

Why Should Local and State Governments Pay Attention to the New International Treaties?

Jennifer Gerbasi and Mildred Warner

June 2002

International trade arena is gaining a new audience. Traditionally a matter reserved exclusively for the federal government, state, county and municipal governments are taking a closer look at how the new generation of trade treaties may place greater demands on all levels of government. Governments are trying to understand the best way to enjoy the benefits from the markets and protections provided by the treaties while retaining local governmental authority. The Western Governors Association, the National Council of State Legislators, and the National League of Cities are a few entities that have made public requests to the US negotiating body, the United States Trade Representative (USTR) for clarification of or protection from the treaty obligations. Why are they concerned?

International Trade Treaties Impact Local And State Laws

As currently formulated, the new treaties may significantly restrain the authority of state and local governments. Though the treaties do not directly require changes to existing laws, they do lay a foundation for challenging democratically created laws and customary domestic practices. A broad range of state and local powers may be impacted including, but not limited to zoning, water management, land use planning, the finality of the court system, and public service provision^[1]. Regional cooperation, business subsidies, regional environmental plans and precautionary health regulations are common tools planners and legislators use to encourage growth and protect human health as well as property values. These mechanisms may be impractical or non-compliant with treaty obligations. New international standards stemming from free trade treaties (such as the North American Free Trade Agreement (NAFTA), the Free Trade Area of the Americas (FTAA), and the General Agreement on Trade in Services (GATS) waive government immunity, forbid the use of many planning tools like those listed above, and supercede local preference and democratically established legislation. Other areas that may be affected by the treaties include pesticide residue laws, recycled content laws, pollution control, licensing requirements and labeling. Customary public policy considerations may not be legitimate in the international trade arena.

Deference to State Laws Supplanted by International Standards

States and localities are currently able to customize legislation to meet local needs and concerns. The treaties obligate federal, state and local laws to comply with international standards. If there is a conflict, international arbitration tribunals are authorized to interpret the law and levy heavy financial fines for non-compliance. Historically, when federal and state laws have differed, US courts have given deference to state laws as long as they did not contradict the federal law. The government closest to the citizens is assumed to be most able to represent local preferences and priorities. Public policy and economic conditions are criteria for selecting what is appropriate in the context of each geographical area. These new international trade tribunals are not obligated or encouraged to follow or consider US customs or law. State and federal governments have historically enjoyed some protections from frivolous lawsuits because they cannot be sued without consenting to the case. Under the NAFTA, immunity is waived. Foreign nationals with financial investments in the United States can challenge laws they perceive as limiting expected profits. Investors challenge the national government directly, not the specific state or local government. State and local governments have no seat at the negotiating table or arbitration panel hearings. It is unclear

whether the government body that passed the offending measure or the nation will pay if the challenge is successful.

New Rights Bring Investors on Par with Nations

An "investor" is any person, company or lender with a financial venture that sells goods or services in a participating country where the investor is considered foreign (i.e. US investor in Mexico)^[iii]. These investors have a right to sue for "government measures" that affect their investments negatively. The rights are based on the legal principle that commercial entities have a right to be ruled by the least burdensome laws necessary to achieve the stated objective. Laws must pass a three-part test that proves that:

1. the objective is considered legitimate under the WTO;
2. it is the least trade restrictive alternative available; and
3. the measure does not constitute a disguised restriction on trade.

These new investor rights may exceed the rights given to citizens under the Constitution. Foreign investors may be paid for partial regulatory takings that are considered non-compensable, reasonable losses for the privilege of citizenship in the domestic context^[iii]. This change is the basis of much of the concern voiced by state and local governments.

Devolution and Preemption: Concurrent and Competing Trends

In contrast to "devolution" which is increasing the authority of state and local government, international trade agreements appear to encroach on state sovereignty. State and local government associations have made public statements to Congress outlining their concerns that State rights to self-governance under the 10th amendment are being eroded. The National Association of Counties (NACo) has long been on guard against federal preemption in the domestic context. NACo has only recently voiced concerns about international trade treaties prompted by investor provisions in the Andean Trade Promotion and Drug Enforcement Treaty. California has created the Senate Select Committee on International Trade Policy and drafted legislation specifically to identify the potential threats to public health, the environment and the legislative process. Local governments from Oregon to Massachusetts have written resolutions requesting a more meaningful presence in the negotiations, or the ability to opt out of these treaties entirely. Academics, non-governmental organizations (NGOs) and the international community are also studying international treaties and attempting to join the debate at the negotiating table.

The concerns of the government groups are similar, and the resolutions to Congress and requests for information from the USTR have common themes. State and local governments are seeking to participate fully in the negotiations to try to preserve the traditional powers of state and local governments. In case of failure in that pursuit, they are requesting that the USTR protect these rights in the negotiations. Specifically, they are asking the USTR or Congress to:

- Provide open and transparent proceedings including negotiations, submissions and arbitrations and a mechanism for meaningful participation in those proceedings.
- Reserve equal rights to the people, and apply constitutional restrictions equally to foreign investors.
- Preserve police powers that are the basis for protecting human health, environmental resource conservation and fair competition.

- Make states and localities immune from the investor challenges.
- Require the investor's national government to consent to the claim being brought against the defending government to avoid frivolous claims or those that do not serve the greater public interest.
- Preserve the concept of federalism in practice in the United States by ensuring that States continue to be the dominant policy makers in traditional areas such as land use planning, education, and public services.

Financial Claims May Stall Legitimate Regulations

In theory, governments can continue to manage in the usual fashion even under the treaties. However, the taxpayer would have to pay millions of dollars for the federal government to defend the measure and pay the fines if defeated. The current potential liability to the United States from NAFTA claims is \$1.8 billion USD. The number of claims is expected to expand proportionally with the addition of 31 more countries under the Free Trade Area of the Americas (FTAA). There is no indication at this point if the Federal government will pass the cost of fines on to the state and local governments or continue to pay out of general funds.

The challenges span the gamut of local legislative efforts^[iv].

- *Methanex v. United States*: A Canadian company is challenging a California resolution to ban a ground water pollutant. Potential cost: \$970 million
- *Ethyl v. Canada*: \$13 million was paid as a settlement in a case parallel to *Methanex*. Canada also apologized and lost the right to ban the chemical (banned already in some US states).
- *Loewen v. United States*: Challenges the Illinois standard court of appeals process, which requires a bond equal to 150% of damages. Potential cost: \$725 million
- *Sun Belt Water, Inc. v. Canada*: Questions the right to refuse to export a natural resource. Potential cost: \$220 million
- *Metalclad v. Mexico*: \$17 million paid to stop water pollution from a hazardous waste facility.

Ohio Democrat Congressman Sherrod Brown stated that “in NAFTA and in every public health challenge under the WTO, 33 straight times, public health laws, environmental laws, and food safety laws, every single time they have been struck down”. Given the potential implications of these challenges, it is surprising that there are not more governments actively involved in this debate. In early 2002, Bill Moyers broadcast the issue to the public over PBS in the program “Trading Democracy”. The media has given a glimpse of the increasingly popular protests against “free trade”, the WTO and the FTAA. However, these protests have not focused on state and local government concerns. NGOs have been effective in getting their agenda heard, but state and local governments have not been very active in the public debate.

More State and Local Governments Should Join the Debate

States and local governments rely on history and future demands to formulate current but predictable legislation that meets the needs of the communities they serve. State representatives have not convinced the treaty negotiators of the dangers of loss of this

stability due to trade obligations. Treaty negotiators believe free trade treaties should focus on economic issues and some state and national sovereignty must be lost in the give and take of treaty formation.^[v] Neither the framers (including government and commercial interests) nor the public are focused on the implications for everyday governance of our states and cities. Planners and elected representatives of this country need to educate themselves about the issues that affect their constituents and regions. A balance must be struck between the benefits of free trade and the preservation of state and local sovereignty.

^[i] Keuhl, Senator S., Senate Joint Resolution No. 40 – Relative to international investment agreements submitted to the legislature March 20, 2002.

^[ii] The North American Free Trade Agreement, Chapter 11, Article 1101.

^[iii] Dalton, Robert, E., 1999. National Treatment Law and Practice. M. Leigh and L.B. Ederington, Eds. Chapter 6, "United States". American Society of International Law, Washington, DC.

^[iv] International Institute for Sustainable Development, 2001. Public Rights, Public Problems: A guide to NAFTA's controversial chapter on investor rights. World Wildlife Fund, Canada.

^[v] Record of statement to the Subcommittee on Ways and Means Hearing on Free Trade Deals: Is the United States Losing Ground as its Trading Partners Move Ahead? March 29, 2001.