicates Article XII of the WTO's General Agreement on Trade in Services (GATS) "Restrictions to Safeguard the Balance of Payments" provision. Both the GATS and TPP language apply to "serious balance-of-payments and external financial difficulties or threat thereof" (GATS XII-1).

  Thus, the provision would only apply to capital controls enacted for certain reasons (e.g. to remedy balance of payments crises or "exceptional" macroeconomic problems), while capital controls used for other policy objectives (e.g. to prevent destabilizing asset bubbles) would still be subject to ISDS challenges. In addition, the GATS language refers to the special needs developing countries may have for such policies. Both the TPP and GATS terms require capital controls to be consistent with the Articles of Agreement of the International Monetary Fund, avoid unnecessary damage to the commercial, economic and financial interests of any other Party, not exceed those necessary to deal with the circumstances and not be used to avoid necessary macroeconomic adjustment. Thus, the safeguard would only apply to those capital controls that an ISDS tribunal – not a government's central bank – deemed "necessary". Governments, not ISDS tribunals, should have the authority to decide when capital management measures are needed and how they should be implemented.

And such measures are to be temporary and phased out progressively. Under the TPP provision, even capital controls used to *respond* to balance-of-payments and other macroeconomic problems (rather than to prevent them) could run afoul of the provision's requirement, if they last longer than 18 months. Use beyond this time period is subject to majority approval of the other TPP parties. This restriction would preclude the use of capital controls for longer-lasting financial crises. The provision would have failed to safeguard, for example, the capital controls that Malaysia, also a TPP party, implemented in 1997 in response to the Asian financial crisis, which were phased out slowly *over a decade.* Indeed, the overarching requirement that such policies be temporary means the "safeguard" does not provide policy space for capital controls of a more permanent nature, such as those relating to capital inflows that are designed to *avoid* balance-of-payments and other macroeconomic problems. For example, the capital management policies of Chile, a TPP party, involve standing laws of general application that were not implemented in response to a specific crisis, but to avoid the conditions that could cause one. A separate TPP annex would allow Chile alone to maintain or enact capital controls that are consistent with its own domestic laws to ensure financial stability (Annex 9-E). No such protection is available for other TPP nations.

The TPP provision adds two further constraints. First, such measures are subject to ISDS challenges as indirect expropriations. That is to say that while the safeguard may permit a TPP country to enact a capital control, it may also be required to compensate a foreign investor if doing so results in a significant reduction in the value of that investor's investment. There is no comparable obligation to compensate private investors in the GATS. And, in TPP capital controls "shall not apply to payments or transfers relating to foreign direct investment."

- **The TPP provision on environmental, health and other regulatory objectives is meaningless.** The text includes a provision, largely copied from past U.S. pacts, on "Investment and Environmental, Health and other Regulatory Objectives" that provides no meaningful safeguard against ISDS challenges to public interest policies (Article 9.15:"Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure **otherwise consistent** with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental, health or other regulatory objectives." (emphasis added). The provision's inclusion of self-cancelling language means that a signatory government may enact public interest protections, *so long as doing so does not conflict with the sweeping rights that the pact gives to foreign investors*. But it is precisely when investors' broad rights conflict with environmental, health or other regulatory objectives that a government needs an agreement to specify that its right to regulate trumps its obligations to foreign investors. Thus, this provision is meaningless. Indeed, a tribunalist in the *S.D. Myers v. Canada* NAFTA ISDS case noted that this provision, also included in NAFTA, was among those referred to by trade analysts as "'tautologies' or as 'diplomatic, rather than legal' statements." A recent legal review from Cambridge University Press concluded that this clause "falls short in failing to add more than a nebulous provision that can easily be marginalized."

  In an earlier leaked version of the TPP Investment Chapter, one country proposed an additional paragraph to this text that read: "The Parties recognise that it is inappropriate to encourage investment by relaxing its health, safety or environmental measures. Accordingly, a Party should not waive or otherwise derogate from or offer to waive or otherwise derogate from, such measures as an encouragement for the establishment, acquisition, expansion, or retention in its territory of an investment of an investor." This proposed language has been omitted from the final TPP investment chapter. (And while similar language has been included in the TPP's environment chapter, the inclusion of such language in past FTAs, such as the U.S.-Peru FTA, has failed to prevent or discipline rollbacks of environmental protections explicitly enacted to encourage investment – *see Sierra Club's analysis of the final TPP environment chapter for more*.)

Finally, while a few TPP countries tried to exempt specific domestic public interest policies from the broad obligations of the Investment Chapter in the leaked January 2015 version of the text, all of these exceptions have been eliminated in the final text. As a result, Australia's public health programs, Malaysia's procurement measures and Canada's cultural promotion policies would all be exposed to ISDS challenges under the TPP. And while the text includes a provision to prevent ISDS challenges to tobacco-related health measures, the deal would allow ISDS attacks on a wide array of other public health policies, from patent laws that tamp down the rising cost of medicines to commonsense bans on toxins to requirements for firms to mitigate pollution.

- **A new article makes a hortatory reference to encouraging corporate social responsibility**. Language included in the final TPP investment chapter is even weaker than the already-hortatory "corporate social responsibility" language proposed in an earlier leaked version. While the earlier language stated that each signatory government "should encourage" firms to *voluntarily* incorporate principles of corporate social responsibility, the approved language in the final text merely notes that the signatory governments "reaffirm the importance" of such non-binding encouragement (Article 9.16).

- **Foreign investors could not invoke procedural ISDS provisions from other agreements, but could still try to invoke even broader substantive rights for foreign investors than found in the TPP.** While the "most-favored nation treatment" provisions of ISDS-enforced pacts are supposed to simply require governments to treat foreign investors from a pact's signatory countries no less favorably than investors from other countries, foreign firms have successfully used these provisions as a loophole to "import" broader foreign investor privileges from other pacts. Doing so has allowed foreign firms to launch ISDS cases against governments for allegedly violating obligations to which the governments never agreed. The TPP text includes a new provision that appears aimed at partially closing this loophole, indicating that foreign investors cannot use the "most-favored nation treatment" obligation to import *procedural* rights from other pacts (Article 9.5.3). However, the provision would not prevent foreign investors from importing broader substantive rights from other pacts. For example, the language would appear to allow tribunalists to grant a foreign investor, upon its request, access to definitions of "indirect expropriation" and "minimum standard of treatment" that are even more expansive and more favorable to investors than those included in the TPP, posing an even greater threat to public interest policymaking.

- **The United States, unlike most other TPP countries, has chosen to subject sovereign debt restructuring to ISDS challenges.** An annex in the investment chapter seeks to ensure that disputes related to sovereign debt and sovereign debt restructuring are not subject to the full range of investment chapter disciplines (Annex 9-G). But a footnote states that the partial safeguards for sovereign debt restructuring "do not apply to Singapore or the United States." That is, were Singapore or the United States to negotiate a restructuring of its sovereign debt that applied equally to domestic and foreign investors, foreign investors alone would be empowered under the TPP to challenge the non-discriminatory restructuring before an ISDS tribunal, claiming violations of any of the broad substantive foreign investor rights provided by the TPP Investment Chapter.

- **Despite prior opposition, and in defiance of the Australian government's own Productivity Commission, Australia has agreed to subject its policies and taxpayer funds to the jurisdiction of ISDS tribunals under the TPP**. In prior leaked versions of the investment chapter, Australia had included a footnote stating that it would not be bound to ISDS enforcement. That footnote has been eliminated, meaning that, for the first time, the TPP would expose Australia to ISDS attacks from U.S. firms – the world's most aggressive users of ISDS. (Australia successfully resisted U.S. pressure to include ISDS in the existing U.S.-Australia FTA.) This decision by the Australian government directly contradicts the advice of the government's own pro-free-trade and pro-TPP Productivity Commission, which warned in a June 2015 report against including ISDS in Australia's trade pacts. The commission concluded that ISDS-enforced obligations in FTAs "depart from national treatment principles by affording substantive appeal rights to foreigners not available to domestic firms, risk impeding domestic regulatory reform (regulatory chill), include safeguards and carve-outs of uncertain effect, lack transparency and have inadequate parliamentary scrutiny." In addition, the commission found that ISDS provisions "are not necessary or sufficient to foster investment flows between developed countries" and warned that they could "expose the Australian Government to potentially large unfunded contingent liabilities dependent on decisions by international arbitration tribunals." With the Australian government's reversal on ISDS in the TPP, all TPP countries would be subject to the private investor-state corporate enforcement regime. This would also impose new obligations on Japan, New Zealand, Malaysia, Brunei and Vietnam – the TPP countries that do not have existing U.S. FTAs.