The United States-Mexico-Canada Agreement Significantly Curtails Foreign Investment Protection

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On September 30, 2018, the United States, Mexico and Canada announced they had reached an agreement to revamp the 24-year-old North American Free Trade Agreement (NAFTA), which now will be known as the United States-Mexico-Canada Agreement (USMCA). This includes a significantly rewritten system for investment claims (known as Chapter 14). Investors who have relied on NAFTA to protect their cross-border investments can use this opportunity to reassess their existing investment protection structures and consider alternative ways to achieve protection under other bilateral or multilateral investment treaties.

The USMCA curtails the substantive protections available to investors in several fundamental ways. It rolls back the definition of expropriation so as to protect against "direct" expropriation only, thus reversing longstanding U.S. policy that previously sought to protect interests against indirect expropriation (*i.e.*, measures tantamount to expropriation). The USMCA also states that the "minimum standard of treatment" owed to foreign investors is expressly tied to customary international law, thus cementing a position adopted by NAFTA in a controversial 2001 "interpretation." It further states that "'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by [the minimum standard of treatment], and do not create additional substantive rights." Art. 14.6(2).

The newly released Chapter 14 thus has significant ramifications for investors, particularly in the broader context of investor-state arbitration. In the current system, Chapter 11 of NAFTA allows investors to seek international arbitration to remedy violations of NAFTA's substantive investment protections. Under Chapter 14 of USMCA (assuming the existing NAFTA is terminated, and USMCA enters into force), investors may continue to bring "legacy" arbitration claims (*i.e.*, claims concerning investments established or acquired between January 1, 1994, and the termination of the existing NAFTA) under the existing NAFTA for three years. Thereafter, under the USMCA, investor-state arbitration will cease to be available with respect to either Canadian investments in the U.S. or Mexico, or for U.S./Mexican investments made in Canada. This means that those investors will have to resort to national courts, state-to-state arbitration, or investor-state arbitration under a different treaty (if applicable). One such alternative is the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), in the case of Mexican investors in Canada or Canadian investors in Mexico. Canada, the United States and Mexico also have entered into bilateral investment treaties with other countries that may provide alternative sources of protection if investments are correctly structured to avail of those treaties.

For investments made by U.S. investors in Mexico (or vice versa), investor-state arbitration would still remain available between the United States and Mexico pursuant to Annex 14-D of the USMCA, but its scope is substantially limited. The USMCA, significantly rewrites the basic guarantees so that investor-state arbitration only would be permitted in cases of denial of post-establishment national treatment and "Most Favored Nation" violations, or in the case of direct expropriation. Even there, procedures are changed. In a departure from the existing NAFTA, investors under the new treaty will be required to seek recourse before a competent court or administrative tribunal of the respondent state, for a minimum of 30 months, before commencing investor-state arbitration. They also will have to give 90 days' notice of their arbitration claims. These rules significantly delay any access to international remedies.

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Pursuant to Annex 14-E, some U.S. and Mexican investors will enjoy broader access to investor-state arbitration, including the right to bring claims for violation of minimum standard of treatment and indirect expropriation, but this only applies to investments that qualify as "covered government contracts" in sectors such as oil and natural gas production, power generation, telecommunication, transportation, and certain infrastructure investment that are not for the exclusive use of either Mexico or the United States (*see* Annex 14-E, art. 6(b)). Annex 14-E has some further unusual features, and provides that it can be modified or eliminated in the future, and will not operate if the respondent state is no longer "a party to another international trade or investment agreement that permits investors to initiate dispute settlement procedures to resolve an investment dispute with a government." Annex 14-E, art 2.(a)(i)(B). In short, if either the U.S. or Mexico were no longer party to any treaties with investor-state arbitration provisions, the expanded scope of arbitration for "covered government contracts" no longer would apply.

In sum, the USMCA significantly narrows the scope of future arbitral claims brought by investors, as well as the protections they may seek. Nevertheless, affected investors can seek to mitigate the impact of these changes through effective investment planning and structuring.