Investment Forum Hosted by Ways and Means Committee Democrats

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Thank you for this opportunity to discuss the investment chapter of the Trans-Pacific Partnership. My name is Michael Smart and I am Vice President of Rock Creek Global Advisors, an international economic policy consulting firm. I have been involved with investment policy for more than a dozen years, as a lawyer and advisor in the private sector, as a member of the National Security Council staff, and as trade counsel for the Senate Finance Committee under then Chairman Max Baucus. I am speaking today solely on my own behalf and not on behalf of any client or company.

When U.S. companies engage in the global economy, they serve their foreign customers not only by exporting from the United States but also through their overseas affiliates. Sales by these affiliates, in fact, were nearly double the value of U.S. exports in 2013. International agreements that liberalize both trade and investment rules, therefore, create the best opportunity for U.S. companies to expand market share and create jobs. That is why investment chapters have been an essential part of U.S. free trade agreements for more than 20 years.

Although the United States began negotiating investment treaties in the early 1980s, it did not face its first claims until the mid-1990s. The United States prevailed in every one of those cases – as it has in every case since then – but the experience sensitized U.S. policymakers to the perspective of respondent governments. This experience is reflected in Trade Promotion Authority (TPA), both the 2002 and 2015 legislation, which sets forth specific negotiating objectives regarding the substantive investment rules and the procedures for resolving disputes.

The TPP investment chapter is fully aligned with those instructions from Congress. Specifically, the chapter meets the TPA objectives to reduce or eliminate investment barriers and secure investor rights comparable to those available in the United States. Those rights protect investors against nationality-based discrimination, violations of due process, local-content requirements, and uncompensated takings of property.

The TPP investment chapter also meets TPA objectives related to the investor-state dispute settlement mechanism, or ISDS. It establishes procedures to dismiss frivolous claims and award costs and attorneys' fees to the respondent government. It enhances public participation, including through acceptance of amicus submissions. And it ensures transparency, including by making documents and hearings open and available to the public.

While the TPP investment chapter deserves support, it is not perfect. Its weaknesses primarily arise from the Parties' attempt to placate the critics of ISDS who demand proof of a negative: that investment rules do not encroach on legitimate regulatory activity.

It should be a sufficient response that no ISDS tribunal has ever found a non-discriminatory measure of general application to breach an investment obligation. In the absence of such a case, the critics should bear the burden to identify the circumstance where a regulator must breach an investment obligation to advance a legitimate public interest and show that such action is not already sheltered by an exception provided for in the chapter.

Even though that burden has not been met, the TPP investment chapter nonetheless adds new text to the provisions on national treatment, MFN, the minimum standard of treatment, and expropriation. The new text, which is not found in any existing U.S. agreement, arguably does no more than clarify the scope of these obligations relative to a government's right to regulate. It is quite possible, however, that a tribunal, seeking to give meaning to this new language, could tip the scales in a way that shields governments from liability for bad actions that otherwise would constitute a treaty breach.

The TPP investment chapter also includes an unfortunate, sector specific carve-out from ISDS. I am not referring to the carve-out for tobacco control measures, which has received significant public attention, but the one that prevents financial institutions from bringing claims for nationality-based discrimination. The United States eliminated this carve-out in 2008, when the Treasury Department, the Federal Reserve, and the Securities and Exchange Commission decided that it was harmful to U.S. financial institutions operating overseas and unnecessary to ensure the right of financial regulators to protect the safety and soundness of the U.S. financial system. The Obama Administration confirmed this position and endorsed full access to ISDS by financial institutions in the 2012 model BIT.

It is disappointing that the Administration was unable to secure these protections in TPP, leaving financial institutions without an effective remedy for discriminatory actions by foreign governments. The Administration does, however, have the opportunity to mitigate the harm by ensuring that the carve-out does not appear in future agreements, including the U.S.-China bilateral investment treaty and the Transatlantic Trade and Investment Partnership.

Despite these shortcomings, the TPP investment chapter represents a good outcome for the United States that will promote the interests of U.S. companies while ensuring ample room for governments to regulate. It gives U.S. investors new international protections in four markets where they do not currently exist, including Japan and Malaysia. It also includes reforms to investment rules and procedures that earned the support of all TPP parties, including Australia, which rejected ISDS in the context of our existing bilateral FTA.

Thank you for this opportunity to share my views. I look forward to your questions.