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The XL Stands for "Extra Litigation"

TransCanada says if the United States doesn't approve the Keystone XL pipeline, it might sue under NAFTA.

By Brian Palmer

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TransCanada and its allies in the Canadian government contend that blocking the Keystone XL pipeline would violate the North American Free Trade Agreement (NAFTA), the 1994 treaty that facilitates trade between the United States, Canada, and Mexico. If the president doesn't approve its pipeline, TransCanada says it could sue us.

This would be a peculiar gambit to play at this point. Keystone XL's fate is still a U.S. political matter, and saber rattling is not likely to endear a foreign corporation like TransCanada to American voters. More importantly, the threat of a lawsuit doesn't intimidate the federal government the way it does a used car dealer. The U.S. Justice Department employs the world's largest stable of attorneys and has never lost a NAFTA challenge. That's not to say TransCanada couldn't win—as you'll learn below, the vagueness of the relevant laws makes the outcome of these cases nearly impossible to predict—but the timing is bizarre.

"This is a Hail Mary," says Anthony Swift, a staff attorney in NRDC's international program. (Disclosure.) "TransCanada has made a series of outlandish threats against governments at every level, but they rarely carry them out."

TransCanada's threat is more worrisome because of what it represents: a growing boldness on the part of major corporations to combat environmental, health, and labor regulations in international tribunals rather than fighting them in domestic courts before politically appointed or democratically elected judges.

The underlying issue is found in Chapter 11 of NAFTA, which contains an Investor-State Dispute Settlement provision, or ISDS. It enables a North American corporation to sue the United States, Canada, or Mexico in a special extra-national tribunal over treaty violations. These provisions have become common in free-trade agreements, despite being widely opposed by ideologically diverse groups of politicians and legal experts who believe they limit national sovereignty and undermine health, environmental, and labor laws.

Here's an example of an ISDS at work: In 1997, Canada banned the import of the gasoline additive MMT over neurotoxicity concerns. The U.S. manufacturer (then known as Ethyl but now called Afton) sued Canada, claiming that the ban violated NAFTA. After losing some procedural decisions, Canada decided to settle. Afton took home $13 million in damages, and the Canadian government agreed to reverse the MMT ban. In this one case, we can see several problems with ISDS provisions.

THEY TREAT CORPORATIONS LIKE NATIONAL GOVERNMENTS.

"ISDS provisions are an anomaly in international law, which was traditionally about the relationships between nation-states," says Matthew Porterfield, a senior fellow studying trade and environmental issues at Georgetown University.

The Kyoto Protocol, for example, addressed climate change on the national level—it did not dictate the behavior of individual corporations. The Antarctic Treaty created a system for countries, not corporations or universities, to manage the uninhabited continent. Individuals and corporations cannot sue the U.S. government for violations of the Geneva Convention. Trade agreements are also typically enforced by governments against other governments—not by corporations. This is how international treaties and protocols work.

THEY ARE DISCRIMINATORY.

"Oppressed minorities can't sue governments under international law, but big corporations can under ISDS," says Simon Lester, a trade policy analyst at the Cato Institute. "That's fundamentally unfair."

THEY ARE VAGUE.

Governments don't know what sorts of regulatory activity might enable a corporation to sue them. Let's go back to the MMT case. The manufacturer claimed Canada's ban on the chemical constituted an "indirect expropriation" of its assets. Essentially, Afton argued that Canada undermined the company's profitability by banning its product. Other corporations have accused government regulations of failing NAFTA's "fair and equitable treatment" standard. What does "fair and equitable" mean exactly? It's supposed to mean the regulation is consistent with those of other countries, but it doesn't always work that way.

"In practice," says Porterfield, "it comes down to the tribunals to decide what they think is fair and equitable. It ends up being very subjective."

This, by the way, would likely be the basis of any TransCanada suit against the United States. The company would claim that the Keystone XL rejection is inconsistent with our government's historical approach to pipelines.

Vagueness and subjectivity are problematic in any legal system, but they are especially worrisome in ISDS litigation. The tribunals—the people who get to decide what chemicals governments can ban, what worker protections they can implement, or what limits they can put on carbon emissions—are composed primarily of corporate lawyers rather than real judges. Not just any corporate lawyers, though. They are practicing ISDS lawyers, who regularly represent corporations in very similar cases. This is a major conflict of interest.

“It’s not like a domestic legal system with dedicated judges and lawyers,” says Lester. “You have people acting as a judge in one case, then the next day they are litigating another case. There is a risk that they will consider how their decisions [as judges] might affect their other cases and clients.”

THEY ARE UNDEMOCRATIC.

Technically, the only thing a corporation can win in an ISDS lawsuit is money. But, in reality, ISDS provisions can give corporations veto power over new laws and regulations. Since any government would be terrified of losing a major lawsuit, it might agree to drop its regulation—one developed by a legitimate, democratic process—to avoid having to pay damages to a foreign company. That’s what happened in the MMT case: Afton reduced their financial demands after Canada agreed to reverse the ban.

The mere prospect of an ISDS case can put smaller countries over a barrel. In 2010, cigarette maker Phillip Morris sued Uruguay for requiring health labels on cigarettes. The country couldn’t even afford to defend itself, let alone pay the potential damages. Billionaire New York City Mayor Michael Bloomberg eventually gave the country $375 million, but he can’t be expected to defend every ISDS case in the world. (The cigarette case is ongoing, which is an indication of how expensive the process can be.)

Fortunately, the U.S. government doesn’t have those sorts of worries—yet. Even if TransCanada were to win its threatened NAFTA case, the damages would be relatively small in the grand scheme of the U.S. budget. But imagine if a coalition of foreign energy companies decided to sue us (or Canada, or Mexico…) on the theory that carbon pollution standards affected them unfairly. The potential damages in that case could be significant. Energy companies—or any company, for that matter—shouldn’t have that much power over our government.