

**THE POTENTIAL IMPACT OF INTERNATIONAL TRADE AGREEMENTS  
ON GROUND WATER WITHDRAWAL REGULATIONS**

**REPORT TO THE JOINT STANDING COMMITTEE  
ON NATURAL RESOURCES**

**BY THE**

**WATER RESOURCES PLANNING COMMITTEE**

**AND THE**

**CITIZEN TRADE POLICY COMMISSION**

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## **Executive Summary**

**Introduction:** International trade policies and agreements are complex and developed through lengthy negotiations at the national level. Currently, they are negotiated without meaningful consultation with the states. Their focus is to open trade opportunities and to limit barriers to trade in the global economy. Some aspects of trade agreements may affect state sovereignty and regulatory authority.

The 124<sup>th</sup> Legislature passed Public Law 2009, chapter 132, which directed the Water Resources Planning Committee, in coordination with the Office of the Attorney General and the Citizen Trade Policy Commission, to conduct an examination of the potential legal impacts of international trade agreements on the State's ability to manage its ground water resources, including, but not limited to, the potential consequences of permitting foreign companies to extract ground water.

The *Citizen Trade Policy Commission (CTPC)* was established by the Legislature in 2003 to provide an on-going state-level mechanism to assess the impact of international trade policies and agreements on Maine's state and local laws, business environment, and working conditions. The *Water Resources Planning Committee (WRPC)* was established by the Legislature under the Land and Water Resources Council in 2007. The overarching charge to the WRPC is to plan for sustainable use of water resources. The Office of Attorney General is also involved in this review effort due to the complexity of legal issues involved in trade agreements and water law. A representative from the Office of Attorney General also sits on the CTPC.

**Study process:** The WRPC and the CTPC held five joint meetings from July through December 2009 to discuss various aspects of international trade agreements and ground water. Included in these discussions were an overview of Maine's ground water resources, a review of Maine's current regulatory environment for ground water withdrawals, a review of Maine ground water law, and an overview of international trade agreements.

The WRPC and CTPC were fortunate to have Mr. William Ware (Adjunct Prof., Harrison Institute for Public Law, Georgetown University and Policy Director, Forum on Democracy & Trade) participate in several meetings. He agreed to develop an overview paper focused on our question of the potential impact of international trade agreements on ground water regulations.

The CTPC and WRPC held a public hearing on October 15, 2009 at the State House for the purpose of receiving public input to the discussion on the potential impacts of international trade agreements on the State's ability to regulate ground water withdrawals. About thirty people attended the hearing and twenty-one people spoke, presenting a broad spectrum of interests and concerns on the topic. Some key points expressed at the hearing were: 1) continue to carve water out of international trade agreements; 2) concern about dispute resolution through tribunals; 3) a view that the State would be better positioned to protect ground water resources if ground water were placed within the public trust; 4) support for economic development through international investment agreements; 5) the view that current state regulations are adequate to protect resources and existing uses.

The WRPC and CTPC also reviewed several timely articles and legal briefs focused on international trade and water resources.

## Conclusions and recommendations:

The following recommendations and conclusions received the unanimous consent of the members of the Citizen Trade Policy Commission and the members of the Water Resources Planning Committee.

The Maine Legislature should continue to make decisions regarding ground water and other natural resources using a transparent process with opportunity for public input, and state agencies should continue to apply the law in a manner consistent with due process. International trade agreements, which are currently negotiated without sufficient consultation with states, contain provisions that could expose Maine laws to challenges in international tribunals whose decisions take precedent over state and federal law. There is potential for these treaties to undermine our state's capacity to put laws into place that protect the health and well being of our citizens. The Legislature and the CTPC should take action to monitor these trade negotiations and agreements. They should further take action to seek to change this undemocratic system in which agreements are negotiated without transparency and without meaningful consultation with the states.

- 1) In future policy deliberations, the Legislature should consider that the best defense against challenges under international trade agreements is to continue its existing process of adopting regulations that are clear, reasonable, have a sound basis, are applied equitably, and that are established through due process.

Articles and legal briefings by attorneys from diverse backgrounds all confirm this view. Maine's current regulatory framework for ground water withdrawals evolved over years of public debate, and focus on impacts of withdrawals on other water-dependent resources and activities, rather than discriminating against particular uses of ground water, and thus position the State well against challenges under international trade agreements.

- 2) The Legislature should encourage the development of a better system for consultation between the State and the U.S. Trade Representative (USTR) as future trade agreements are negotiated.

Currently, states have little input as trade agreements are negotiated. The negotiating process lacks transparency and precludes states from any meaningful participation in the negotiations even though the agreements have significant potential impact on state regulatory authority. The Legislature should encourage our Congressional Delegation to establish a more inclusive and transparent process for USTR consultation with states on trade matters that have the potential for impacting states.

- 3) The Legislature should encourage Maine's Congressional Delegation to insist on the codification of these two specific tribunal decisions regarding certain disputes under international trade agreements:

- a. *Methanex* decision. The NAFTA tribunal in *Methanex v. United States* soundly rejected Vancouver-based Methanex Corporation's claim for nearly a billion dollars in compensatory damages for California's phase-out of the gasoline additive MTBE because it was polluting lakes and ground water and was endangering the public health.

- i. Specifically, narrow indirect expropriation so that it does not apply to nondiscriminatory regulations as explained in the *Methanex* award. In other

words, establish that the adoption or application by any national or sub-national government of any bona fide and non-discriminatory measure intended to serve a public purpose shall not constitute a violation of an expropriation article of an investment agreement or treaty.

- b. *Glamis* decision. The tribunal ruled for the U.S. when a Canadian corporation sued under NAFTA for actions taken by the Department of Interior and the State of California, imposing environmental and landuse regulations on Glamis's proposed open-pit gold mine.
  - i. Specifically, narrow the minimum standard treatment to the elements of customary international law as explained in the U.S. brief in *Glamis*, in which the State Department argued for a reading of MST confined to three elements: (1) compensation for expropriation, (2) "internal security," and (3) "denial of justice" where domestic courts or agencies (not legislatures) treat foreign investors in a way that is "notoriously unjust" or "egregious" such as a denial of procedural due process. Further, the expectation of a stable or unchanging legal environment is not to be understood as part of customary international law.

- 4) The Legislature may wish to consider requiring that future contracts between governmental units in Maine and private investors include a waiver of any right by investors to seek compensation through international investment arbitration.

The lack of clarity, certainty, and predictability in international trade and investment law allows international arbitration tribunals broad discretion. While some tribunals have used their discretion wisely and prudently, the precedents of past decisions do not bind future tribunals.

Requiring such a waiver in governmental contracts would move dispute resolution from international arbitration tribunals to U.S. courts, where precedential actions are an important foundation of the judicial process. Some consideration should be given, however, to whether such action would put Maine at a competitive disadvantage for international investment and whether such a waiver could be used to show discrimination against a certain class of private investors.

- 5) Because of the potential impact of international trade agreements on state sovereignty and state regulatory authority, the Legislature should provide adequate support for the CTPC so that it can do the work with which it is charged by statute. While the Commission has received national recognition for its work since its inception and has served as a model for other states wishing to establish similar citizen commissions, recent funding cuts have left the CTPC without any staff assistance and it currently lacks the capacity to adequately monitor, assess and respond to the complex and complicated issues involving international trade agreements and their consequences to the people of Maine. The Legislature should therefore consider establishing a position that would:
  - a. Support the Maine Citizen Trade Policy Commission in monitoring negotiations on international trade agreements and case law from tribunal settlements and support it in providing input to the Legislature, Governor, Maine Congressional

Delegation and the U.S. Trade Representative on international trade issues and their impact on the people and economy of Maine.

- b. Assist the CTPC with reviewing the potential impacts of international trade agreements on state regulatory authority and support the CTPC in advising the Legislature and legislative policy oversight committees when considering such impacts in policy decisions.
  - c. Assist in communicating concerns and needed actions to the Legislature, Governor, Congressional Delegation, U.S. Trade Representative, and others.
- 6) a. We recommend that the Legislature encourage the U.S. Trade Representative and Maine's Congressional Delegation to continue to carve water out of future international trade agreements and existing agreements that may be renegotiated.
- b. The research undertaken for this report did not identify any decisions that shed light on the specific issue of whether a legislative change to a public trust rule governing ground water would improve the chances of a Maine regulatory statute withstanding a challenge based on a trade treaty.

Some members of the public supported taking steps to protect Maine's ground water due to its importance and the potential impacts of world shortages and global warming. These measures included continuing to carve water out of international trade agreements, and changing the standard governing the use of Maine's ground water to a public trust.

Many of the speakers at the public hearing expressed concern about the impact of treaty provisions on Maine's system of regulating the use of ground water. Several speakers emphasized that water is different from the vast majority of products that are subject to trade agreements, and even other natural resources in that it is necessary to life. The importance of water is reflected in existing state and federal regulation, designed to ensure both its safety and continued availability.

For these reasons, water should continue to be carved out of international trade agreements. As treaties are negotiated, the parties decide which products and services should be covered, and bargaining determines those that are included. The unique nature of water makes it ill-suited for this type of decision making, i.e., extending treaty coverage to water in return for coverage of some sought after product(s) of the bargaining partner. Water is not a good or a product in the common usage of those terms. While there are serious shortages of water in parts of the world, and even in parts of the United States, resolution of this issue should not be determined by private investors exercising rights that they believe are conferred on them by trade treaties.

The concept that Maine should change the doctrine governing ground water to one of public trust is a more complex issue. The substantial research that has been conducted for this report did not identify any decisions made under the provisions of any trade treaty that address the concept that moving to a public trust rule would improve the likelihood of withstanding a trade treaty challenge.

However, there are potential legal consequences under state and federal law if the Legislature were to adopt a public trust rule. Litigation in state or federal court challenging the impact of the specific changes upon ownership interests would be likely. The legal issues involved in resolving such a challenge are complex, and the outcome cannot be predicted with certainty,

but if such a challenge were successful, it seems likely that the potential damages that could be awarded would be high.

As the Maine Law Court noted in declining to judicially abrogate the absolute dominion rule, there are “heavy policy considerations” involved in making such a change that render it more suitable for legislative study and decision. *Maddocks v. Giles*, 1999 ME 63, 728 A.2d 150, ¶ 12. Such a study and recommendations concerning the policy and regulatory implications of changing the absolute dominion rule are beyond the scope of the charge to this group, and are clearly material to any decision that a different rule would lead to a better water policy for the State. As emphasized in our first recommendation, the best protection against treaty challenges is the establishment of sound regulatory measures, grounded in science and facts, developed through a legislative and rulemaking process that encourages public input, and that are applied to all, consistent with due process. Maine has a thorough regulatory system for water resources that meets this standard.

## THE POTENTIAL IMPACT OF INTERNATIONAL TRADE AGREEMENTS ON GROUND WATER WITHDRAWAL REGULATIONS

### Introduction

International trade policies and agreements are complex and developed through lengthy negotiations at the national level. Currently, they are negotiated without meaningful consultation with the states. Their focus is to open trade opportunities and to limit barriers to trade in the global economy. Several aspects of international trade agreements should be of concern to the Maine Legislature.

- The U.S. Trade Representative negotiates trade agreements at the national level. State views on the potential impacts of agreements may not always be well represented during those negotiations, involving little consultation with the states and inadequate information about the agreements on state sovereignty and regulatory authority.
- In certain circumstances, regulations in Maine intended to protect public health and/or the environment may be viewed by some as “barriers to trade” and may be the target of challenges under trade agreements.
- Disputes under trade agreements are resolved through international arbitration tribunals rather than courts.
- Additional trade agreements are the subject of on-going negotiations.

All of these may affect state sovereignty and the ability of the State to govern itself through democratic processes. This report specifically examines the State’s ability to manage ground water resources in the arena of international trade.

The 124<sup>th</sup> Legislature passed Public Law 2009, chapter 132, which directed the Water Resources Planning Committee, of the Land and Water Resources Council, in coordination with the Office of the Attorney General and the Citizen Trade Policy Commission, to conduct an examination of the potential legal impacts of international trade agreements on the State's ability to manage its ground water resources, including, but not limited to, the potential consequences of permitting foreign companies to extract ground water. The examination was to include a review and assessment of the following subjects as they relate to or impact international trade agreement issues and the State's regulation of its ground water:

1. Property rights related to the ownership of ground water.
2. The various common law doctrines relating to the use of ground water, including the absolute dominion rule and the reasonable use rule.
3. Natural resources other than ground water.

Our review focused on the first two points. We did not specifically address the third point on resources other than ground water, but the results of our work can be instructive in considering these other resources.

The *Citizen Trade Policy Commission (CTPC)* was established by the Legislature in 2003 to provide an on-going state-level mechanism to assess the impact of international trade policies and agreements on Maine’s state and local laws, business environment, and working conditions. The 22-member Commission includes six Legislators, an Attorney General designee, representatives from the Department of Labor, the Maine International Trade Center, the Department of Environmental Protection, the Department of Agriculture, Food, and Rural

Resources, and the Department of Human Services, and ten public members representing business, labor, health, government, and environmental interests.

The *Water Resources Planning Committee (WRPC)* was established by the Legislature under the Land and Water Resources Council in 2007. The WRPC draws its membership from state agency ground water professionals, water utilities, agricultural water users, the bottled water industry, other commercial water users, private well drillers, and a water advocacy organization. The overarching charge to the WRPC is to plan for sustainable use of water resources. This is accomplished through scientific investigations and improved water resource data in watersheds deemed potentially at risk from overuse of water resources, and to convene planning groups in watersheds where cumulative use approaches unsustainable conditions.

The Office of Attorney General is also involved in this review effort due to the complexity of legal issues involved in trade agreements and water law. A representative from the Office of Attorney General also sits on the CTPC.

Appendix A includes membership lists for the WRPC and the CTPC.

## **Background**

Water policy has been an important focus of the Maine Legislature over the past several decades. We provide here a summary of key efforts. The Appendix contains a thorough review.

*Ground Water Protection Commission – 1978-1980.* This Commission made broad recommendations regarding investigations and mapping of the State’s aquifers, most of which has been accomplished in the succeeding decades.

*Water Transport Law, 1987.* Facing the threat of large-scale water transport to southern New England, the Legislature passed this law to prohibit transport of water across town lines in containers larger than 10 gallons. Through appropriate regulatory review, exemptions are permitted for three-year terms.

*Water Supply Study Commission, 1987-1990.* This effort focused on the adequacy of the State’s water supply for all uses, potential impacts from water export, and adequacy of regulations. The Water Resources Management Board established through this effort.

*Water Resources Management Board, 1989-1990.* This stakeholder board recommended several changes to water policy. The Legislature should:

- adopt the “reasonable use” doctrine for ground water;
- establish priorities for use where supplies are limited;
- replace the Water Transport Law with a permitting process;
- encourage water conservation;
- implement a strategy for collecting water supply and use data.

*Sustainable Water Use Policy Process, 2000-2002.* This stakeholder process focused on water use information and policies related to in-stream flows, and marked the beginning of a lengthy process that culminated in the Chapter 587 in-stream flow rules administered by the Maine DEP.

*Water Use Reporting Law, 2002.* This law grew from the previous process and requires all major surface and ground water users to report volumes to the State annually.

*Review of Ground Water Regulations Working Group, 2005-2007.* This stakeholder group conducted a comprehensive review of the then current regulations governing withdrawals of ground water. Among the chief work done by this group was a systematic review of water supply and demand in watersheds statewide. This effort revealed that Maine does not have a statewide crisis with regard to water use, but that there are some watersheds that should be the focus of additional investigations. The Working Group recommended:

- addressing water issues through a watershed approach;
- establishing a Water Committee to oversee water information and investigations;
- establishing a permitting process for significant wells under the Natural Resources Protection Act.

*Water Resources Planning Committee, 2007 – to-date:* This Stakeholder Committee is charged with coordinating agency water information, conducting water investigations in watersheds where demand is a high percentage of supply, and convening planning groups in watersheds as needed.

*Significant Ground Water Well Permit, 2007:* The Legislature established the Significant Well Permitting Program within the Natural Resources Protection Act for high-volume wells – those pumping at least 50,000 gallons per day within 500 feet of water bodies, and those pumping at least 144,000 gallons per day more than 500 feet from a water body.

*124<sup>th</sup> Legislature, First Regular Session, 2009:* The Legislature debated fourteen bills dealing with ground water, most of them focused on concerns with bottled water. Several of these bills grew from two recent events: exploration for a potential bottled water source in Shapleigh; a potential long-term contract for water between the Kennebunk-Kennebunkport-Wells Water District and a commercial bottler.

A more complete historical perspective is offered in Appendix B.

## **Domestic Legal Context**

### 1. Common Law Doctrines Governing Use of Ground Water<sup>1</sup>

Ground water law has developed on a state by state basis, typically separate from the law governing the use of surface water. States now recognize several different common law ground water doctrines, and most, including Maine, have also enacted statutes that significantly modify these common law principles. Bulk sales of ground water for bottling purposes can be conducted under any of these doctrines, provided that any regulatory requirements applicable to extraction (which may differ from state to state) are satisfied.

In *Maddocks v. Giles*, 1999 ME 63, 728 A.2d 150, the Maine Law Court rejected the argument that Maine’s version of the absolute dominion rule had become outdated and should be judicially abrogated, concluding (among other things) that the “heavy policy considerations” involved in this issue made it more suitable for legislative study and decision. ¶ 12. Such a study and recommendations concerning the policy implications of changing the absolute

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<sup>1</sup> The information in this section of the Report is derived from Assistant Attorney General Paul Gauvreau’s paper, “Review of International Trade Agreements and the Management of Groundwater Resources: a Review of Maine Groundwater Regulation,” dated September 11, 2009. It can be found at: <http://www.maine.gov/legis/opla/ctpcadditionalmtmatsept112009.pdf>, pp. 18-28.

dominion rule are beyond the scope of the charge to this group, and would appear to be material to any decision that a different rule would lead to a better water policy for the State.

(a) Absolute Dominion Rule: For over 130 years, Maine has relied on the absolute dominion rule to govern ownership of ground water by common law. The absolute dominion rule is based on the premise that the owner of the surface land above ground water owns the water, much like the soil and rocks. However, unlike the soil and rocks, the amount of water existing under a defined parcel of land will rise and fall, depending on the usage of other landowners and relevant weather conditions such as (most obviously) rainfall. Generally the restrictions imposed by statute on the absolute dominion rule concern the *use* of groundwater rather than its *ownership*. For example, while the amount of water extracted may be subject to limitations, its ownership remains with the owner of the land.<sup>2</sup>

There are a number of regulatory statutes that apply to ground water, which are listed below (see page 10). As a result, Maine's rule would more accurately be described as a modified absolute dominion rule.

(b) Reasonable Use Rule: This rule provides that a landowner's use of ground water must bear a reasonable relationship to his or her use of the land above the ground water. It gives courts the authority to restrict uses which cause unreasonable harm to other users within an aquifer, which the absolute dominion rule would not support. As a result, the reasonable use rule may require balancing between competing uses from the same aquifer.

As hydrogeological principles became better understood, and competing societal needs for ground water developed, the trend has been away from the concept that the owner's right to sub-surface waters is unqualified. Thus, the reasonable use rule replaced the absolute dominion rule in many jurisdictions.

(c) Correlative Use Rule: The owners of overlying land and the non-owners or water transporters have correlative or co-equal rights in the reasonable, beneficial use of ground water, and the authority to allocate water is held by the courts under this rule. If an aquifer cannot accommodate all ground water users, the courts may apportion the uses in proportion to their ownership interest in the overlying surface estates.

A disadvantage of this rule is that litigation is required on a case by case basis to apportion uses; however, the judicial power to allocate water rights protects the public interests as well as the rights of private users.

(d) Prior Appropriation Rule: Under this rule, the first landowner to beneficially use or divert water from a water source is granted priority of right. Rights are obtained by putting the water to a beneficial use, and new users are not allowed to interfere with existing senior rights. The amount of groundwater that senior appropriators may withdraw can be limited based upon reasonableness and beneficial purposes. Some states that rely upon this rule have adopted a regulatory permitting system.

While prior appropriation is relatively easy to apply to surface waters where unappropriated waters are visible and available, it is difficult to apply with ground water, where intensive, deliberate study is necessary to assess the quantity and availability of ground water.

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<sup>2</sup> The concept of ownership is sometimes difficult to apply to ground water, for example, ground water taken from an aquifer that lies under several parcels of land.

(e) Restatement of Torts Rule: Under this rule, a landowner who uses ground water for a beneficial purpose is not subject to liability for interference with another's use unless the withdrawal: unreasonably causes harm to a neighbor by lowering the water table or reducing artesian pressure; exceeds a reasonable share of the total store of ground water; or creates a direct and substantial effect on a watercourse or lake and unreasonably causes harm to a person entitled to the use of its water.

(f) Public Trust: The Hawaii Constitution states that "all public resources are held in trust by the state for the benefit of its people." Haw. Const. art. XI, § 1. It further establishes a public trust obligation "to protect, control and regulate the use of Hawaii's water resources for the benefit of its people." Haw. Const. art. XI, § 7. Hawaii is an example of a state that follows this rule for ground water.

## 2. Current regulatory framework governing water withdrawal

- *Water Use Reporting:* The Maine Department of Environmental Protection, in coordination with other state agencies, maintains a water use-reporting program. All water users above 20,000 gallons/day are required to report their usage.
- *Site Location of Development regulations.* Any major new facility that disturbs at least 3 acres of area must get a Site Location permit from the Maine DEP. The applicant must show that the development will not have an adverse impact on the environment. If the facility involves water extraction, such as a bottling facility, geologists at the DEP require a thorough analysis of the water resources and impacts of any proposed withdrawals on other resources. Permittees are required carefully monitor water usage and to submit reports of water usage.
- *Bottling facility license.* The Maine Department of Health and Human Services licenses water bottlers in Maine. The DHHS must approve any new source for human consumption. As part of their analysis, geologists at DHHS also review the impact of withdrawals on other water uses in the area.
- *Bulk Water Transport.* If a water developer wishes to move water in bulk (containers larger than 10 gallons) across a town line, say from a wellhead to a bottling facility, they need approval from the Maine DHHS under the Bulk Water Transport law. Geologists at DHHS, the Maine Geological Survey, and the Maine DEP rigorously review applications for water transport.
- *Wells in LURC jurisdiction.* In areas of the state regulated by LURC, permits are required for any large-scale ground-water extraction. The applicant must show that the development will not have an adverse impact on the environment. Staff from LURC and the Maine Geological Survey rigorously review these applications. Permittees are required to carefully monitor water usage and to submit reports on water usage to LURC. Permits are conditioned and withdrawals may be limited based on resource conditions.
- *Significant Well permit.* Any well within 500 feet of surface water producing 50,000 gallons or more per day (144,000 gpd if more than 500 feet) must be permitted under the Natural Resources Protection Act by the Maine DEP. Exceptions for irrigation wells. This includes wells previously permitted under Bulk Water Transport. The applicant must show no adverse impact on ground water, surface water, water-related natural resources, or existing uses. Permittees are required carefully monitor water usage and to submit reports of water

usage. Permits are conditioned and withdrawals may be limited based on resource conditions.

- *Chapter 587 In-stream flow rules.* Wells may not be pumped in such volumes as to reduce flows in nearby streams below seasonally defined threshold flows.

3. Constitutional protections against taking property without just compensation: the takings clause as it applies to possible ownership changes.<sup>3</sup>

Both the U.S. and Maine Constitutions prohibit the taking of private property for public use without just compensation. A legal challenge to any statutory change in the ownership rights of a landowner in ground water could be brought on the basis of a complete loss of the use of the property (a *per se* claim) or on a fact-based case-by-case basis (an *ad hoc* claim). Absent a physical occupation of land or a complete denial of all economically beneficial use of the land, the courts are more likely to apply the *ad hoc* fact-based analysis.

There is no bright-line test for what constitutes an *ad hoc* taking, and careful examination of all relevant facts and the application of the specific regulatory requirement at issue is necessary. The three-part test applied by a court when a fact-based takings claim is made includes:

(a) The economic impact on the property owner. A court would examine the value of a landowner's property in light of the challenged regulation and compare it to the value without the new requirements, and then determine whether the value of the property has been so severely diminished that it has been rendered substantially valueless. Mere diminution in value, even if significant, has been found insufficient; the inability to put property to its most profitable use has also been found insufficient where the property retains some value under permitted uses.

(b) Legitimate investment backed expectations. The U.S. Supreme Court has said that a landowner does not have a constitutional right to a frozen set of laws and regulations. For example, a landowner cannot rely on the maintenance of the same zoning. Facts regarding a landowner's knowledge of actual or potential regulations when the property was bought or developed will be relevant to whether his expectations are reasonable.

(c) The character of the government action. The courts will also look at the legitimacy of the government regulation when analyzing its restriction on the use of property. If the purpose of a statute or regulatory system is to protect the environment, it will likely be upheld as a legitimate exercise of the state's police power.

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<sup>3</sup> The material in this section of the Report is taken from Assistant Attorney General Peggy Bensinger's paper, "The Takings Clause of the U.S. and Maine Constitutions: How They Might Impact Legislation Modifying Groundwater Ownership," dated September 11, 2009. It can be found at: <http://www.maine.gov/legis/opla/ctpcadditionalmtmatsept112009.pdf>, pp. 29-32.

## Brief Review of International Trade Agreements<sup>4</sup>

General. A description of how trade treaties operate will put the question of their impact on ground water in context. To begin with, there are numerous treaties to which the U.S. is a party that can potentially apply to any particular good or service. The General Agreement on Tariffs and Trade, or the “GATT,” and the General Agreement on Trade in Services, or the “GATS,” are administered by the World Trade Organization (“WTO”), which has 153 member countries. There are also regional trade treaties, such as NAFTA and CAFTA. Finally, there are bilateral trade agreements between two countries; if they contain investment agreements they may also be referred to generally as “IIAs.” The U.S. is a party to numerous bilateral agreements, and new ones are always in development.<sup>5</sup> Some bilateral trade agreements are bilateral investment treaties (“BITS”), which are specifically designed to protect investments in countries where typical legal protections for business are not otherwise in place.

The parties to a treaty will negotiate the products or services that are covered, referred to as “commitments,” frequently by identifying “sectors,” which are related goods or services. Within these commitments countries may identify exceptions, which are called “carve-outs.” The U.S. has committed more than ninety different service sectors under the GATS, and these will likely differ from the service sectors committed to coverage by other countries. The parties will also establish the legal requirements that apply to trade under the treaty, which generally contain substantive and procedural protections for the participants, as well as certain very limited exceptions to the coverage of these rules. These rules are the primary reason why international trade treaties have potential effects on state laws and regulations, in that they focus on the type of regulation perceived as non-tariff barriers to trade. And in the case of the GATS, the most far-reaching of all the WTO agreements, the detail of these trading rules continues to be a subject of negotiation. None of the current commitments by the U.S. or any other country has identified water as a sector.<sup>6</sup>

Claims that a country has violated a treaty are brought country to country (or, in the case of investor claims, discussed below, by an investor against a country). So for example, if a claim were brought asserting that a Maine law violates a particular treaty obligation, the claim would be brought against the U.S. and defended by the U.S. Department of State with support from the State of Maine. Claims are litigated through an arbitration process rather than by the courts, resulting in a decision that is binding only on the parties to the dispute. Damages may be awarded to a prevailing country or investor.

Investment provisions. NAFTA’s Chapter 11 gives investors the right to bring treaty challenges against a country in which they have a presence and are doing business, as do other international investment agreements and the BITS. The GATT and GATS do not permit investor challenges.

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<sup>4</sup> The material in this section of the Report is largely taken from the “Final Report on Water Policy and International Trade Law,” by William Waren, Policy Director of the Forum on Democracy and Trade, and Adjunct Professor, Harrison Institute for Public Law, Georgetown University, dated December 8, 2009, and referred to herein as “the Waren Report.”

<sup>5</sup> A list of countries with which the U.S. has bilateral trade agreements, and the text of those agreements, can be found on the USTR’s web site at <http://www.ustr.gov/trade-agreements/free-trade-agreements>.

<sup>6</sup> Waren report, page 4.

A. Expropriation. Member nations are required to compensate investors if national, state or local governments “directly or indirectly nationalize or expropriate” an investment of the other countries' investors in its territory. The definition of investment is broader than that of constitutionally protected property rights in this country. The substantive standards are also more generous. By way of comparison, unconstitutional regulatory takings must effectively deprive the owner of all uses of the property.

In *Methanex v. U.S.*, California’s ban on methanol, the key ingredient in the gasoline additive MTBE, was challenged under NAFTA as an expropriation of property by a Canadian company that was its largest producer through two of its U.S. based subsidiaries. The ban was based on the unique threats that MTBE posed to the environment and public health in the state, where a number of public water supplies were contaminated with the water-soluble substance. A number of other states had enacted laws requiring phase-out and ban of MTBE.

The arbitration tribunal concluded that a nondiscriminatory regulation for a public purpose, enacted in accordance with due process and which affects a foreign investment among others does not constitute expropriation in the absence of specific commitments to refrain from regulation were made to the investor. This interpretation of the expropriation rule not only clarifies it, but does so in a manner that accommodates much of what American courts would determine to be within the scope of governmental regulatory authority. Because the lack of precedential status of arbitration decisions means that government cannot rely on this interpretation for protection (when, for example, crafting legislation), a number of parties have advocated for the codification of the Methanex rule in treaties with investor rights.

B. Minimum standard treatment. International investment agreements also require member nations to provide foreign investors with a “minimum standard of treatment” under international law. This standard includes a right to “fair and equitable treatment and full protection and security.” While the concept embedded in this general standard can be read to approximate due process, it can also be read more broadly to permit an aggressive review of economic regulation.

As a result, certain of the decisions interpreting minimum standard treatment have found that it imposes a duty on government to maintain a stable and predictable legal environment together with consistent behavior and transparent requirements. Such broad protections of investors make it difficult to establish bona fide regulatory requirements to address new developments, something that the Legislature is often called on to do and which comports with due process as state and federal courts have interpreted it.

For this reason, the successful defense of *Glamis Gold v. United States* was especially significant. In *Glamis*, a Canadian company made a claim under NAFTA seeking \$50 million in compensation based on the actions of the federal and California governments in imposing environmental and land use regulations on Glamis’ proposed open pit gold mining operation in an area that is sacred to the Quechen Indian Nation. In declining to adopt the “stable regulatory environment” standard, The tribunal concluded that the stable regulatory environment was not supported by international law, and that to violate the fair and equitable treatment standard, an action by a nation-state must be either 1) sufficiently egregious and shocking as to be a gross denial of justice, or 2) creation by the state of objective expectations in order to induce investment followed by repudiation of

those expectations. Again, given the lack of precedential effect of this decision, codification of this standard would provide needed guidance. One of the proposals is to codify the MST standard along the lines that the U.S. argued in its Glamis brief, so that it covers three elements: 1) compensation for expropriation; 2) a lack of internal security sufficient to protect foreign businesses according to accepted international law standards; and 3) denial of justice by courts or agencies in a manner that is notoriously unjust.

Other relevant standards established by treaties. As can readily be seen by the extensive analysis in the Waren Report that addresses the extent to which bottled water and bulk water sales may be covered by existing trade agreements, it is a complex task to simply determine whether a product or service is covered. It is not practical to assess each proposed regulatory measure, whether legislative or administrative, for possible treaty implications. Such an approach would require the following steps: 1) identifying the trade agreements that cover the product or service; 2) determining what, if any, standards might be used to challenge the regulation; 3) if a potential violation is identified, determining whether any exceptions in the agreement might apply; and 4) in the case of agreements that allow investors to bring challenges, analyzing their potential claims.

Not only would such an approach be burdensome and impractical, it would detract from the long established legislative and administrative processes that are based on regulating in the public interest based on facts elucidated in a public process according to well developed case law outlining rights conferred by statute and constitution. Rather, as we recommend below, government should continue to operate as it has, but with awareness of the most prominent of the treaty standards, as outlined herein.<sup>7</sup>

In addition to the investment agreement standards of expropriation and minimum standard treatment discussed above, the following standards are commonly relied upon.

A. GATT Rules:

1. Most favored nation: any advantage granted to any product originating in or destined for any other country shall be accorded to the like product originating in or destined for the territories of all other contracting parties.
2. No restrictions other than duties, taxes or other charges: prohibits restrictions on importation of any product from another party's territory through quotas, import or export licenses or other restrictions.

B. GATS Rules:

1. National treatment: prohibits discrimination in favor of domestic suppliers, including laws that change conditions of competition;
2. Market access: prohibits quantitative limits on service suppliers or volume of service.

C. GATS Exceptions: conflict with a trade rule is excused if a necessity test is met and the purpose of the measure is 1) necessary to protect public morals; 2) necessary to

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<sup>7</sup> The WTO's continuing efforts to negotiate standards specific to the "domestic regulation" of its member countries is of course a significant potential source of new requirements, but there are also treaties in negotiation at any point in time as well as negotiations to clarify or adjust existing treaty commitments and standards. In short, this is not a closed process.

protect human or animal health; 3) necessary to protect privacy or prevent fraud; 4) necessary in the view of each country to safeguard essential security interests.

### **Study process**

The process for this study consisted of joint meetings of the CTPC and WRPC, a public hearing, and development and review of various reports.

*Summary of meetings of the CTPC and WRPC.* The CTPC and the WRPC held joint meetings on five occasions from July through December 2009.

July 24, 2009: This was an organizational meeting where the CTPC and the WRPC considered the questions that should be the focus of our investigations/discussions, an outline of the review process, and preliminary planning for a public hearing. The CTPC was able to engage Mr. William Waren of the Forum on Democracy & Trade to develop a report on international trade agreements and ground water regulations specific to Maine.

September 11, 2009: At this meeting, the CTPC and WRPC heard several presentations.

- Background on Maine's ground water resources Carol White, C.A. White Associates.
- Overview of Maine's regulation of ground water withdrawals, Robert Marvinney, Maine Geological Survey.
- Background on international trade agreements given by Sarah Bigney, Maine Fair Trade Campaign.
- Legal review of Maine's ground water regulation and ground water ownership, Paul Gauvreau and Peggy Bensinger, Office of the Attorney General.
- Preliminary report on water policy and international trade agreements, William Waren, Forum on Democracy & Trade.

October 30, 2009: Mr. Waren presented an overview of his revised report (discussed below).

November 20, 2009: The CTPC and the WRPC discussed preliminary actions to recommend to the Joint Standing Committee on Natural Resources in January.

December 11, 2009: The CTPC and WRPC discussed and approved revised recommendations.

*Public hearing.* The CTPC and WRPC held a public hearing on October 15, 2009 at the State House for the purpose of receiving public input to the discussion on the potential impacts of international trade agreements on the State's ability to regulate ground water withdrawals. The CTPC and WRPC announced the date and time of the hearing well in advance via press release and information on the CTPC website. Various interest groups also posted the announcement for this hearing on their websites. About thirty people attended the hearing and twenty-one people spoke. Several groups were represented at the hearing, including Protect our Water and Wildlife Resources, Defending Water for Life, and Save Our Water. Economic and commercial interests were also represented at the hearing. Unaffiliated individuals also spoke. The full summary of the hearing is in Appendix C. Some key points expressed at the hearing:

- Carve water out of international trade agreements: Many members of the groups and some individuals expressed concerns that water should not be treated as a commodity and should be carved out of international trade agreements. Some expressed the concern that the "global water crisis" would put increasing pressure on Maine's water resources through these agreements.

- Tribunals: Disputes under international trade agreements are resolved through tribunals. Some hearing participants expressed concerns that such tribunals are not democratic, and are not open, transparent processes. Decisions from tribunals have the potential to undermine state and local regulations and democratic processes.
- Public trust/Absolute dominion rule: Some hearing participants expressed their view that placing ground water in the public trust and/or abolishing Maine’s absolute dominion doctrine with regard to ground water would enable the State to better protect these resources from challenges under international trade agreements.
- Economic support: Several hearing participants expressed the views that Maine needed more foreign investment, that “water in its natural state” is not a good, that the United States has never lost a NAFTA challenge, and that reasonable regulations that are fairly applied form the best defense against challenges under international trade agreements.

*Reports considered in the review.* As part of our process, the CTPC and WRPC reviewed and discussed several important legal articles that presented a broad variety of opinions regarding the potential impact of international trade agreements on a state’s ability of regulate ground water withdrawals.

1. Waren report. Mr. William Waren (Adjunct Prof., Harrison Institute for Public Law, Georgetown University and Policy Director, Forum on Democracy & Trade) participated in several CTPC/WRPC meetings and agreed to develop an overview paper focused on our question of the potential impact of international trade agreements on ground water regulations (Appendix D). His report also provides many policy options, some of which have been adopted in the section on recommendations. Some key points from his report:
  - a. “Water in its natural state” is not a commodity under international trade agreements. Bulk water may be considered a commodity, and bottled water certainly is a commodity under trade agreements.
  - b. Although water is currently held out from many international trade agreements, through negotiations on future agreements and tribunal decisions, water and water services could be included.
  - c. Disputes under international trade agreements are decided by tribunals, not U.S. courts. Tribunals work independently, drawing no precedent from past tribunal decisions. Although recent tribunal decisions have been favorable to U.S. interests, past decisions do not necessarily provide guidance to future tribunals.
  - d. A strong policy position for defense against challenges under international trade agreements is to ensure that regulations are reasonable, have a sound basis, are applied equitably, and a developed through due public process.
2. Slater article.<sup>8</sup> Published in the Wayne Law Review (2007), this article by Scott Slater (private attorney specializing in water) is narrowly focused on the nature of property interests in water and the limits of trade laws in the context of water resource management.
  - a. Water rights are an interest in real property to which trade laws do not apply.

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<sup>8</sup>Slater, S. S. 2007, State water resource administration in the free trade agreement era: as strong as ever: Wayne Law Review, v. 53, p. 649-714. <http://orgs.law.wayne.edu/lawreview/doc/recent%20issues/53.2.pdf>  
<http://www.bhfs.com/NewsEvents/Publications?find=23155>

- b. Ground water regulations will prevail against investor protections as long as regulations are non-discriminatory, are not applied arbitrarily, and established through due process in the public interest. Regulations that arbitrarily discriminate against certain products made from water would weaken this defense.
3. Hall article.<sup>9</sup> Published in the University of Denver Water Law Review (2010), this article by Noah Hall (Prof., Wayne State University Law School) uses the example of bottled water to examine the protection of freshwater resources in the arena of global water markets. Prof. Hall represented several environmental organizations in the *Michigan Citizens for Water Conservation v. Nestle Waters North America, Inc.* case.
- a. “Water in its natural state” is not a good, but at some point in its extraction, use, and incorporation into a product, water becomes a good subject to trade agreements. States can protect water in its natural state without running afoul of NAFTA and, likely, GATT.
  - b. States may regulate and restrict bottled water to the extent necessary to conserve their water resources. Thinly disguised protectionism and outright discrimination against the use of water for bottled water would run afoul of NAFTA and GATT.
  - c. States have ample authority to protect ground water and ground water-dependent natural resources without the ground water itself being subject to the public trust doctrine. State constitutions, statutes, and the police power allow states to regulate water use, include ground water withdrawal, without expanding the public trust to ground water.

### **Conclusions and recommendations**

The following recommendations and conclusions received the unanimous consent of the members of the Citizen Trade Policy Commission and the members of the Water Resources Planning Committee.

The Maine Legislature should continue to make decisions regarding ground water and other natural resources using a transparent process with opportunity for public input, and state agencies should continue to apply the law in a manner consistent with due process. International trade agreements, which are currently negotiated without sufficient consultation with states, contain provisions that could expose Maine laws to challenges in international tribunals whose decisions take precedent over state and federal law. There is potential for these treaties to undermine our state’s capacity to put laws into place that protect the health and well being of our citizens. The Legislature and the CTPC should take action to monitor these trade negotiations and agreements. They should further take action to seek to change this undemocratic system in which agreements are negotiated without transparency and without meaningful consultation with the states.

- 2) In future policy deliberations, the Legislature should consider that the best defense against challenges under international trade agreements is to continue its existing process of adopting

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<sup>9</sup> Hall, N. D., 2010, Protecting freshwater resources in the era of global water markets: Lessons learned from bottled water: Denver Water Law Review. Professor Hall represented several environmental and conservation organizations as *amici* in the *Michigan Citizens for Water Conservation v. Nestlé Waters North America Inc.*

regulations that are clear, reasonable, have a sound basis, are applied equitably, and that are established through due process.

Articles and legal briefings by attorneys from diverse backgrounds all confirm this view. Maine's current regulatory framework for ground water withdrawals evolved over years of public debate, and focus on impacts of withdrawals on other water-dependent resources and activities, rather than discriminating against particular uses of ground water, and thus position the State well against challenges under international trade agreements.

- 2) The Legislature should encourage the development of a better system for consultation between the State and the U.S. Trade Representative as future trade agreements are negotiated.

Currently, states have little input as trade agreements are negotiated. The negotiating process lacks transparency and precludes states from any meaningful participation in the negotiations even though the agreements have significant potential impact on state regulatory authority. The Legislature should encourage our Congressional Delegation to establish a more inclusive and transparent process for USTR consultation with states on trade matters that have the potential for impacting states.

- 3) The Legislature should encourage Maine's Congressional Delegation to insist on the codification of these two specific tribunal decisions regarding certain disputes under international trade agreements:

- c. *Methanex* decision. The NAFTA tribunal in *Methanex v. United States* soundly rejected Vancouver-based Methanex Corporation's claim for nearly a billion dollars in compensatory damages for California's phase-out of the gasoline additive MTBE because it was polluting lakes and ground water and was endangering the public health.
  - i. Specifically, narrow indirect expropriation so that it does not apply to nondiscriminatory regulations as explained in the *Methanex* award. In other words, establish that the adoption or application by any national or sub-national government of any bona fide and non-discriminatory measure intended to serve a public purpose shall not constitute a violation of an expropriation article of an investment agreement or treaty.
- d. *Glamis* decision. The tribunal ruled for the U.S. when a Canadian corporation sued under NAFTA for actions taken by the Department of Interior and the State of California, imposing environmental and landuse regulations on Glamis's proposed open-pit gold mine.
  - i. Specifically, narrow the minimum standard treatment to the elements of customary international law as explained in the U.S. brief in *Glamis*, in which the State Department argued for a reading of MST confined to three elements: (1) compensation for expropriation, (2) "internal security," and (3) "denial of justice" where domestic courts or agencies (not legislatures) treat foreign investors in a way that is "notoriously unjust" or "egregious" such as a denial of procedural due process. Further, the expectation of a stable or unchanging legal environment is not to be understood as part of customary international law.

- 4) The Legislature may wish to consider requiring that future contracts between governmental units in Maine and private investors include a waiver of any right by investors to seek compensation through international investment arbitration.

The lack of clarity, certainty, and predictability in international trade and investment law allows international arbitration tribunals broad discretion. While some tribunals have used their discretion wisely and prudently, the precedents of past decisions do not bind future tribunals.

Requiring such a waiver in governmental contracts would move dispute resolution from international arbitration tribunals to U.S. courts, where precedential actions are an important foundation of the judicial process. Some consideration should be given, however, to whether such action would put Maine at a competitive disadvantage for international investment and whether such a waiver could be used to show discrimination against a certain class of private investors.

- 6) Because of the potential impact of international trade agreements on state sovereignty and state regulatory authority, the Legislature should provide adequate support for the CTPC so that it can do the work with which it is charged by statute. While the Commission has received national recognition for its work since its inception and has served as a model for other states wishing to establish similar citizen commissions, recent funding cuts have left the CTPC without any staff assistance and it currently lacks the capacity to adequately monitor, assess and respond to the complex and complicated issues involving international trade agreements and their consequences to the people of Maine. The Legislature should therefore consider establishing a position that would:
  - b. Support the Maine Citizen Trade Policy Commission in monitoring negotiations on international trade agreements and case law from tribunal settlements and support it in providing input to the Legislature, Governor, Maine Congressional Delegation and the U.S. Trade Representative on international trade issues and their impact on the people and economy of Maine.
  - d. Assist the CTPC with reviewing the potential impacts of international trade agreements on state regulatory authority and support the CTPC in advising the Legislature and legislative policy oversight committees when considering such impacts in policy decisions.
  - e. Assist in communicating concerns and needed actions to the Legislature, Governor, Congressional Delegation, U.S. Trade Representative, and others.
- 7) a. We recommend that the Legislature encourage the U.S. Trade Representative and Maine's Congressional Delegation to continue to carve water out of future international trade agreements and existing agreements that may be renegotiated.
  - b. The research undertaken for this report did not identify any decisions that shed light on the specific issue of whether a legislative change to a public trust rule governing ground water would improve the chances of a Maine regulatory statute withstanding a challenge based on a trade treaty.

Some members of the public supported taking steps to protect Maine's ground water due to its importance and the potential impacts of world shortages and global warming. These

measures included continuing to carve water out of international trade agreements, and changing the standard governing the use of Maine's ground water to a public trust.

Many of the speakers at the public hearing expressed concern about the impact of treaty provisions on Maine's system of regulating the use of ground water. Several speakers emphasized that water is different from the vast majority of products that are subject to trade agreements, and even other natural resources in that it is necessary to life. The importance of water is reflected in existing state and federal regulation, designed to ensure both its safety and continued availability.

For these reasons, water should continue to be carved out of international trade agreements. As treaties are negotiated, the parties decide which products and services should be covered, and bargaining determines those that are included. The unique nature of water makes it ill-suited for this type of decision making, i.e., extending treaty coverage to water in return for coverage of some sought after product(s) of the bargaining partner. Water is not a good or a product in the common usage of those terms. While there are serious shortages of water in parts of the world, and even in parts of the United States, resolution of this issue should not be determined by private investors exercising rights that they believe are conferred on them by trade treaties.

The concept that Maine should change the doctrine governing ground water to one of public trust is a more complex issue. The substantial research that has been conducted for this report did not identify any decisions made under the provisions of any trade treaty that address the concept that moving to a public trust rule would improve the likelihood of withstanding a trade treaty challenge.

However, there are potential legal consequences under state and federal law if the Legislature were to adopt a public trust rule. Litigation in state or federal court challenging the impact of the specific changes upon ownership interests would be likely. The legal issues involved in resolving such a challenge are complex, and the outcome cannot be predicted with certainty, but if such a challenge were successful, it seems likely that the potential damages that could be awarded would be high.<sup>10</sup>

As the Maine Law Court noted in declining to judicially abrogate the absolute dominion rule, there are "heavy policy considerations" involved in making such a change that render it more suitable for legislative study and decision. *Maddocks v. Giles*, 1999 ME 63, 728 A.2d 150, ¶ 12. Such a study and recommendations concerning the policy and regulatory implications of changing the absolute dominion rule are beyond the scope of the charge to this group, and are clearly material to any decision that a different rule would lead to a better water policy for the State. As emphasized in our first recommendation, the best protection against treaty challenges is the establishment of sound regulatory measures, grounded in science and facts, developed through a legislative and rulemaking process that encourages public input, and

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<sup>10</sup> Such a change could also generate treaty challenges by affected investors. Those who were able to do so might take advantage of treaty provisions such as those authorizing compensation for expropriation (which is somewhat analogous to confiscation) or violations of minimum standard treatment provisions. A successful treaty based claim could result in damages against the federal government and an obligation to take steps necessary to eliminate the Maine law provision that resulted in the award. This is not to conclude that such a challenge would be successful, but rather to point out the consequences in such event.

that are applied to all, consistent with due process. Maine has a thorough regulatory system for water resources that meets this standard.