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While the nation was
mourning the 3,000 lives lost
on the morning of
September 11, 2001,
the financial ramifications
of the terrorist attacks on

In the Wake of September 11: Our Economy and the World

the World Trade Center
and the Pentagon
rippled across the country
and to almost every
corner of the globe



NAFTA: Compensating Business for the Inconvenience of Protecting Public Welfare?

Do certain rules under the North American Free Trade Agreement (NAFTA) require governments to roll back regulations protecting public welfare and to pay compensation to businesses because these regulations have, in some way, adversely affected their investments and profitability? Many critics contend that businesses are using the investment rules under NAFTA in ways never intended to roll back government regulations that diminish their profits. But supporters argue that NAFTA investment rules have encouraged the flow of needed private capital which helps to create jobs and increase economic activity in the host country, and have painted opponents as scaremongers reflexively opposed to any open trade and investment.

Both supporters and detractors of NAFTA investment rules say that the debate is reaching a higher pitch as representatives from almost every country in the Western Hemisphere have started negotiations to include these rules in an all-encompassing Free Trade Agreement of the Americas (FTAA) which will essentially expand the NAFTA agreement throughout the hemisphere. Will these investment rules help to expand economic prosperity or will it roll back laws protecting public welfare in order to benefit business?

NAFTA Chapter 11: An Investor's Bill of Rights?

NAFTA, a free trade agreement second in importance only to the treaties underlying the European Union, is designed to liberalize trade and investment (i.e. open up more sectors of an economy to competition and investment) for Canada, Mexico, and the US by progressively eliminating

almost all barriers to trade by the year 2003.

The actual NAFTA agreement itself is divided into many chapters governing the rules of trade among the three nations in such areas as telecommunications, financial services, and intellectual property. Chapter 11 of the NAFTA agreement deals specifically with the rules governing investment matters. These rules were created to promote foreign investment and commercial development by reducing the risk of investing in another NAFTA country. Several decades ago, after some countries such as Mexico had expropriated American property, foreign investors began to lobby for stronger rules (such as those in Chapter 11) to protect their future cross-border investments.

Under Chapter 11, private investors from a NAFTA country (the US, Canada, and Mexico) are given several rights (such as the right to transfer profits out of the host state) when they invest in another NAFTA country. Chapter 11 also lays out the obligations of NAFTA governments when dealing with investment matters. For example, under the concept of "national treatment," a host government must not give foreign investors and their investments less favorable treatment than that accorded to domestic investors and their investments under like circumstances.

The most controversial provision in Chapter 11 prohibits a host government from directly or indirectly expropriating (or "taking") a foreign investment without providing compensation unless the expropriation was carried out for a bona fide public purpose (such as protecting human health or the environment). International law scholars generally agree that a state does not have to pay compensation for the loss of property or economic activity as a result of implementing regulations protecting the public welfare if these regulations are not discriminatory in nature. But the expropriation provision has stirred up controversy because it does not explicitly define the kinds of government actions which would constitute an expropriation of an investment. In fact, analysts say that legal circles in the US still vigorously debate this point in domestic legal matters.

More power for private investors?

Chapter 11 also provides a dispute settlement process (popularly known among policymakers and activists as the "investor-state" dispute settlement process) which is initiated directly by a private investor of a NAFTA country against a host state (i.e. the country where the investment is made). A private investor may bring a claim if it believes that a breach in a government's obligations under Chapter 11 has caused harm to its investment.

The dispute settlement process takes place in the form of arbitration where disputing parties submit their disagreements to an impartial body for a legally-binding decision. Arbitration proceedings are generally less adversarial than courtroom settings, less expensive, and provide more privacy to the disputing parties. Observers say that the proceedings are designed "to protect the commercial privacy of the litigants." The public is excluded unless both

Continued on next page

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Founded in 1996, the Center for International Law supports teaching and research in all areas of international law, and concentrates on the law of international trade and finance. The Center organizes events whereby students, faculty, and guests of New York Law School may interact with experts who link theory and practice.



Many anti-globalization protestors say that NAFTA requires governments to compensate businesses if certain regulations affect their profitability. Supporters of NAFTA argue that these protestors are reflexively opposed to any kind of open trade and investment.

parties agree to allow the public to attend its proceedings, which almost never occurs. Private investors can choose from arbitration proceedings currently available under the auspices of the United Nations Commission of International Trade Law or the International Center for the Settlement of Investment Disputes, both of which were established in 1966 to resolve commercial disputes.

A three-person tribunal settles disputes by interpreting the rights of investors and obligations of governments under Chapter 11. All decisions rendered by a tribunal are final and generally not subject to review unless the tribunal committed fraud or exceeded its jurisdiction. If the government is the losing party in the dispute, the tribunal could order the government to pay compensation for any breaches of Chapter 11 provisions.

In the entire NAFTA agreement, only Chapter 11, concerning investment, allows a private individual or company to file a claim against a NAFTA government. All other disputes arising under NAFTA can only be brought by one government against another government. On the other hand, a NAFTA host government cannot initiate the investor-state process against a private investor. (But an investor is still subject to the laws and regulations of a host state.) Furthermore, the investor-state process does not apply to investors making investments in their home states. In a case where, say, American investors believe that certain US regulations have harmed their investments, they will have to file their grievances with an American court.

The case for and against Chapter 11

Many critics say that when the Parties to NAFTA had created Chapter 11, it was intended to be used as a last resort "aimed at protecting an investor through extraordinary means in extraordinary circumstances," and they usually cite cases where a host government expropriates investments and

property from private investors. But now, these critics claim, large corporations are using Chapter 11 to "fend off proposed new regulations, lobby for or against specific government actions, and generally to preserve or gain a competitive position."

Pointing to recent tribunal decisions, opponents of Chapter 11 say that many companies are demanding compensation for alleged damages to their investments caused by regulations protecting public health and safety, which have typically been viewed outside the scope of expropriations. One critic asked hypothetically: "At what point do high environmental standards become an expropriation affecting a business and its profits?" Critics also contend that the public is left in the dark about tribunal decisions because governments have no legal obligation under Chapter 11 to announce notices of arbitration. In fact, as of last year, none of the NAFTA governments had made public any of the documents from these arbitration proceedings. Critics also argue that it is troubling for private arbitration bodies to take up issues of public concern, especially if public money compensates private investors.

Critics also claim that tribunal members are not accountable to anyone. Unlike, say, the dispute settlement process under the World Trade Organization where an appellate body can review decisions by a lower panel and all decisions are reviewed by the full WTO membership sitting as the Dispute Settlement Body, all decisions rendered by a NAFTA tribunal are final and generally not subject to review. Critics also point out that the mere threat of filing a claim under Chapter 11 has chilled the passage and enforcement of environmental laws and other regulations designed to protect the public welfare.

Supporters counter that Chapter 11 has helped to increase prosperity in all NAFTA countries, especially Mexico, by providing a more predictable environment for investors (which, in turn, leads to more investment and jobs). They also point out that detractors of Chapter 11 (whom they describe as anti-globalization protestors) are generally opposed to any open trade and investment anyway. And without the private arbitration proceedings available under Chapter 11, supporters say that disputes would be drawn out in full public view and force the disputing parties to take rigid stances which they might not have taken otherwise.

Others also point out that small- to medium-sized companies (and not large multilateral corporations) have overwhelmingly used the dispute settlement process under Chapter 11 and that there is no direct proof that simply threatening to use this process has chilled the passage of government regulations.

Both supporters and detractors sometimes point to the very same cases to support their claims concerning Chapter 11. Since 1994, investors have filed 22 cases. Three of the better known cases reveal that the expropriation provision has stirred much debate over whether Chapter 11 is being abused, as critics contend, to overturn public welfare regulations for the benefit of business.

Continued on page 15

IN THE WAKE OF SEPTEMBER 11: OUR ECONOMY AND THE WORLD

In the wake of the destruction of the World Trade Center and parts of the Pentagon, policymakers and economists began the process of determining and preparing for the short- and long-term effects of the terrorist attacks. While people were mourning the 3,000 lives lost on the morning of September 11, 2001 (including the lives of two New York Law School graduates), the financial ramifications of the attacks rippled across the country and to almost every corner of the globe.

Most economists now believe that the attacks had further damaged an American economy which had, months before, slipped into a recession (the first in a decade). And the many countries that had depended on the American consumer to buy their goods and services have seen their fortunes decline along with the US economy. Although the financial effects of the attacks have been substantial (for example, consumer spending dropped and unemployment increased), policymakers are now discussing when and how strongly the US economy will jump back. This section of the newsletter provides a broad overview of how the US and other regions of the world were affected by and responded to the attacks in the days and months after September 11, and how the attacks will affect the US and world economy.

AN ALREADY-WEAK ECONOMY FALTERS AFTER THE ATTACKS

There is a general consensus among economists and policymakers that the economy had already gone into a recession well before the terrorist attacks, and that the attacks may have only prevented a quick turnaround and recovery. In the words of one commentator: "The terrorist attacks of September 11 knocked the wobbly legs out from under an already shaky economy."

Several signs pointed to a slowing economy prior to the attacks. Compared to the previous year, imports bought by US consumers had dropped 15 percent in the three months prior to the attacks. Unemployment had also jumped to 4.9 percent in August 2001 from 4.5 percent the previous month, which exceeded analyst expectations. Collection of state sales tax revenues across the country fell by \$5 billion in the three months before the attacks. And new home construction in August 2001 fell almost seven percent from the month before. Consumer confidence polls (which serve as a psychological measure of people's feelings about the health of the economy) also dropped in early-September to their lowest level since 1993.

The National Bureau of Economic Research (NBER), a nonprofit organization which has been tracking business cycles for several decades, later confirmed that the economy had, indeed, gone into a recession in March 2001, ending the longest economic expansion in American history – exactly ten years after it started in 1991. Rather than using the popular definition of a recession (two consecutive quarters of decline in the nation's gross national product), the NBER examines broad economic indicators in employment, personal income, industrial production, and manufacturing and trade sales.

A RECESSION UNLIKE OTHERS

Recessions in the past 25 years usually began with the Federal Reserve increasing interest rates in order to cool down an overheating economy. As consumer spending declined in response to higher rates and businesses saw a drop in their profits, the manufacturing sector of the economy would cut business investment and begin worker layoffs. But the current recession began first with a decline in the output of the manufacturing sector, which comprises companies making and distributing essentially everything that is used everyday such as heavy machinery, plastics, furniture, paper products, and computer discs.

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End of the party: The recession in 2001 was the first in a decade and ended the longest economic expansion in American history. There have been 10 recessions since 1945, and most have lasted for an average of 11 months. According to one commentator, the terrorist attacks on September 11 "knocked the wobbly legs out from under an already shaky economy."

Many analysts believe that soaring business investment in the latter half of the 1990s (which created hundreds of thousands of jobs) had built up an excess of goods for which demand had dropped as soon as the stock market began faltering in March 2000 (led by the steep decline in technology stocks). During the late-1990s, business spending grew at more than 10 percent a year but fell almost 12 percent in the months before the September attacks. Many companies realized that they had hired too many workers and equipment in expectation of an ever-growing economy. Said one analyst: "Most economists now blame companies' misplaced optimism and zealous over-investment during the final years of the boom for the current collapse."

As a result of this over-investment, the manufacturing sector cut production and began to lay off workers. In fact, US manufacturing activity shrank for 15 consecutive months beginning in August 2000. And since March 2001, this sector of the economy had cut 1.8 million jobs. Yet, despite this decrease in manufacturing activity, economists pointed out that consumer spending (which accounts for two-thirds of the economy) continued to rise and essentially supported not only the US economy, but other economies abroad which depend on American consumers to buy their goods. But for the economy to recover, they say, the manufacturing sector must begin investing again.

WHEN WILL THE US ECONOMY BOUNCE BACK?

Many economists agree that the course of the US economy (and the world economy in general) will depend on how the American government, businesses, and consumers respond to terrorist threats. Fears of a prolonged conflict against suspected terrorists (which could have continued to dampen consumer confidence and spending) quickly abated in early December 2001 as the US military quickly dislodged and captured many terrorist elements in Afghanistan.

In the days and weeks after September 11, the US government quickly introduced several confidence-building measures to shelter the economy from the immediate effects of the attacks. For example, the Federal Reserve made billions of dollars available to banks in case any faced credit problems, and it later cut interest rates to their lowest levels in decades. The US Congress passed a \$40 billion emergency aid bill to assist recovery efforts and to fight a global war against terrorism. Whether these measures will bolster consumer and business confidence still remains to be seen.

But so far, leading economic indicators have shown a mixed picture on whether the US economy will bounce back quickly. The unemployment rate across the country increased to 5.6 percent in January 2002 (from 4.9 percent in September 2001) and is expected to rise to 6.5 percent by the middle of this year. One economics research group reported that approximately 248,000 jobs around the country had been lost as a direct result of the attacks in 2001, and that another 1.6 million people would lose their jobs this year. Analysts also predict that while most municipal economies should rebound later this year, New York City will not begin its recovery until 2004.

Although consumer spending had its biggest drop in more than 15 years in the month after the attack, it later went up and down like a seesaw as retailers offered huge discounts on their merchandise. By the end of November 2001, the New York Stock Exchange had regained all of its losses in the days following the terrorist attacks. The Dow Jones Industrial Average even surged passed the 10,000 mark in December 2001, leading some analysts to declare – perhaps prematurely – a quick end to the recession. In a sign that the economy may be improving, officials point out that the economy actually grew one percent in the last quarter of 2001. The Federal Reserve also held steady its benchmark rate in late January 2002, but it still indicated that business activity remained "soft" across the US and that any recovery would begin in late summer 2002. The remainder of this section will describe some immediate effects of the terrorist bombing and how the US and other countries responded to the attacks.

Continued on next page



On September 14, 2001, Congress passed a \$40 billion emergency spending bill to help New York and other areas recover from the terrorist attacks and to fight a war against terrorism. The most the government had previously given out in federal disaster aid was \$7 billion to Northridge, California, in 1994, to help that city recover from an earthquake.



According to one economics research group, New York City will reportedly lose 150,000 jobs, Los Angeles 69,000 jobs, and Chicago 68,000 jobs this year as a direct result of the terrorist attacks. New York City had already lost over 100,000 jobs last year. But analysts say that many of these positions will be restored as the economy improves.



In addition to the many industries floundering as a direct result of the attacks, the US Postal Service (USPS) also asks for a government bailout. An anthrax scare cost the USPS \$300 million in lost revenue as fewer people used the mail. The USPS also spent millions of dollars on security measures to detect and destroy the deadly bacterium. Many policymakers expect the price of a first-class stamp to rise to 37 cents by this summer.



In the weeks following September 11, market capitalization of securities listed on the New York Stock Exchange dropped more than \$1 trillion (out of a total of around \$11 trillion). The Dow Jones Industrial Average eventually regained all of its September 11 losses. According to one think tank: "The attacks did very little real damage to the US capital markets or their ability to generate income and wealth."

THE FEDERAL RESERVE SWINGS INTO ACTION

A few hours after the attack on September 11, the Federal Reserve Bank (which is the nation's central bank) released a two-sentence press release stating: "The Federal Reserve System is open and operating. The discount window is available to meet liquidity needs." This essentially meant that the government would make money available to banks and other financial institutions (in the form of low-interest, overnight loans) in the event that panicky investors, depositors, and large institutional investors quickly withdrew large amounts of money from their accounts or if banks had trouble making or receiving payments. In less than a week, the Federal Reserve had made over \$175 billion available to the banking system.

Since September 11, the Federal Reserve has lowered short-term interest rates four times to 1.75, which is the lowest in 39 years. (The short-term rate was six percent at the beginning of 2001.) It decided to keep rates steady in January 2002, citing improving economic conditions. In order to stimulate the economy or prevent a downturn, the Federal Reserve lowers short-term interest rates which then makes it less expensive for consumers and businesses to borrow money, although many people point out that it takes months or sometimes a year for the economy to feel the effects of any changes. Some economists have also argued that lower interest rates won't address a major problem in the economy – over-investment by companies during the late-1990s.

CONGRESS PASSES \$40 BILLION EMERGENCY AID BILL

Three days after the terrorist attacks, the US Congress passed a \$40 billion emergency spending bill to fight a war against terrorism and also to help New York and the Pentagon recover from the attacks. President Bush promised that half the money (or about \$20 billion) would go toward reconstruction efforts, especially in New York. Under the terms of the emergency bill, President Bush would decide how to spend \$10 billion himself and then another \$10 billion with 15 days' notice to Congress. Congress would allocate the remaining \$20 billion with recommendations from the President.

STOCK MARKETS PLUNGE, THEN RECOVER

The New York Stock Exchange (NYSE), where listed securities have a combined market value of almost \$11 trillion (making it the largest stock exchange in the world), closed for four business days after the September 11 attacks. The NYSE last closed in March 1933 (for almost 10 days) when bank regulators had to identify insolvent banks in the midst of the Great Depression. The Dow Jones Industrial Average (or "average") – which measures the stock performance of thirty companies that represent different sectors of the American economy – closed at 9605.51 on September 10. No NYSE average is available for September 11. Other stock exchanges in Europe, Latin America, and Asia halted trading early after the attacks but not before seeing their averages decline sharply.

When the NYSE reopened on September 17, 2001, the average declined by seven percent (or 684.81 points), surprising many analysts who expected a much steeper decline in the wake of the attacks. During heavy trading, investors sold the stocks of those companies whose financial interests they believed were the most vulnerable to the attacks, especially those in the insurance, airline, and financial services industries. Indeed, the stocks of many of these companies saw percentage decreases in the double digits. Despite further declines, the average soon surpassed the 10,000 mark on December 5, 2001. Most other stock markets around the world had also regained most of what they lost on September 11. Many analysts point out that while Lower Manhattan suffered the brunt of the terrorist attacks, "the infrastructure and equipment which allows for trading and other transactions had remained largely intact."

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FROM A SURPLUS TO A DEFICIT IN THE TENS OF BILLIONS

Since 1998, the US government had been running a budget surplus in the hundreds of billions of dollars (i.e. the government collected more in taxes and revenue than it actually spent, which had not happened since 1969), and budget forecasters expected these surpluses to run for the next ten years. Much of the surplus actually consists of Social Security tax revenues which policymakers have promised not to use for any other purpose short of financing a war or other national emergencies.

In the months after September 11, the White House announced that the attacks (in combination with the economic downturn) would reduce future surpluses and create budget deficits for at least the next three fiscal years. Some of the unexpected expenses arising from the attacks include: the war in Afghanistan (which cost almost \$2 billion a month); the recovery and disaster relief efforts; and increased spending on security measures, unemployment payments, and welfare benefits. The administration also anticipated a drop in the collection of income tax revenue because of the declining economy. The government is expected to use at least \$262 billion of the Social Security surplus this year to run general operations.

For the current fiscal year, Congress estimates a deficit of at least \$15 billion (meaning that at least \$15 billion in expected revenues won't materialize). This is down from a surplus of \$127 billion in fiscal year 2001 and \$236 billion in fiscal year 2000. Currently, the US government has a *debt* of \$3.3 trillion (which reflects the net total of all past *deficits*).

EFFECTS OF THE ATTACKS RIPPLE THROUGHOUT THE STATES

As a direct result of the terrorist attacks and the already-declining economy, states across the country have been cutting their current year budgets to make up for anticipated shortfalls in sales, income, and corporate tax revenues. (Every state - except Vermont and the US government - has statutory or constitutional requirements for its legislature to pass and maintain a balanced budget.)

According to the National Conference on State Legislatures, 43 states have seen the collection of tax revenue drop below forecasts; 37 states have lost more jobs than they gained between March and November 2001; and 36 states have made budget cuts because of anticipated shortfalls in the current year budget. These budget cuts, which could total over \$15 billion, have caused reductions in city services and government programs.

Many states are also facing unforeseen expenses in the form of additional security measures (such as overtime for police and emergency workers) to protect government buildings and airports from possible terrorist threats. The National Governors' Association estimates that states will have to spend an additional \$10 billion during the current fiscal year for these measures. While the federal government has indicated that it might help the states defray some of these costs, most political analysts say otherwise since the government itself is running a deficit.

THE AIRLINE INDUSTRY: GROUNDED AND GOING BANKRUPT?

Immediately after the attacks, the US government grounded all commercial flights for two days. According to the Department of Transportation, the cancellation of flights and reduction in passenger bookings cost each major airline over \$250 million a day in lost revenue and increasing maintenance costs. With the industry quickly using its cash reserves and facing the risk of bankruptcy, every major airline announced worker layoffs which soon reached 70,000 people over a course of 11 days after the attacks. Flight attendants argued that the ensuing airline layoffs were politically motivated to pressure Congress into creating a bailout package for the airline industry. Airline executives estimated that the industry will lose between \$18 and \$33 billion over the next 18 months as a direct result of the terrorist attacks.

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After being closed for four working days, the New York Stock Exchange reopened to significant losses for the airline, insurance, and financial services industries which were seen as most vulnerable to the attacks. Metlife fell 6.5 percent; Morgan Stanley dropped 13 percent; and US Airways plunged 52 percent. On the other hand, sales of US flags, guns, and picture books of the World Trade Center increased.



The US government grounded almost all flights in the US soon after the attacks. On the afternoon of September 13, 2001, there were about 250 commercial aircraft flying over US skies. There are normally around 6,000 planes in the air on any given afternoon.



In providing extra security after the terrorist bombings, veteran New York City police officers each earned an average of \$50,000 in overtime pay. In 2001, the city paid over \$1.7 billion in overtime as a direct result of the attacks.



Despite large losses in 2001 as a direct result of the terrorist attacks, prospects for the insurance industry are expected to improve. In addition to increasing premiums rates to reflect the costs of the attacks, insurance companies are expected to raise over \$25 billion from the private investment market to expand operations and create new insurance companies.

Lobbyists for the industry soon demanded a government rescue plan, arguing that because commercial aviation supported many other businesses such as hotels and car rental agencies, a bankrupt airline industry would further hurt an ailing US economy. Others dispute this assertion, pointing out numbers from the Commerce Department showing that the industry and its satellite businesses make up only four percent of the \$11 trillion American economy.

Congress soon assembled a \$15 billion bailout package for the industry, which included \$5 billion in cash to cover immediate losses and \$10 billion in bank loans (which are not fully guaranteed – meaning that taxpayers may not foot the bill in case an airline cannot repay its loan). Responding to critics who cried corporate welfare, Congress argued that because the fortunes of the airline industry had dropped so quickly, a bailout was necessary, in part, to boost public confidence. Under the terms of the package, only those airlines presenting viable business plans and willing to compensate the government for the loans in the form of fees or securities would be given preference. To date, the government has given tentative loan approval to one airline, America West, but only after it had exacted an option to buy one-third of that airline's equity.

THE INSURANCE INDUSTRY: A GLUE BECOMING UNSTUCK?

In the weeks after the attacks, the reinsurance industry – which is also known as the "insurers for the insurance industry" because it backs up primary insurers or acquires a portion of their coverage – announced that it would no longer offer terrorist coverage unless the government helped the industry absorb the costs of future attacks. This, says the industry, will allow them to set reasonable terrorist insurance premiums in the future.

Supporters of the industry also say that without terrorism coverage, banks and other lending institutions would refuse to make loans for large-scale projects in construction, transportation, manufacturing, and real estate. One member of Congress referred to insurance as "the glue that holds our economy together." Analysts estimate that the insurance industry will pay out between \$40 to \$50 billion over the next few years for claims arising from the September 11 terrorist attacks, dwarfing the estimated \$20 billion in federal aid to New York and \$1 billion in contributions raised by the Red Cross and other charitable organizations.

While not dismissing the importance of insurance outright, many critics scoff at the notion that the economy will collapse without terrorism insurance. They argue that the insurance industry simply needs to update their financial models to calculate the probability of new terrorist attacks and then price their new policies accordingly. Although these critics point out that the insurance industry is quite healthy (having over \$300 billion in capital for all property and casualty claims), the industry argues that more large-scale terrorist attacks in the future could quickly drain its resources. Legislation to help the insurance industry, which included long-term federal loans to manage future terrorist losses, was bottled up in Congress at the end of 2001.

Despite losses last year, analysts expect the earnings for the insurance industry to rise sharply next year. Premiums are expected to rise at an annual rate of 10 to 15 percent to reflect the costs of the terrorist attacks.

AN ECONOMIC STIMULUS PLAN FIZZLES IN CONGRESS

Fearful that the terrorist attacks had deepened the downturn in the economy and that interest rate reductions on the part of the Federal Reserve were not having a fast enough effect, Congress began working on a "economic stimulus package." Some elements of this plan included giving tax credits for new business investment; extending unemployment benefits beyond the customary 26-week limit; and accelerating the tax cuts passed in June 2001. (This stimulus package would be separate from the \$40 billion emergency aid bill to fight the war against terrorism and to help in the recovery efforts, and also separate from the \$15 billion aid bill to help the airline industry.)

Continued on next page

Critics of the stimulus plan argued that it would imperil the long-term health of the country by creating larger deficits through more tax cuts and increased spending, which could then raise long-term interest rates (such as those for mortgages). Many economists also noted that the economy may revive on its own without an economic stimulus. The proposed stimulus package fell apart at the end of December 2001 when Democrats and Republicans in Congress were unable to reach a compromise over whether the government should provide health insurance subsidies for people who lose their jobs. Recent Congressional efforts to pass a new stimulus package have failed. But Congress did agree to extend unemployment benefits for several weeks beyond the regular limit.

WHAT HAPPENED AT GROUND ZERO IN NEW YORK?

Although the terrorist attacks on September 11 affected almost every state and municipality across the country, New York City and the surrounding tri-state area obviously suffered the most severe physical and economic damage. While New York Law School did not suffer any structural damage to its buildings as a result of the attacks, it lost two graduates. Classes were cancelled on September 11 and did not begin again until September 24.

In the weeks after the attacks, the New York State Department of Labor estimated that more than 115,000 workers in New York City would lose their jobs during the current fiscal year as a result of the terrorist attacks. In fact, the city had lost over 79,000 jobs in October 2001 alone, which surprised government officials who were expecting these losses to occur over a period of several months. The city's unemployment rate increased to 6.9 percent in November from 6.2 percent in October.

City officials estimate that, during the current fiscal year, New York City will lose over \$1 billion in revenues as a direct result of the terrorist attacks (mainly coming from a decline in income, sales, hotel, and other tax revenues). To make up for this budget shortfall, New York City announced a 15 percent across-the-board cut in every city agency budget. Under current laws, the city must balance its budget for each fiscal year. City officials also estimate a deficit of over \$4 billion for the 2003 fiscal year. (New York City currently has outstanding loans totaling over \$42 billion, most of which is for loans taken out to improve the structural quality of roads and bridges.)

In October 2001, the comptroller (who is the city's chief financial officer) issued a report estimating that the terrorist attacks would cost the city over \$105 billion over the next two years. Some critics have pointed out that it was in the city's best interest to make the final tally as high as possible so that city and state officials would be able to ask for more federal aid. Other groups estimated the losses at around \$83 billion.

Economists and analysts say that the three main engines driving the city's economy – retailing, financial services, and tourism and entertainment – would be badly hurt in the aftermath of the attacks. The retail sector is forecast to lose \$15 billion this year. And according to the New York City Partnership, the city's travel and tourism industry will lose up to \$13 billion in revenue and see the elimination of 25,000 jobs by 2003.

The financial services industry (located mostly near the Wall Street area next to the World Trade Center) had already begun to shed tens of thousands of workers before the attacks as a result of hiring during the economic boom of the 1990s. Although the financial services industry makes up only five percent of total city employment, it provides over 15 percent of the city's annual tax revenue. And with further anticipated layoffs, the city's income tax revenue is expected to decline as a result.

President Bush promised to give \$20 billion in recovery aid to New York City in the days after the attacks, but it wasn't until after much wrangling that Congress finally gave New York City \$8.2 billion in aid in December 2001, which will be used for grants and loans to small businesses, compensation for hospitals, and general recovery efforts. Although the Bush administration said that it will eventually give the remainder of the \$20 billion, it did not suggest a timetable.

Continued on page 12



The leaseholders of the World Trade Center sought \$7 billion in claims against insurance companies, arguing that each of the two hijacked planes constituted a separate attack covered by a \$3.5 billion policy. Insurance companies argue that the two attacks were a "single insurable incident" worth only \$3.5 billion. A settlement seems likely.



Workers most badly affected by the terrorist attacks have been low-wage earners such as janitors, cashiers, waiters, and drivers. A labor-backed think tank estimated that 60 percent of the jobs lost (as a result of the attacks) paid an average salary of \$23,000. The news is different for Wall Street. Despite the terrorist attacks, the economic downturn, and the mass layoffs in the financial industry before and after the attacks, 2001 will still be the fourth or fifth most profitable year in Wall Street history.

WTO to Begin New Trade Round: "A Perfect Balance of Unhappiness"



Against the backdrop of a war in Afghanistan and a slowing world economy, the member nations of the World Trade Organization (WTO) agreed to begin a new round of multilateral trade negotiations (the first in eight years) to bring down tariffs and other barriers to global trade.

During its ministerial conference in Doha, Qatar, in November 2001, WTO member nations signed off on an agenda of issues which will form the basis of actual negotiations beginning in January 2002 and concluding in January 2005. The World Bank estimates that a successful conclusion of new trade negotiations (which have been dubbed the "Doha Round") could increase world prosperity by almost \$3 trillion by the year 2015. The average worldwide tariff stands at 12%, down from 15% in 1994 when the last trade round was concluded.

The WTO is the premier organization setting the rules for international trade and the settlement of trade disputes. Under WTO rules, member nations must hold periodic meetings (called ministerial conferences because the attendees are trade ministers from member nations) at least once every two years to discuss trade matters and review any on-going negotiations. The last ministerial conference, held in 1999 in Seattle amidst anti-globalization protestors, ended in failure as WTO member nations failed to agree on an agenda for new trade negotiations.

The last major trade round (called the Uruguay Round after the country where negotiations were initiated) was completed in 1993 and has been described by policymakers as the largest trade negotiation in history. The Uruguay Round covered negotiations (and lowered tariffs) in almost every area of trade in goods, and also in new areas such as intellectual property and trade in services. This round also reformed the world trade system by creating the WTO and revising procedures for resolving trade disputes among member nations. Policymakers and critics had often sought to make the WTO's predecessor, the General Agreement on Trade and Tariffs, more effective in resolving trade disputes.

From the beginning of the talks in Doha, policymakers have said that WTO member nations faced heavy political and public pressure to agree to new trade talks in order to revive a faltering world economy further weakened by the

terrorist attacks in New York on September 11, 2001. For the first time since the 1970s, every major industrial region of the world (i.e. the US, Europe, and Japan) faced a simultaneous economic downturn. The last ministerial meeting held in Seattle failed, in part, because many WTO members refused to put on an agenda for future negotiations any issue deemed important to influential domestic lobbies.

For example, under pressure from powerful farm lobbies, the nations of the European Union (EU) refused to negotiate an end to export subsidies for their farm products. The US, under pressure from steel unions, refused to discuss their use of antidumping provisions which allow the US to sanction trading partners who allegedly sell merchandise (such as steel) below their cost of production. Developing nations, many of whom are still struggling to comply with basic WTO obligations and commitments, refused to agree to a new trade round unless the WTO agreed to a "development round" to address their concerns first.

Against an uncertain economic landscape following the events of September 11, many WTO member nations made several (and, some would say, painful) concessions to bring the ministerial conference to a successful conclusion. One Japanese trade official described the final declaration and agenda as a "perfect balance of unhappiness" for all sides. While many of the concessions may have seemed to disappoint the many domestic lobbies trying to shield their businesses from foreign competition, policymakers point out that these concessions were padded with language intended to provide political cover for the negotiators.

At the conclusion of the meeting, the US said that it would be willing to "clarify" the use of its antidumping rules during future trade negotiations, but stressed that it would keep these provisions in place since they are compatible with WTO rules and also help to shield US industries from unfair competition from abroad. And while the EU agreed to discuss the "phasing out" of export subsidies for Europe's agricultural products, it noted that this concession would not "prejudge" the outcome of future negotiations (meaning that the EU could, after all, decide to maintain its export subsidies at a later date). Developing nations say that while they gained little from the ministerial meeting, they succeeded in clarifying whether the intellectual property rules under the WTO allowed countries to break drug patents to address public health crises. (See the "Global trade round-up" on page 17 for more details.)

In addition to these issues, the Doha Round will begin negotiations in other areas including: services; intellectual property; investment; competition policy; electronic commerce; and technology transfers. Members of the WTO will review the pace of negotiations in the Doha Round at the next ministerial meeting in Mexico in 2003. ❖

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NYLS Alumnae Profile

Name and Year: K. Elizabeth Ryder '93, consultant, international legal development.

Describe your work and responsibilities: I work in the field of "International Legal Development," which means I liaise with governments, bar associations, and non-governmental organizations to reform legal systems and legislation. Most of the projects I undertake are in crisis areas or countries where the legal regime is weak or unable to address rapidly changing social or economic needs.

My experiences include developing a Judicial Training Center, with the American Bar Association, to guide judges in the former Soviet republics through new legislation and legal practices. We examined, for example, laws on commerce, freedom of expression, and criminal rules of evidence. I worked to develop the curriculum; identify lecturers; and establish links with similar institutions in Central Europe and France. With the United Nations, I coordinated the development of forty Legal Aid Centres in Bosnia and Herzegovina that provide legal services to displaced persons and refugees trying to return to their pre-war homes. As part of my work, I also developed legal strategies to present claims to the Human Rights Chamber (an extension of the European Court of Justice in Strasbourg).

The field of international legal development has grown dramatically since the disintegration of the Soviet Union, and new programs were developed to share western expertise. Funding for such programs is provided largely by governments and inter-governmental organizations, and partly by private foundations and charities. The United States Agency for International Development (USAID), for instance, works with recipient-governments to develop programs that support democracy and free markets. USAID then outlines broad programmatic goals; allocates funding; and solicits bids from American non-profit or private consulting groups to implement the actual projects, which include everything from the development of new tax legislation to gender issues research. Most employment opportunities are found with such consulting groups, some of which include:

American Bar Association/Central & East European Law Initiative; America-Mideast Educational and Training Services; American Refugee Committee; Associates in Rural Development, Inc; Civic Education Project; Checchi and Company Consulting, Inc; Chemonics International, Inc; DPK Consulting; International Rescue Committee; Institutional Reform of the Informal Sector; and Nathan Associates. All of these groups have Internet webpages.

For those "in the field," your work might focus on legislative reform; streamlining court administration; strengthening independent bar associations; or developing non-governmental legal organizations. Back at the home-office, positions typically involve monitoring developments in the field; coordinating regional work; modifying programs to reflect changes in the political climate; and designing future programs that build on the reforms already in place. Generally, you gather experience in the field, where positions vary from three months to several years, and then apply for more secure positions in the US.

While exciting, this career is also quite challenging. Living within a society that has experienced radical change through war, economic collapse, or a fundamental transformation of government presents obvious hardships. Aside from a chronic lack of basic amenities, working with counterparts unfamiliar with legal ethics can test our traditional notions of right and wrong. It can also be tricky to juggle short-term work contracts, student loans, and family – especially if you have to relocate with little notice.

Career advice for NYLS students: The first step is to choose an area of law or region of the world that interests you. If you are concerned with human rights, I suggest you contact watchdog groups (such as Human Rights Watch) that report violations occurring around the world and organizations addressing the violations. If you prefer commercial matters, keep your eye on the USAID web page for interesting projects and find out which consulting groups have been contracted to implement the project. Language is a plus but not a prerequisite. If you can find volunteer or internship positions, apply. Getting your foot in the door is the most difficult step.

I have found most positions through personal contacts (made by attending seminars, networking, and requesting informational interviews) and general job postings. There is a relatively small cadre of lawyers moving through these projects and we often hear about open positions from one another. I also review several computer list-serves. Three particularly useful sites are: CEEJOBS (Central and Eastern Europe); NISJOBS (Newly Independent States); and DEVJOBS (Development). All three are part of the Yahoo groups network (groups.yahoo.com). You simply sign up and check postings at your convenience.

And remember that grades are important, but not decisive. International legal development requires someone who can see the obstacles (legal, political, and cultural); develop strategies to overcome them; and make reliable and progressive local contacts who can carry on the work when you leave. These skills are not reflected in your grades, and employers realize that. Personally, I have found this work rewarding and very interesting, but you have to be ready to move quickly and hit the ground running. As you can imagine, plans are already being laid (and recruiting has begun) for reform work in post-Taliban Afghanistan. ❖

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For the first time since the 1970s, the United States, Europe, and Asia are experiencing a simultaneous economic downturn which was further exacerbated by the terrorist attacks. The US recession (which began in March 2001) was followed by a Japanese and German recession by the end of last year.



The US prohibited almost all foreign flights (and trade) to the US for five days after September 11. Airplanes carry more than 40 percent of Japan's exports to the US. States bordering Mexico complained that extra security measures created waits at the border lasting for hours and prevented thousands of Mexican consumers from shopping in the US, costing businesses millions of dollars in lost revenue.

In February 2002, after repeated efforts by the New York Congressional delegation to secure a timeline as to when the state would receive more federal aid, the White House budget director accused New York politicians of "money-grubbing." President Bush later traveled to New York and declared: "When I say I'm going to do something, I'm going to do it," referring to his promise of \$20 billion in aid. Still, political analysts say that efforts to secure aid for New York are losing steam among politicians who argue that victims in the Oklahoma City terrorist bombing in 1995 have gone without substantial federal aid. On the other hand, residents and businesses in New York City are expected to receive over \$40 billion from private insurance companies over the next few years.

WHAT HAPPENED ABROAD?

Although the attacks occurred in the US, their effects were felt all over the world as many countries have come to rely on the American economy to pull along their own economies. Even those countries not dependent on the US for trade have seen their trading partners experience downturns as a result of the slowdown in the US.

CANADA AND MEXICO

Because of their proximity and strong ties to the US (especially after the passage of the North American Free Trade Agreement in 1994), both Canada and Mexico have come to rely on the American economy to fuel their growth. The recent downturn in the US has led to a corresponding decline in those two economies. One analyst described Canada and Mexico's dependence on the US as so complete that "they are now essentially powerless to do much but wait for the US economy to get going again." Government figures reveal that over 85 percent of Canadian and Mexican exports go to the US, making up over 25 percent of the gross national product of each country.

In the immediate aftermath of the terrorist attacks, US Customs officials stepped up border inspections to verify the identities of all visitors. Trucks carrying merchandise and other goods endured waits of up to three or four hours to enter the US. Some border points in Canada saw waits of up to 15 hours which then increased the price of goods as many customs brokers and freight forwarders instituted a small surcharge for the delays. Months later, the Canadian government said that although the new security measures did hamper trade between the US and Canada, it had no significant economic impact.

The Bank of Canada (which is the equivalent of the Federal Reserve in the US) has lowered its interest rates twice since September 11, to 2.25 percent, to prevent any downturn from entrenching itself in the economy. But unlike the US which is trying to spend its way out of the recession through a variety of aid packages, Canada (like Europe and Japan) decided not create a broad array of spending programs. The unemployment rate in Canada later increased to 7.5 percent (compared to 5.8 percent in the US at the start of 2002), and the stock exchange in Toronto ended down 20 percent last year.

In the aftermath of the attacks, Mexico saw a decrease in direct foreign investment which it has come to rely upon for creating new jobs and investment opportunities in the country. But analysts see Mexico as providing a safer investment environment than its neighbors in Latin America because its economy is closely integrated with the US economy. Despite the current downturn, the Mexican stock market actually closed up 19 percent last year.

EAST ASIA

Many countries in this region have come to rely on the US to buy their exports, and view the American economy as its "best customer, biggest market, and key investor." But any downturn in the US would also lead to a corresponding decline in East Asia. For example, Taiwan depends on exports for 50 percent of its total economic output, while Singapore depends on exports for 90 percent of its output.

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Recent figures show that the US imported over \$400 billion in goods from East Asia in 2000. Many economies in the region were already experiencing a downturn before the terrorist attacks, with analysts citing weak demand for Asian exports, especially electronic consumer goods.

In the hours after the attacks, the stock markets in Japan, Hong Kong, Korea, and Taiwan fell substantially. The Tokyo Stock Exchange fell below its 10,000 mark for the first time in 17 years. Although most of the exchanges regained their losses in the next few weeks, over half of all major stock markets in East Asia had closed down last year. Japan's markets were down 29 percent for the year; Hong Kong 21 percent; and Singapore 20 percent.

Another immediate effect of the attacks was an abrupt curb in trade between East Asia and the US. In the hours after the attacks, the Federal Aviation Administration (FAA) prohibited all foreign airlines from entering the US for five days. When the FAA later allowed international flights, it prohibited passenger planes from carrying any cargo when entering US airspace. Almost half of all goods shipped by air from Asia are loaded onto passenger planes. Japan alone ships over 40 percent of its exports to the US by air (equivalent to about \$76 billion). As undelivered merchandise began to pile up in warehouses in Japan, Korea, and Taiwan, production lines in factories slowed down, and companies began to lay off workers.

Soon after the attacks, the Bank of Japan (which is the central bank for Japan) made \$17 billion in credit available for banks and other institutions in the event they had trouble making or receiving payments. But the Bank did not cut its benchmark interest rate which already hovered near zero percent. (It currently stands at 0.1 percent.) Other central banks in Korea, Hong Kong, and Singapore also cut their interest rates to stabilize the Asian financial markets. In December 2001, Japan entered its fourth recession in ten years. Although the terrorist attacks in New York did not directly create the recession in Japan, that country's manufacturing sector relies on the US economy to buy over 30 percent of its goods.

China is the one notable exception to the downturn. In the words of one analyst: "Unlike many other economies around the world, China's vast economy barely registered a tremor from the September 11 attacks." Because the country has strict capital controls (meaning that foreign investors simply cannot quickly withdraw their money), China did not experience the same downturn as those faced by its neighbors. And over the past few years, China has also reduced its dependence on exports to the US to about nine percent of its gross domestic product.

LATIN AMERICA

Major stock markets in Latin America closed early in the hours after the attacks, but saw major declines – Brazil's leading market fell almost 10 percent and closed down 24 percent for the year; Argentina closed down almost 30 percent; and Venezuela 11 percent. Although not every country in Latin America relies on the US to buy its exports, a global downturn in the industrialized world generally spreads to emerging market countries (such as those in Latin America). For example, while Argentina sends more of its exports to Brazil and Europe, a recession in the US would likely lead to a downturn in Europe which could then spread to its trading partners in Latin America and other parts of the world.

In the months after the attacks, Latin America saw a decline in the flow of foreign investment capital. According to the Institute of International Finance, foreign investment in the region fell to \$45 billion in 2001 from \$61 billion the year before. Brazil saw its own decline in foreign investment to \$20 billion in 2001, down from \$40 billion in 2000.

Although Latin America felt the effects of the terrorist attacks, Argentina's declaration of a moratorium on the payment of its \$132 billion public debt in December 2001 (which was not in response to the attacks) has created more worries for its neighbors who are unsure how it will affect economic stability in the region.

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The war against terrorism in Afghanistan cost the US almost \$2 billion a month. Some lawmakers wanted US allies to help defray these costs. During the Persian Gulf war in 1991, US allies (especially Arab nations) paid nearly 90 percent of the \$60 billion bill.



Ending a decade-long battle, the US House of Representatives voted in September 2001 to release \$582 million in back dues to the United Nations in an effort to shore up international support for a global war against terrorism. The US Senate had passed a similar bill months earlier.

The Argentine government later ordered all dollar-denominated deposits to be converted into pesos and prohibited the transfer of foreign exchange (including corporate profits) to other countries. Some of these emergency measures were later rescinded.

WESTERN EUROPE

As in the case of East Asia, Europe had begun to experience an economic downturn months before the attacks, as consumer confidence in the US began to decline. In the days after the attacks, major stock markets across Europe saw substantial drops (although most had recovered their losses within a few months). But almost every European stock market had losses for the year, averaging 23 percent.

In the months after the attacks, the European Central Bank (which sets monetary policy for the 12 member nations of the European Economic and Monetary Union) cut its benchmark interest rate to 3.25 percent (its third cut in 2001) and made available billions of dollars in loans to banks and other European financial institutions. Despite calls by business leaders to cut further its benchmark rate, the Central Bank voiced concern that too much credit at low rates could create inflationary pressures in the future and would prevent EU members from meeting pre-planned budget targets. (The European Central Bank's overriding and statutory priority is to curb inflation.) Unlike the US, EU member nations in the Economic and Monetary Union are legally bound to reduce their budget deficits to acceptable limits.

Germany, which is the largest economy in Europe and whose economic health affects the entire well-being of the continent, saw increasing unemployment in the months after the terrorist attacks and almost no economic growth. In fact, with consumer spending declining in the US and other major countries, Germany saw its exports of cars and industrial machinery (a large component of its economy) decline throughout the fall of 2001. Germany technically began its recession in December 2001. And as the German economy began to falter, so too did the economies of its neighbors where an average of 30 percent of exports go to Germany. At the end of last year, major companies across Europe announced plans to eliminate over 400,000 jobs.

THE DEVELOPING WORLD

According to the World Bank, people living in developing countries (especially Africa) will suffer, by far, the worst effects of a slowing global economy further weakened by the September 11 attacks. Developing countries are usually more vulnerable to sudden downturns in the world economy because their own economies are highly dependent on exports of raw materials and other commodities (such as oil and precious metals) to the industrialized world where demand can go through wide swings. These same countries often cannot fall back on other sectors of their economies for a steady stream of revenue. In the weeks after the attacks, commodity prices did begin to drop (for example, agricultural prices dropped by five percent), as traders indicated that a recession in Asia, Europe, and the Americas would reduce the demand for raw goods.

Furthermore, aid to the developing world is expected to decrease. In the past six years, development aid to this part of the world has declined to just one percent (or about \$40 billion a year) of total development aid. The social effects of a downturn will hit developing countries much harder than their counterparts in the industrialized world because many don't have adequate social safety nets or savings to help people cope with unemployment. Those nations whose economies are primarily dependent on tourism (such as those in the Caribbean) also faced a crisis in the days right after the attacks as travelers cancelled 80 percent of all bookings in September and October. The Bahamas depends on tourism for half of its gross domestic product. In other countries such as the Dominican Republic, tourism is the nation's largest wage earner. The IMF later announced that it would provide policy advice and financial support for these countries. ❖



Despite a raging war in Afghanistan, member nations of the World Trade Organization (WTO) met in the Middle Eastern country of Qatar in November 2001 and decided to begin a new round of global trade talks. The last WTO meeting, held in Seattle in 1999 to lay the groundwork for new trade talks, ended in failure amidst anti-globalization protestors.



As a direct result of the slowdown in the global economy, the World Bank estimates that over 40,000 children will die of malnutrition and disease and another 10 million will fall below the Bank's extreme poverty line of living on less than \$1 a day.

Ethyl Corp. v. Canada: The first Chapter 11 case

The Ethyl case is the first where a foreign investor claimed that a breach of a host government's obligations under Chapter 11 had caused harm to its investment. The Ethyl Corporation, based in the US, established a Canadian subsidiary to import the chemical methylcyclopentadienyl manganese tricarbonyl (or "MMT") to be used as part of a gasoline additive in Canada. But that country was in the process of enacting legislation (the "MMT Act") which would have banned the import of MMT because some studies had shown (though inconclusively) that the chemical posed a risk to human health and the environment. The soon-enacted law then ended any sales and use of MMT in Canada because the only manufacturer and source of the chemical was located in the US.

Ethyl claimed that the Canadian government had breached several obligations under Chapter 11 which led to \$251 million in damages to its investment in Canada (i.e. the company's Canadian subsidiary). Ethyl argued that the MMT import ban constituted an indirect expropriation of its Canadian subsidiary because the ban could not be considered a measure that protected public welfare. The company pointed out that many studies undertaken by the Canadian government itself revealed that MMT actually "did not present a risk to human health or the environment." The company then argued that "since MMT is not a threat to human health . . . the Government of Canada could not prohibit MMT through any of its health legislation." The import ban of MMT had effectively put the subsidiary out of business, argued Ethyl, and Canada should make compensation for the company's lost investment.

The Canadian government responded that the import ban could not be considered an expropriation because the government took nothing belonging to Ethyl. By banning the import of a chemical which it believed was harmful to human health and the environment, Canada responded, it had simply exercised its regulatory powers recognized by international law to protect the public welfare, and that it shouldn't have to pay compensation for its actions.

Canada later settled the case and acknowledged that there was no conclusive evidence showing that MMT was harmful to human health. Ethyl agreed to drop its \$251 million lawsuit in exchange for Canada's dropping its MMT ban and paying Ethyl \$13 million for costs and lost profits. Because the two parties had reached a settlement, environmentalists noted that the tribunal did not explicitly rule on Ethyl's arguments as to whether the MMT ban should be considered an expropriation. But they worried that other businesses would use similar arguments to strike down laws affecting their profits.

Supporters of the decision say that Ethyl had rightly pressed its claim for compensation under the investor-state dispute settlement process – the Canadian government had passed the MMT Act knowing that it was not conclusively backed by scientific evidence which then led to the lost investments for the company.



Turning a landfill facility into a rare cactus preserve: In *Metalclad Corporation v. Mexico*, critics ask at what point does NAFTA consider high environmental standards to be an expropriation of an investment?

Metalclad Corp. v. Mexico: Landfill to cactus preserve

In 1993, the Metalclad Corporation, a US-based waste management company, began construction of a landfill facility in the municipality of Guadalcalzar in Mexico. According to Metalclad, federal authorities in Mexico had assured the company that all permits required for the construction of the facility would be issued without any problems, and that municipal permits were not necessary to build the landfill.

Municipal authorities later did stop construction in 1994, citing the lack of a municipal permit. Construction continued after the company applied for a permit which was later denied. But the company claimed that even after the denial of the municipal permit, federal authorities authorized a ten-fold expansion of the landfill facility, and construction soon continued. In September 1997, after the landfill facility was largely completed, the local governor issued an "ecological decree" declaring that the area around (and including) the landfill site would become a preserve for a rare cactus. This decree effectively ended any prospects for the company to operate the landfill. Metalclad then filed a claim of \$90 million against Mexico, arguing that Mexico had breached, among other obligations, its responsibility to provide compensation for expropriating the company's investment (embodied in the largely-completed landfill facility which could not be used because of the ecological decree).

A NAFTA tribunal ruled unanimously in favor of Metalclad, and argued that Mexico had indirectly expropriated Metalclad's investment without providing compensation. In a decision that worried activists, the tribunal defined expropriation under NAFTA as including "not only open, deliberate and acknowledged takings of property . . . but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use of property." The tribunal said that the implementation of the decree would "in and of itself, constitute an act tantamount to expropriation" and also ruled that it "need not decide or consider the motivation or intent of the adoption of the

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ecological decree" in making its decision.

Environmentalists say that they were alarmed by the decision because the tribunal's definition of an expropriation, they say, set a low standard as to whether a government measure could be considered an expropriation and because the decision ignored the environmental purpose of the ecological decree. Critics say that the decision could undermine a government's recognized ability to pass laws to protect the public interest without having to provide compensation to affected parties.

Supporters of the decision say that the case is a clear example of an expropriation. The tribunal's decision noted that officials in Mexico had denied the municipal permit and then issued their ecological decree "well after construction [of the landfill facility] was virtually complete." The tribunal later awarded Metalclad an award of \$16 million instead of the company's original request for \$90 million. Although Mexico disputed the judgment and award, it did make full payment to the company.

Methanex Corp. v. US: Compensation for all businesses?

This ongoing case is the first where a foreign investor has brought a claim against the US government for alleged breaches of Chapter 11. Methanex Corporation, a Canadian-based company, is the world's largest manufacturer of the chemical methanol which is an ingredient used in the gasoline additive MTBE. Methanex said that it owned two investments in the US – a methanol plant in Louisiana and a methanol-marketing subsidiary in Texas. Past studies have shown that MTBE is a possible human carcinogen which is highly soluble in water and travels rapidly through soil. The US government claimed that "leaks and spills of gasoline containing MTBE . . . do pose a substantial threat to drinking water supplies" and that, in particular, California had "experienced some of the worst and most widespread MTBE contamination of groundwater of any state in the US."

After a 1997 study commissioned by the State of California concluded that there were significant risks to human health and the environment due to the use of MTBE, the Governor of California issued an executive order establishing a timeline to phase out the use of MTBE in gasoline by December 31, 2002.

Methanex filed a claim against the US government for \$970 billion, arguing that the issuance of the executive order had reduced the demand for methanol by phasing out of use of MTBE in California, and that this was tantamount to an expropriation of its investments (as embodied in the value of its stock; its methanol market in California; and the value of its Louisiana plant and Texas marketing company). As a direct result of the issuance of the executive order, the company argued, its investments had declined in value by almost \$1 billion over the past several years. While it conceded that a government had a right under international law to pass regulations for a public purpose (such as protecting human health) without having to provide compensation, Methanex argued that the executive order was

not implemented to serve a public purpose, but, instead, was intended to help American companies offer substitute products that compete with methanol.

The US government replied that it didn't expropriate anything that could be considered an investment belonging to Methanex. It pointed out that the decline in the share price of Methanex began in 1995 (two years before California had commissioned its MMT study) and simply reflected a global oversupply of methanol. The government also said that the global price for methanol and the share price for Methanex had actually improved since the implementation of the executive order. It also pointed out that Methanex had closed its Louisiana plant for reasons which had nothing to do with the executive order and that most of the methanol sold on the market is used for purposes other than MTBE.

The government also claimed that, contrary to assertions made by Methanex, the executive order and similar measures were "nondiscriminatory environmental measures to protect public health by safeguarding the public's drinking water supply" and that this action could not be viewed as a compensable expropriation.

The government then pointedly criticized Methanex for even trying to demand compensation for an environmental measure used to protect the public: "Methanex's claim does not remotely resemble the type of grievance for which the States Parties to the NAFTA [agreement] created the investor-State dispute resolution mechanism of Chapter 11. Methanex's case is founded on the proposition that, whenever a State takes action to protect the public health or environment, the State is responsible for damages to every business enterprise claiming a resultant setback in its fortunes . . . Plainly put, this proposition is absurd." The tribunal has yet to issue its decision.

Recent developments

Critics have pushed the three NAFTA countries to clarify and issue "interpretive statements" on certain provisions in Chapter 11, particularly provisions concerning expropriations. They also say that Chapter 11 provisions should not be incorporated into any FTAA agreement as long as there are disputes concerning the interpretation of specific provisions. The implementation of an FTAA (including investment provisions similar to those in Chapter 11) could expose developing countries to judgments in the hundreds of millions of dollars, critics argue. Supporters respond that any clarifications to Chapter 11 could open the entire NAFTA agreement to revision.

Although, in July 2001, the NAFTA Free Trade Commission did issue two clarifications, critics say that it didn't address their concerns. In the meantime, negotiations to incorporate NAFTA-style investment provisions in the FTAA agreement continue. ❖

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Global trade round-up



Anthrax Scare Helps Clarify WTO Intellectual Property Rules

Do the rules governing intellectual property rights under the World Trade Organization (WTO) allow countries to break drug patents during public health emergencies? The recent outbreak of inhaled anthrax infections in the US brought greater attention to this long-running debate.

In October 2001, health officials found packets of a powdered form of inhaled anthrax in various offices in Florida, Washington, DC, and New York City (which infected and then killed several people). Anthrax is a bacterium which causes respiratory complications and death if not treated immediately. Bayer AG, the German manufacturer and patent-holder of the sole antibiotic (called Cipro) approved to treat inhaled anthrax, assured the public that it had the capacity to meet rising demand. But critics, arguing that it would take at least 20 months for the company to produce enough pills for just 12 million people, urged the US government to break Bayer's patent on Cipro by issuing "compulsory licenses" which would then allow generic drug companies to manufacture the antibiotic in large quantities (and at a fraction of the cost) before another outbreak occurred. More than 30,000 Americans (mostly postal workers) began a regimen of Cipro last year to ward off any infections. While the retail cost of Cipro is \$6 per pill, the generic version (though not yet available in the US) costs 15 cents on the global market.

Under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (popularly known by its acronym "TRIPS"), member nations must provide patent protection for any invention. But a government may also issue to companies a compulsory license which would allow them to make a patented product without the patent holder's permission, so long as the patent holder receives adequate compensation. The TRIPS agreement does not list the circumstances that justify giving out compulsory licenses.

A debate concerning whether TRIPS allows the issuance of compulsory licenses during emergencies have become a sore point in relations between developing nations experiencing public health problems such as a spreading AIDS epidemic and industrialized countries wanting to protect drug patents which they say promotes research and innovation. While developing countries say that the TRIPS agreement allows them to break patents

during national emergencies to provide cheaper versions of patented drugs, developed countries such as the US say that the issue is not clear and has threatened to impose sanctions on countries that issue compulsory licenses.

A few weeks after the first outbreak of anthrax, the Canadian health agency, citing "extraordinary and unusual times," announced that it would issue a compulsory license to a generic manufacturer of Cipro in Canada. Both the Bush administration and the pharmaceutical industry argued that there would be no need to break Bayer's patent on Cipro in the US because the company would be able to meet the rising demand for the drug. Furthermore, the administration declared that breaking Bayer's patent (which expires in December 2003) would be illegal. But many patent lawyers argued that federal law clearly allows the US to issue compulsory licenses for patented products.

Under mounting public pressure, the Bush administration soon changed course and demanded that Bayer lower its price for Cipro sold to the government. The Secretary of Health and Human Services also threatened not only to issue compulsory licenses for generic versions of Cipro, but also to request special legislation denying Bayer any compensation as a result of the government's breaking its patent on that drug. The company later announced that it would sell 100 million tablets of Cipro to the government for 85 cents each (rather than the regular price of \$1.43) but would continue to charge pharmacies the same wholesale price of \$4.13 per tablet. Citing an agreement with Bayer, Canada later withdrew its intention to issue a compulsory license on Cipro.

During the WTO ministerial conference in Doha, Qatar, in November 2001, the US and several developing countries (all members of the WTO) issued declarations intended to clarify whether the TRIPS agreement allows flexibility to address public health crises. They agreed that TRIPS gives all WTO members "the freedom to determine the grounds upon which such [compulsory] licenses are granted," particularly during health crises. But they also agreed to continued adherence to the TRIPS agreement. Critics say that the US worked out a compromise to avoid being perceived as setting a double-standard on compulsory licenses. The pharmaceutical industry responded that the declarations were political statements and not legally binding. ❖



Welcome to the club: China's 16- year quest ends

Like a person who holds his breath before finally being admitted to an exclusive club, the People's Republic of China gave a sigh of relief last December when it became the 143rd member of the World Trade Organization (WTO) after 16 years of drawn-out negotiations and delays. With the exception of Russia, all major industrialized and

developing countries are now members of this world body that regulates 90 percent of global commerce and adjudicates trade disputes.

In contrast to trade treaties that China has signed over the years, its entry in the WTO opens that country's vast economy to competition from abroad on a much larger scale than ever before. In the words of one commentator, China's admission to the WTO will set off a "multinational rush to grab a piece of China's promising market of 1.3 billion people." And at the core of the WTO agreement, China must treat all other members and their products on a most-favored-nation basis.

According to American business executives, China must allow (for the first time) foreign investment in and ownership of its potentially huge insurance, banking, and telecommunications industries. In the next few years, US banks can offer consumer loans to Chinese customers, and foreign goods will be sold directly to Chinese consumers rather than through middlemen. US agricultural exports to China are also expected to increase \$2 billion a year. One Congressman described China's admission as a "one-way street" in which China made all of the concessions in order to join the WTO. Unlike the terms reached under, say, the North American Free Trade Agreement, China's entry to the WTO will not provide it with preferential access to the American market. China will have the very same access as does every other US trading partner.

The road to WTO membership has been a long one for China, which began its quest in 1986 when that organization was known as the General Agreement on Tariffs and Trade. China overcame its largest hurdle when the US Congress granted that country permanent normal trade relations in 2000 after long debate. Previously, under Title IV of the 1974 Trade Act, the US had to renew its trade relations with China on an annual basis because of that country's alleged human rights violations. According to the US Trade Representative, if China became a WTO member, the annual review would have violated WTO rules, which require that a member nation treat all other members on a most-favored-nation basis (i.e. if the US required an annual review of China's trade status, it would have to impose the same requirement on every other WTO member).

Many events delayed China's membership to the WTO during the final year of negotiations. Some WTO members charged that China was backtracking on the many promises and concessions it had made to join the WTO. For example, many officials say that China wanted to extend the time period in which it would open its insurance market and phase-out subsidies to its agricultural sector.

Entry to the WTO is expected to bring many benefits to China. For example, Chinese officials believe that new foreign investment in China will help to create thousands of job opportunities. Although it is the world's fastest growing economy, China needs to grow much faster to care for its growing population. Other WTO member nations will also

have to end any existing trade policies that discriminate against Chinese goods. But China also faces many risks. Analysts say that many inefficient, state-controlled enterprises will likely close in the face of greater foreign competition. Because China does not have a strong domestic safety net for displaced workers, these analysts say that the gap between rich and poor will widen, which could lead to social unrest. China will also have to revise many existing laws to make them compatible with WTO rules and also limit government subsidies which have been used to protect domestic industries.

Simultaneously, the WTO admitted Taiwan (which China considers a renegade province) as the organization's 144th member. To prevent China from blocking Taiwan's membership, officials agreed to admit Taiwan under the name "Separate Customs Territory of Taiwan, Kinmen and Matsu," intended to dissipate connotations of a sovereign state wholly independent of China. Hong Kong, now a Special Administrative Region of China, has retained its separate status as a WTO member, in which capacity it, too, is a Customs Territory. ❖



Hello, Euro! So long to francs, guilders, liras, pesetas . . .

Marking a final farewell to such currencies as the French franc, the Deutschmark, and the Spanish peseta, the European Economic and Monetary Union (EMU) began the actual circulation of its single currency – the euro – on January 1, 2002. People now traveling across different countries using the euro will no longer have to exchange their currencies to make purchases or to carry out transactions. The euro made its debut in 1999, but only in an electronic format used in bank transactions and corporate and governmental bookkeeping.

The circulation of actual euro coins and notes is just one of a series of steps that western Europe has taken in recent decades toward political and economic union. Since the 1950s, EMU member nations have ceded their sovereignty in many areas of governance to certain institutions (such as the European Commission, European Parliament, and the European Court of Justice) to create a common market where people, goods and services, and capital can move freely across borders. In the monetary realm, the European Central Bank decides on EMU monetary policy which is then implemented by the central banks of member nations (who are also responsible for the actual printing and distribution of euro in their own countries). Of the 15 member nations of the EU, three members (Denmark, Sweden, and the United Kingdom) have, for the time being, decided not to adopt the euro. These three countries, while still members of the EU, do

not have an official say in formulating monetary policy for the EMU.

Economists generally agree that the introduction of the euro will increase commerce by allowing businesses to sell their goods in many different markets across Europe without having to worry about currency conversions which created market inefficiencies in the past. Policymakers also claim that the circulation of actual euro notes and coins will bring down prices for all kinds of products across the continent since consumers will now be able to compare prices and shop for bargains. But many economists dispute this prediction, arguing that because not all EMU members are at the same level of economic development (for example, Germany is wealthier than Portugal), prices will still differ for the same products in different markets. They also point out that sales taxes differ in every EMU country which can skew prices up or down even if everything is denominated in euros.

Financial analysts also argue that the euro will create an efficient European corporate bond market where companies can now raise millions of euros from across the continent without having to worry about the strength of various currencies.

Disappointing those who were hoping that it would soon surpass the US dollar to become the currency of choice around the world, the euro recently closed at 87 US cents, down from a high of \$1.17. Financial analysts say that despite the current world economic downturn, many investors still believe that US stocks and corporate bonds offer better growth potential than their European counterparts, and have invested their capital accordingly. This, in turn, has led to a decline in the price of the euro.

Other plans are in the works for a more integrated Europe. In the next few years, representatives from EMU member nations supposedly will draw up an EMU constitution to help further coordinate economic and political policies. But many observers say that it is unlikely that individual EMU members will actually push for an American-style constitution where one central government wields more power than individual states. ❖



A \$4 Billion Defeat that Won't Go Away

Like a lingering cold that never seems to clear up, the US is still trying to shake a recent defeat at the World Trade Organization (WTO). In what analysts describe as the most expensive case that any country has ever lost at the WTO, the US is continuing its efforts to work out a compromise with the European Union (EU) which will allow American companies to exempt from taxes the sale of exports made through offshore subsidiaries.

In a case brought by the EU ("United States: Tax

Treatment for 'Foreign Sales Corporations'"), a WTO dispute settlement panel ruled in September 1999 that the tax breaks given under the "foreign sales corporation" (FSC) provisions in the US tax code – whereby American companies export US-manufactured goods through offshore subsidiaries set up in places like the Virgin Islands and Barbados – constituted an illegal export subsidy under WTO rules.

Tax analysts say that under these provisions, US companies were able to reduce the taxes on their export sales by 15 to 30 percent. The EU argued that the FSC provisions gave an unfair advantage to American exports, and that the WTO agreement generally prohibited member nations from subsidizing exports to make them more competitive. Observers say that compliance with the WTO decision would require US officials to rewrite the FSC provisions. The WTO Appellate Body, the highest appeals body in that organization, upheld the original panel decision in February 2000.

Analysts point out that hundreds of American companies, such as Boeing, General Motors, and Motorola, have used the FSC provisions to save over \$3.5 billion in taxes every year, and that businesses have formed more than 7,000 FSCs since the law was first enacted in 1984. Corporate executives say that the EU and many other countries have similar tax provisions where companies don't pay taxes on exports, and that the FSC provisions have allowed American products to stay competitive abroad. US officials also claim that, after losing many high profile trade battles to the US in recent years, the EU decided to challenge the FSC provisions – out of spite – even though their predecessors had been enacted over 15 years earlier.

After trying to work out a compromise, the EU rejected, in November 2000, a US plan which would repeal the FSC provisions and replace them with special income tax rates for export and non-export foreign sales. It said that the proposed changes still constituted a subsidy contingent on exports. After another WTO trade dispute panel ruled in July 2001 that the revised US plan still violated the original decision (later upheld by the WTO Appellate Body), the EU asked for permission to impose sanctions on the US for its failure to comply with the original WTO decision. It claimed that European companies suffered \$4 billion in damages as a result of the FSC regime. Observers say that sanctions will probably take the form of 100 percent tariffs on various American products, ranging from aircraft parts to sports accessories.

Once a WTO arbitrator determines the actual damages, the EU will request permission to impose that amount on the US. (Most arbitration decisions in past cases have reduced the amount of damages by half.) The arbitrator will likely release a decision in early April 2002. In the meantime, US and EU officials are still trying to negotiate an agreement which will prevent the FSC dispute from souring trade relations between the two powers. ❖



The 2002 Otto L. Walter Lecture

Multidisciplinary Practice and the European Court of Justice

In an opinion having worldwide implications, the European Court of Justice has decided a case concerning a ban in the Netherlands that prohibits lawyers and non-lawyers, including accountants, from fully merging their practices. The case was brought against the Netherlands Bar Association by affiliates of two of the Big Five accounting firms, Arthur Andersen and PricewaterhouseCoopers. Seeking to overturn the ban, they assert that it improperly shields the legal services market from competition, and is inconsistent with cross-border rights of establishment within the European Union. Supporters of the ban say that large accounting firms offering integrated legal and accounting services may compromise the core values of the legal profession designed to avoid conflicts of interest, protect client confidentiality, and maintain independent judgment. The Lecture will deal with the history of the case and its likely ramifications.

LECTURER—ANTHONY HUYDECOPER

Advocate-General to the Supreme Court of the Netherlands. Former Chair of the Committee on Multidisciplinary Practice of the European Association of Bar Organizations. He was President of the Netherlands Bar Association when it was sued by the plaintiffs in the case on multidisciplinary practice recently decided by the European Court of Justice.

COMMENTATOR—ROBERT MACCRATE, ESQ.

Senior Counsel, Sullivan & Cromwell; Former President, American Bar Association, and New York State Bar Association

COMMENTATOR—DEBORAH H. SCHENK

Marilynn and Ronald Grossman Professor of Taxation, New York University School of Law

WELCOME—RICHARD A. MATASAR

Dean and President, New York Law School

HOST—SYDNEY M. CONE, III

C.V. Starr Professor of Law, New York Law School

**Thursday, March 7, 2002
4:00 pm–6:00 pm
Wellington Conference Center**

No charge for general admission. But seating is limited. For more information, please visit
www.nyls.edu/content.php?ID=95
or call the Center for International Law at (212) 431-2865.