

An hourglass-shaped graphic with a globe inside. The top bulb is dark blue, and the bottom bulb is light blue. The globe is centered within the hourglass. The text is overlaid on the hourglass.

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*Dispute Settlement Under the Proposed U.S.-Peru Trade
Promotion Agreement: An Overview*

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Abstract. The proposed U.S.-Peru Trade Promotion Agreement (TPA or Agreement) follows current U.S. free trade agreement practice in containing two types of dispute settlement: State-State, applicable to disputes between the Parties to the TPA, and investor-State, applicable to claims by an investor of one TPA Party that the other Party has breached its TPA investment obligations. Implementing legislation for the TPA approving the Agreement and providing legislative authorities needed to carry it out was signed into law December 14, 2007 (P.L. 110-138); the TPA has not yet entered into force.

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CRS Report for Congress

Dispute Settlement Under the Proposed U.S.-Peru Trade Promotion Agreement: An Overview

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Summary

The proposed U.S.-Peru Trade Promotion Agreement (TPA or Agreement) follows current U.S. free trade agreement practice in containing two types of dispute settlement: State-State, applicable to disputes between the Parties to the TPA, and investor-State, applicable to claims by an investor of one TPA Party that the other Party has breached its TPA investment obligations. Implementing legislation for the TPA approving the Agreement and providing legislative authorities needed to carry it out was signed into law December 14, 2007 (P.L. 110-138); the TPA has not yet entered into force. This report will be updated.

The proposed U.S.-Peru Trade Promotion Agreement (TPA or Agreement) follows current U.S. free trade agreement (FTA) practice in containing two types of dispute settlement: (1) general or State-State, applicable to disputes between TPA Parties, and (2) investor-State, applicable to claims by an investor of one TPA Party that the other Party has violated its TPA investment obligations.¹ Investor-State dispute settlement has been a key element of U.S. bilateral investment treaties and with the inclusion of investment obligations in most U.S. FTAs, it has become a feature of these agreements as well. The dispute settlement provisions of the proposed TPA need to be considered in tandem with other TPA obligations to understand the extent to which measures adopted or maintained by a TPA Party may be the subject of dispute settlement. Exceptions to TPA obligations are also an element in assessing the scope of obligations undertaken pursuant to the

¹ The final text of the proposed U.S.-Peru Trade Promotion Agreement (TPA) is posted on the website of the Office of the United States Trade Representative at [http://www.ustr.gov/Trade_Agreements/Bilateral/Peru_TPA/Final_Texts/Section_Index.html]. For additional information on the proposed TPA, see CRS Report RL34108, *U.S.-Peru Economic Relations and the U.S.-Peru Trade Promotion Agreement*, by M. Angeles Villarreal, and CRS Report RS22521, *Peru Trade Promotion Agreement: Labor Issues*, by Mary Jane Bolle and M. Angeles Villarreal.

Agreement.² To date, resort to panels under FTA State-State dispute settlement has been relatively uncommon; further, FTA investor-State proceedings have been invoked almost exclusively under the North American Free Trade Agreement (NAFTA).³ The United States-Peru Trade Promotion Agreement Implementation Act, which approves the TPA and provides legislative authorities needed to carry it out, was signed into law December 14, 2007 (P.L. 110-138). The Agreement itself has not yet entered into force.⁴

State-State Dispute Settlement (Chapter Twenty-One)

State-State or general dispute settlement is set out in Chapter Twenty-One of the proposed TPA, which applies to disputes involving the interpretation or application of the Agreement or wherever a Party considers that an actual or proposed measure of the other Party is or would be inconsistent with the TPA, that the other Party has violated the TPA, or that an enumerated TPA benefit owed the Party — e.g., a tariff reduction — is being nullified or impaired by a non-violative measure of the other Party.

Consultations. The proposed TPA allows a Party to initiate consultations with the other Party regarding matters arising under the Agreement. If a matter is not resolved within 60 days of the initial request (15 days for matters involving perishable products) or another period that the Parties may agree upon, either Party may request a meeting of the U.S.-Peru Free Trade Commission, an administrative body established under Article 20.1 consisting of cabinet-level officials of the Parties or their designees (see Art. 21.5, n.1), which, if it decides to convene, would assist the Parties in promptly resolving the dispute. If the consulting Parties fail to resolve a matter within 30 days after the Commission has convened, or where the Commission has not convened, within 75 days after the initial request for consultations (30 days if perishable goods are concerned), or another agreed-upon period, any consulting Party that participated in the meeting of the Commission, or if the Commission has not convened, had requested a meeting of the

² For example, if a Party invokes the TPA national security exception in a Chapter Ten or Chapter Twenty-One proceeding, the tribunal or panel must find that it applies. TPA, Art. 22.2, n.2.

³ To date, five panel reports have been issued under the U.S.-Canada FTA (currently suspended) and three under the NAFTA. Panel reports are available at the website of the NAFTA Secretariat at [http://www.nafta-sec-alena.org/DefaultSite/index_e.aspx]. For further information on NAFTA investment disputes, see NAFTA Investor-State Arbitrations, at [<http://www.state.gov/s/c3439.htm>]. In 2007, a claim was filed by a U.S. investor against Guatemala under the investor-State provisions of the Dominican Republic-Central America-United States Free Trade Agreement (DR-CAFTA). See International Institute for Sustainable Development, *Investment Treaty News, September 7, 2007*, at [http://www.iisd.org/pdf/2007/itn_sep7_2007.pdf].

⁴ The proposed TPA provides that it will enter into force “60 days after the date on which the Parties exchange written notifications certifying that they have completed their respective legal requirements or on such other date as the Parties may agree.” TPA, Art. 23.4. TPA implementing legislation provides that “at such time as the President determines that Peru has taken measures necessary to comply with those provisions of the Agreement that are to take effect on the date on which the Agreement enters into force, the President is authorized to exchange notes with the Government of Peru providing for the entry into force, on or after January 1, 2008, of the Agreement with respect to the United States.” P.L. 110-138, § 101(b).

Commission, may request that an arbitral panel be established. An arbitral panel is automatically established upon delivery of a request to the other Party.

Panels. Dispute panels consist of three members. The complaining and defending Parties appoint one panelist each. If either fails to do so, the panelist is to be selected by lot from a roster established under the proposed Agreement. The Parties are expected to agree on a third panelist to chair the panel, but if they cannot agree, the chair will be selected by lot from roster members who are not nationals of either of the disputing Parties. Panel selection is subject to timelines set out in the Agreement. Unless the disputing Parties agree otherwise, the panel is to present its initial report to the disputing parties within 120 days after the last panelist is selected. The report is to contain (1) findings of facts and (2) the panel’s determination as to whether a disputing Party is in compliance with its TPA obligations, or whether a measure is causing nullification or impairment of TPA benefits, as the case may be, or any other requested determination. The report must also contain recommendations for resolving the dispute if requested by the Parties. After considering any written comments or requests for clarifications by the Parties, the panel is to issue its final report. The final report is due 30 days after the initial report is presented unless the Parties agree otherwise.

Implementation. On receiving the final report, the disputants are to agree on the resolution of the dispute, which should normally conform with the panel’s findings and recommendations. If the panel has found that the defending Party is not in conformity with its TPA obligations or that it is causing nullification or impairments of benefits, the resolution should be to eliminate the non-conformity or the trade injury. Compensation, suspension of benefits, and monetary assessments are allowed as temporary measures pending compliance. For purposes of U.S. law, dispute settlement results under trade agreements are considered to be non-self-executing and thus, where a federal law or regulation is faulted and the Executive Branch does not have sufficient delegated authority to act, legislation would be needed to comply.⁵

Compensation and suspension of benefits. If the defending Party needs to take action and the disputing Parties cannot agree on resolving the dispute within 45 days after receiving the final report (or within another agreed-upon period), the defending Party must enter into compensation negotiations with the complainant. If the Parties cannot agree on compensation within 30 days, or if they have agreed on compensation or a means of resolving the dispute and the defending Party has not complied with the agreement, the complaining Party may suspend benefits “of equivalent effect” (e.g., impose tariff surcharges on selected imports from the defending Party). The complaining Party must notify the defending Party of its intent, including the amount of proposed retaliation. If the defending Party believes that the amount is “manifestly excessive,” or that it has complied in the proceeding, as the case may be, it may ask the panel to reconvene to consider the issue. If the panel determines that the proposed suspension of benefits is excessive, it must determine the proper level of retaliation. The complaining Party may

⁵ Note § 102(a) of P.L. 110-138, the TPA implementing legislation, stating that “No provision of the Agreement, nor the application of any such provision to any person or circumstance, which is inconsistent with any law of the United States shall have effect.” See also § 102(b) of the statute regarding the relationship of the TPA to state law.

suspend benefits up to this level, or if the amount has not been arbitrated, the level that it originally proposed, unless the defending Party has been found to be in compliance.

Monetary assessments. The complaining Party may not suspend benefits if the defending Party notifies the complainant by a given date that it will pay an annual monetary assessment. The disputing Parties are to consult on the amount, but if they are unable to agree within 30 days, the assessment will be set at a level, in U.S. dollars, equal to 50 percent of the level of benefits the panel has determined to be proper or, if there has not been a panel determination, 50 percent of the amount originally proposed by the complaining Party. Unless the U.S.-Peru Free Trade Commission decides otherwise, the assessment is to be paid to the complaining Party in equal quarterly installments. Under the proposed TPA, the Commission may decide instead that the assessment be paid into a fund and expended at its direction “for appropriate initiatives to facilitate trade between the disputing Parties.” If the defending Party does not pay the assessment, the complaining Party may suspend benefits as arbitrated or proposed, as the case may be.

Compliance review. If the defending Party believes that it has complied in the proceeding, it may refer the matter once again to the panel. The panel is to issue its report within 90 days after the defending Party notifies the complaining Party of its panel request. If the panel decides in favor of the defending Party, the complaining Party must promptly terminate any trade retaliation and the defending Party will no longer be under an obligation to pay any monetary assessment it has agreed to.

No private rights of action. The proposed TPA prohibits a Party from providing a private right of action under its domestic law against the other Party on the ground that the latter has failed to conform with its TPA obligations. As has been the practice with past FTAs, Peru TPA implementing legislation includes a provision precluding private rights of action under the Agreement (P.L. 110-138, § 102(c)).

Labor and Environment Disputes. Both Chapter Seventeen, the labor chapter of the TPA, and Chapter Eighteen, its environment chapter, contain special consultation provisions that must be invoked before a Party may resort to Chapter Twenty-One dispute settlement. Unlike most earlier FTAs with labor and environment chapters, however, the TPA does not limit the use of its general dispute settlement procedures to specified provisions of those chapters or limit initial remedies for non-compliance to the payment of an annual monetary assessment (see, e.g., DR-CAFTA, Arts.16.6.7, 17.10.7, 20.17.1).

Labor disputes. The proposed TPA differs from earlier FTAs with regard to its substantive labor obligations and the extent to which its general dispute settlement procedures apply to labor disputes. While the TPA, like earlier FTAs, requires each Party to “not fail to effectively enforce its labor laws ... in a manner affecting trade or investment between the Parties ... ,” it further requires that each Party “adopt and maintain in its statutes and regulations, and practices” enumerated labor rights as stated in the 1998 International Labor Organization (ILO) Declaration on Fundamental Principles and Rights at Work. To establish a violation of this provision, however, a Party must also show that bilateral trade or investment is affected (Art. 17.2, n.1). The TPA also requires Parties not to waive or otherwise derogate from ILO-related implementing measures in a manner affecting bilateral trade or investment, where the derogation would be inconsistent with a fundamental labor right, and includes within its domestic labor law enforcement requirement laws adopted or maintained in accordance with the new ILO-related provision. While most earlier FTAs allowed general dispute settlement procedures to be

initiated only with regard to their labor law enforcement requirement, TPA general dispute procedures apply to Chapter Seventeen without such a limitation. Before a Party may invoke these procedures for a labor issue, however, it must first seek to resolve the matter under Chapter Seventeen consultation provisions. If the Parties fail to resolve a dispute within 60 days after consultations are requested, the complaining Party may seek consultations or a meeting of the U.S.-Peru Free Trade Commission under Chapter Twenty-One and, following this, may invoke the rest of the Chapter.

Environmental disputes. As is the case with labor issues, the proposed TPA differs from earlier FTAs with respect to substantive environmental obligations as well as the extent to which its general dispute settlement procedures apply to environmental disputes. Like earlier FTAs, the TPA requires each Party to “not fail to effectively enforce its environmental laws ... in a manner affecting trade or investment between the Parties...” It also places a new requirement on each Party to “adopt, maintain, and implement laws, regulations and all other measures to fulfill its obligations” under listed multilateral environmental agreements (MEAs), and includes laws implementing the MEAs within its domestic enforcement obligation.⁶ To establish a violation of the MEA implementation requirement, however, the complaining Party must also demonstrate that the other Party has failed to act in a manner affecting bilateral trade or investment (Art. 18.2, n.1). Chapter Twenty-One dispute settlement procedures generally apply to disputes under Chapter Eighteen articles, but where a dispute arises under the latter, the complaining Party may not resort to Chapter Twenty-One unless it first seeks to resolve the matter under Chapter Eighteen consultation provisions. If the Parties fail to resolve a dispute within 60 days of the initial consultation request, the complaining Party may seek consultations or a meeting of the U.S.-Peru Free Trade Commission under Chapter Twenty-One, and may then proceed under the Chapter if it so chooses. If a dispute panel is convened and the dispute involves an MEA obligation, the panel must follow specified directions in Chapter Eighteen in making its findings and determination (Art. 18.2.8).

Investor-State Dispute Settlement (Chapter Ten)

Chapter Ten, the proposed TPA investment chapter, allows U.S. investors in Peru and, likewise, Peruvian investors in the United States, to file arbitral claims against Peru and the United States, respectively, for violations of Chapter Ten obligations.⁷ Claims may involve measures of states and localities to the extent they are covered by Chapter Ten. An arbitral proceeding may be initiated by an “investor of a Party” on the ground that other Party has breached a TPA investment obligation, an investment authorization, or an investment agreement, and the investor has incurred loss or damage from the

⁶ Listed MEAs are the Convention on International Trade in Endangered Species, the Montreal Protocol on Substances that Deplete the Ozone Layer, and conventions on wetlands, pollution from ships, and various marine species. The TPA also generally requires Parties not to derogate from environmental laws in a manner that weakens protections afforded in those laws in a manner affecting bilateral trade and investment and contains an Annex on Forest Sector Governance.

⁷ Chapter Ten includes obligations relating to, *inter alia*, national, most-favored-nation, and minimum standards of treatment, expropriation, and transfers of investment-related funds into and out of the host country. Parties have exempted specified existing and future non-conforming measures from certain Chapter Ten obligations. See TPA, Art. 10.13. Special dispute settlement provisions apply when restrictive measures involving transfers are at issue. TPA, Annex 10-E.

breach.⁸ The investor may also submit a claim on behalf of an enterprise of the other TPA Party that the investor owns or controls, where the enterprise is alleged to have been injured by the breach. Investor-State dispute settlement may also be invoked in certain cases involving financial services institutions in the United States and Peru (Art. 12.1.1). The investor may submit a claim under various arbitral mechanisms, including the Convention on the Settlement of Investment Disputes (ICSID Convention) and ICSID Rules of Procedure, UNCITRAL Arbitration Rules, or, if the disputants agree, any other arbitration institution or rules.⁹ The United States and Peru give their blanket consent in the TPA to the submission of Chapter Ten investor claims.

Once an investor claim is filed, a three-member arbitral tribunal will be established. One arbitrator is to be appointed by each disputing party, and the third, the presiding arbitrator, is to be appointed by agreement. If the tribunal has not been constituted within 75 days after the claim is filed, the Secretary-General of ICSID, if requested, is to appoint the outstanding arbitrators or arbitrators. Chapter Ten contains rules for the conduct of the arbitration, including allowing the tribunal to accept and consider *amicus* submissions from persons or entities that are not disputing parties and to rule on preliminary objections by the challenged Party that the claim submitted is legally not a claim for which a Chapter Ten award may be made. Multiple claims with certain common elements may be consolidated. Subject to provisions aimed at preventing disclosure of protected information, documents submitted by the parties and tribunal orders, awards and decisions are to be made available to the public. The tribunal must also conduct public hearings.

When a claim involves an alleged breach of a TPA obligation, the tribunal is to decide the issues in accordance with the TPA and applicable rules of international law. If the U.S.-Peru Free Trade Commission has issued an interpretation of a TPA provision, as it is authorized to do under Article 20.1.3(c), the decision is binding on the tribunal and any tribunal decision or award must be consistent with the Commission decision. A tribunal may only make monetary awards and thus may not direct a Party to withdraw or modify a disputed measure. An award may consist of monetary damages, restitution of property, or both. If restitution is awarded, the Party is to pay monetary damages and applicable interest in lieu of restitution. The tribunal may also award costs and attorney's fees. It may not award punitive damages. An arbitral award has no binding force except between the disputing parties and with respect to the case at hand. A prevailing investor may not seek enforcement of the final award until 90 or 120 days after it is issued (depending on the arbitral rules used), a period allowing for possible proceedings to revise or annul the award. If the Party does not ultimately abide by a final award, the investor may request that a panel be established under the TPA State-State dispute settlement provisions to determine compliance. Regardless of whether a compliance panel is sought, however, the prevailing investor may seek judicial enforcement of the award under various multilateral conventions providing for the recognition and enforcement of international arbitral awards.

⁸ An "investor of a Party" is "a Party or a state enterprise thereof, or a national or an enterprise of a Party, that attempts through concrete action to make, is making, or has made an investment in the territory of another Party; provided, however, that a natural person who is a dual national shall be deemed to be exclusively a national of the State of his or her dominant and effective nationality." TPA, Art. 10.28.

⁹ Both the United States and Peru are Parties to the ICSID Convention and may thus avail themselves of the Convention and its Rules. For further information on arbitration under the Convention, see [<http://www.worldbank.org/icsid/>].