After more than seven years of political debate and controversy, TransCanada, the company behind the proposed Keystone XL pipeline, announced that it intends to seek more than $15 billion in damages because of the State Department’s rejection of its request for a Presidential Permit to construct and operate the cross-border facilities necessary for the pipeline to transport oil sands crude from Canada into the United States for ultimate delivery to Gulf Coast refineries. TransCanada filed a notice that it intends to sue the United States under the investor-state dispute settlement (ISDS) provisions of the North American Free Trade Agreement (NAFTA) just two months after the State Department denied the permit request on the grounds that its approval would have undermined U.S. global leadership on the issue of climate change, among other things. (TransCanada also filed a separate lawsuit in federal court seeking declaratory and injunctive relief, which is discussed in a separate CRS Legal Sidebar.) TransCanada has argued that the United States’ delay in processing, and ultimate rejection of, its permit application, breached U.S. obligations under NAFTA to: (1) accord its investment nondiscriminatory treatment (NAFTA Articles 1102 and 1103); (2) provide its investment with a minimum standard of treatment (MST) under international law (Article 1105); and (3) refrain from uncompensated expropriation of its investment (Article 1110).

TransCanada’s case may become relevant to the congressional debate over approval of the 12-nation Trans-Pacific Partnership trade agreement, which contains ISDS provisions that would enable an injured investor of a TPP member country with an investment in another TPP country to sue the country hosting its investment for breaching certain investment agreement obligations. This sidebar provides a few initial thoughts on TransCanada’s case based on the text of NAFTA and prior investment arbitration decisions. It is important to note that TransCanada has not yet filed a formal complaint setting out in detail its legal arguments, but it is expected to do so soon. Prior NAFTA investment tribunal decisions would not legally bind any future tribunal considering this case, but they may inform analysis of the issues.

The disputing parties will likely argue over which U.S. and foreign pipeline projects should serve as standards of comparison for evaluating TransCanada’s discriminatory treatment claims. TransCanada has alleged that the United States discriminated against it by subjecting Keystone XL to a lengthier presidential permitting process and ultimately rejecting the permit based on “new and arbitrary criteria.” Articles 1102 and 1103 of NAFTA generally require the United States to accord Canadian investors and investments treatment no less favorable than the treatment the United States provides to U.S. or foreign investors or investments “in like circumstances.” In determining that a domestic or foreign investor is “in like circumstances” with the complaining investor, some tribunals have considered, among other things, whether the comparator investor is in the same economic sector and subject to the same regulatory regime as the complaining investor, while other tribunals have suggested that the range of comparators should be defined more broadly.

Assuming that the comparator will be a company that built a pipeline requiring a U.S. permit, it is not clear whether the comparator’s project would have to be a cross-border oil pipeline requiring a Presidential Permit or a project subject to the same amount of controversy as Keystone XL. However, if the tribunal determines that the comparator must be a cross-border oil pipeline project of similar magnitude to Keystone XL, the disputing parties may argue over whether the
Canadian Alberta Clipper oil sands pipeline project, for which the State Department approved a Presidential Permit after about two years of review, could serve as a comparator with respect to TransCanada’s claims under Article 1103.

The disputing parties in the TransCanada case may also argue over the significance of the NAFTA investment arbitration panel’s 2015 decision in *Clayton/Bilcon v. Canada*. TransCanada has argued that the United States failed to accord its investment the MST in accordance with international law. The exact content of the MST obligation remains unclear, but prior NAFTA cases with factual similarities to the TransCanada case may provide some guidance as to what the obligation entails.

In *Clayton/Bilcon v. Canada*, a Delaware-based U.S. company sought to build a coastal quarry and marine terminal in Nova Scotia. The Canadian and provincial government ultimately denied Bilcon a permit to operate the project following an environmental review of the project. A NAFTA tribunal found that Canada breached the MST with respect to Bilcon in significant part because the Canadian environmental review panel, without notice to the investor, “adopted an unprecedented approach” that evaluated the project based on “a new standard of assessment rather than fully carrying out the mandate defined” by Canadian laws. Similarly, TransCanada has argued that the State Department’s rejection of its Keystone XL Presidential Permit request on the grounds that it would undermine U.S. efforts to encourage other countries to combat climate change was unprecedented and unrelated to the merits of the project, in part because the State Department concluded that construction and operation of the pipeline would not significantly impact climate change.

A NAFTA tribunal might look to *Bilcon* in deciding whether this conduct violated the MST. However, the United States could argue that the *Bilcon* case is distinguishable because, in that case, Canadian law provided specific factors and requirements for an environmental review, whereas the United States made the decision to reject the Keystone XL Presidential Permit according to a broad “national interest” standard that arguably provides a great deal of discretion to the executive branch.

TransCanada will likely face significant hurdles in arguing that the U.S. government expropriated its investment without payment of adequate compensation. Article 1110 of NAFTA protects a variety of property interests constituting “investments” from expropriation not undertaken: (1) for a public purpose; (2) on a non-discriminatory basis; (3) in accordance with due process and the MST; and (4) upon payment of adequate compensation. TransCanada appears to argue that the United States has effected an indirect expropriation by denying it a permit, thereby substantially interfering with its use of property such as construction equipment, pipe, land easements, and long-term contracts with shippers to transport oil.

To succeed on these claims, TransCanada may have to show that the permit denial “radically deprived” its investment of its economic value. In addition, an investor's reasonable expectations have played a key role in the outcome of arbitral decisions on expropriation. When the law in a particular field is uncertain, the investor may have difficulty establishing that it had reasonable investment-backed expectations regarding regulation of its investment. Moreover, when an investor enters a heavily regulated field (e.g., transportation of energy products), it may expect that government actions will negatively impact the value of its investment.
TransCanada, the company behind the proposed Keystone XL pipeline, has filed two legal challenges to the State Department’s recent decision not to issue the Presidential Permit needed for construction and operation of the pipeline across the U.S.- Canada border. One of these challenges, a claim that the State Department’s decision violates the North American Free Trade Agreement (NAFTA), is discussed in a separate CRS Legal Sidebar. The other challenge, a complaint filed with the U.S. District Court for the Southern District of Texas, alleges that the Constitution does not grant the President and the executive branch “unilateral power to prevent the domestic and international commerce reflected in the development and operation of a major U.S. oil pipeline extending abroad from established domestic oil pipeline systems.”

Specifically, TransCanada argues in the complaint that the permit denial should be invalidated and the executive branch should be enjoined from enforcing the rejection and permit requirement for the Keystone XL border-crossing facility because Congress, which is authorized by the Constitution to regulate domestic and foreign commerce, has addressed oil pipeline development generally, facilitated cross-border trade in petroleum products, and passed legislation that would have authorized the Keystone XL pipeline specifically were it not for a presidential veto. TransCanada claims that these expressions of congressional intent supersede any executive branch authority to regulate border-crossing pipelines. This argument appears intended to address two district court case decisions in the last decade, Sisseton-Wahpeton Oyate v. U.S. Department of State and Sierra Club v. Clinton, which upheld the executive branch’s authority to permit pipeline border crossings based, in part, on the absence of congressional action regarding oversight of such facilities.

In both cases the district courts rejected arguments that the State Department and the President do not have authority under the Constitution to grant Presidential Permits because the Constitution reserves the power to regulate foreign commerce to Congress. Those decisions held that issuing permits for border-crossing facilities was a valid exercise of the executive branch’s authority to conduct “foreign affairs” or “foreign policy.” However, both courts seemed to acknowledge that Congress has concurrent or even primary authority to authorize and regulate such facilities, and the executive branch’s authority to do so relies, at least in part, on the absence of a legislative framework for such authorization and regulation. The court in Sisseton-Wahpeton Oyate found that the executive branch permitting authority depends, in part, on the fact that “Congress has failed to create a federal regulatory scheme for the construction of oil pipelines, and has delegated this authority to the states”; while the court in Sierra Club noted that “Congress has not attempted to exercise any exclusive authority over the permitting process” and that “Congress's inaction suggests that Congress has accepted the authority of the President to issue cross-border permits.”

TransCanada attempts to differentiate its case from the Sisseton-Wahpeton Oyate and Sierra Club cases by arguing that: (1) Congress has passed laws that govern interstate oil transportation and that “facilitate cross-border trade and investment between the United States and Canada”; and (2) Congress passed legislation opposing “the President’s attempt to unilaterally exercise power over the Keystone XL Pipeline.” If the U.S. District Court for the Southern District of Texas defers to Sisseton-Wahpeton Oyate and Sierra Club on executive branch authority to permit border-
crossing facilities, TransCanada’s first argument may be unpersuasive since many of laws TransCanada cites were in effect when the *Sisseton-Wahpeton Oyate and Sierra Club* decisions were decided, which suggests that the *Sisseton-Wahpeton Oyate and Sierra Club* courts found that those laws did not affect presidential authority to permit border-crossing pipeline facilities.

TransCanada’s second argument attempts to distinguish the circumstances surrounding the Keystone XL permitting decision from those in *Sisseton-Wahpeton Oyate and Sierra Club*. In order to rule in favor of TransCanada based on this argument, the U.S. District Court for the Southern District of Texas would have to find that by citing the inaction of “Congress,” the courts in *Sisseton-Wahpeton Oyate and Sierra Club* were referring not to enactment of a legislative framework but rather to more limited action. Examples of congressional action cited in the TransCanada brief include: legislation enacted by the 112th Congress that mandated a decision on a previous Keystone XL permit application by a certain date; various pieces of legislation in the 113th Congress authorizing the pipeline that passed the House but not the Senate; and legislation in the 114th Congress to approve the pipeline that the House and Senate passed but the President vetoed. None of these appear to constitute a legislative framework for permitting cross-border pipeline facilities as the *Sisseton-Wahpeton Oyate and Sierra Club* envisioned, but they do indicate congressional intent with respect to the Keystone XL pipeline that was absent in those cases. Of course it is also possible that the U.S. District Court for the Southern District of Texas may simply reach a conclusion about the legitimacy of executive branch authority to regulate border-crossing facilities that differs from the conclusions reached by the courts in *Sisseton-Wahpeton Oyate and Sierra Club*. Those cases were also district court decisions, and while the court is likely to take them into consideration, they are not binding.

TransCanada’s complaint also argues that even if Congress had not expressed its intent regarding Keystone, this particular permitting decision would still go beyond the power granted to the executive branch under the Constitution. TransCanada claims that this decision represents an expansion of the previously exercised authority upheld in those cases because “[u]ntil now, those limited regulatory powers have been directly related to issues concerning the border crossing and have never been asserted to bar the development of a significant, predominantly domestic facility.” Distinguishing the Keystone XL case from the previous decisions approving the issuance and enforcement of Presidential Permits for border-crossing facilities as legitimate exercises of the President’s foreign affairs authority, TransCanada also notes that “[u]pon information and belief, the permit applications submitted by TransCanada for the Keystone XL Pipeline are the only applications for a major infrastructure project addressed pursuant to Executive Order 13337 that any President has ever denied.” Whether this is sufficient for the court to find that the State Department’s decision is not a legitimate exercise of that authority remains to be seen. A government response to the TransCanada complaint is presumably forthcoming, with a decision likely several months away.

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