Water Grab #1 City of Toronto's Plans for a Water Board Pose Significant Trade Risks

Executive Summary: November 19, 2002

This first in a series of three Case Studies by the Canadian Institute for Environmental Law and Policy (CIELAP) examines the current NAFTA and the expected GATS obligations should the City of Toronto Council vote to change the governance structure of the present Department of Water and Wastewater Services into the Toronto Water Board, a Municipal Service. The focus is on trade obligations concerning public monopolies, free trade in services and investor state disputes. The second Case Study builds upon the first but the focus is on the constitutional aspects, including the public trust doctrine, of two Bills pending before the Ontario legislature concerning the Safe Drinking Water Act (Bill 195) and the Sustainable Water and Sewer Act (Bill 175). The third paper in the series examines the water resource and quality standards required in any event.

Having reviewed the October 21st Chief Administrator's Office Staff Report on "The Establishment of the Toronto Water Board", the Staff Report recommends: that control of the Department of Water and Wastewater Services be given to an appointed Municipal Services Board; that City Council maintain the right to set the water rate and the budget for the new Board; and that the City continues to be the employer of the water and wastewater workforce. Despite the Staff Report's acknowledgement of uncertainty about the trade implications of the various governance structures proposed, it recommends removing these services from an in-house Department to a third party Municipal Service Board, pursuant authorizing provincial legislation, the Municipal Act (2001).

Based upon earlier CIELAP submissions, the Staff did obtain a legal opinion from the City Solicitor on the trade implications should Council approve this significant governance change to the City's water system. While this opinion was helpful in identifying the issues, unfortunately it is based upon an underlying assumption that water services would continue to be provided completely within the public sector. Given that the latest proposal would permit the Board to purchase new and additional services, including water extraction, from outside of the public sector, a significant governance change is contemplated. We recommend that the City of Toronto's decision to restructure be delayed until after the City Solicitor reexamines the trade implications, based upon the description of the proposed powers of the TBW in the October 21st proposal and the public accountability gap and trade concerns are adequately addressed, with new public consultations, and due regard to the public and national interests at stake.

Having conducted our review of the new TWB proposal with current trade obligations, our main findings are as follows:

1. It would be prudent to conduct a new trade review, subject to peer review and public consultations, based upon the October 21st Staff Report that contemplates the Toronto Water board entering into 20 year contracts and leases with the private sector for the provision of water and wastewater services, including the extraction of water from Lake Ontario, prior to the Council taking a decision on governance that would be difficult and costly to reverse.

2. While the TWB might still be considered to be within the public sector, according to NAFTA Chapter 15 (Competition Policy, Monopolies and State Enterprises), trade obligations are triggered as soon as a government "designates" a new public monopoly service. Presumably this governance change also includes the "redesignation" of a service from a Department W &WW to a municipal service board or the establishment of a new public service board, such as the proposed TWB.

3. A new public monopoly under NAFTA Chapter 15 must operate based alone on commercial considerations in the supply of services, and provide non-discriminatory treatment to all NAFTA service providers and investors, while the current, directly accountable to Council Water Department is able to require the best level of service at an affordable price, the best laboratories to detect new pathogens, and the best training for its workers. A redesignation locks in a business-orientated, strictly commercial approach that does not necessarily address wider public interests.

4. NAFTA's Chapter 11 ("Investment, Services and Related Matters") specifically links obligations under Chapter 15 and Chapter 12 (Services) with a powerful investor-led dispute settlement mechanism. These rights and claims are only available to foreign-service providers and investors and not domestic corporations. NAFTA investor disputes do not take place in an open court but rather behind closed doors away from public and media oversight.

5. NAFTA agreements would allow direct foreign investor disputes about how any new public monopoly operates, as well as about what level of environmental and public health standards are acceptable or requiring financial compensation.

6. Under NAFTA Chapter 11, investors can sue governments if a future environmental regulation on water quality standards, set by City Council for example, reduces the profit the investor anticipated. The current Methanex dispute by a Canadian corporation against the State of California for banning the gas additive MTBE because it contaminates water supplies is a case in point. The expropriation claim is for billions of dollars.

7. Current Canadian reservations from free trade in service and investment obligations risk being lost once a particular public service, such as water services, is

supplied in whole or in part by a private firm, even if it was provided on a not-for-profit, i.e., non-commercial, basis.

8. It is unlikely that government and corporate partnerships or concession agreements can contract out of NAFTA or the domestic legislation that implements these trade obligations. These contracts are governed not only by the rules of domestic contract law but also by international investment and services treaties.

9. The general exception to trade obligations for government standards and measures related to the conservation of exhaustible natural resources found in the 1947 GATT has been removed from the NAFTA and GATS agreements. Therefore, government regulation of services to conserve water supplies would not likely be protected and would in any event be subject to state-to-state disputes from over 144 member states of the GATS.

10. The conclusion that a strictly commercial approach to water supply and services is inappropriate for such an essential and non-renewable resource is reinforced when one considers that current GATS negotiations would remove a recognized government exemption from trade disciplines, to regulate for the conservation of exhaustible natural resources

11. Given the GATS limited exception for services provided under "government authority", and without the benefit of a "conservation of exhaustible natural resources" exception, a host of government measures - including robust drinking water quality testing, stream habitat protection and water export controls - would have no safeguard whatsoever from trade and investment disputes at a trade forum. This would create a creating a "chilling effect" on otherwise responsive elected officials to the public interest.

12. Absent provision otherwise, the necessity for government measures, the adequacy of afforded due notice and process and the rationale for deviations from lower international standards or for determinations of non-equivalency all become disputable under the GATS. Even non-discriminatory domestic regulations could be challenged and prohibited unless they are no more "burdensome than necessary".

13. Despite the purported trade and investor-rights constraints, the International Joint Commission (IJC) recognizes that the waters of the Great Lakes are, for the most part, a non-renewable resource. The waters and water quality of the Great Lakes are already suffering from climate change impacts.

14. Water is the subject of human rights and a public trust. The 1867 Constitution Act recognizes that the provinces hold non-renewable resources subject to any Trusts, putting into doubt the constitutional authority of a province or local government to transfer the effective ownership and control of local water works and systems and thus in fact actual public access to and use of the water resource to the private sector. Clear legislative intent would likely be required to exhaust such a public trust.

15. As responsibility moves from a directly elected governance system to a third party water utility board, commission or corporation, without provision otherwise, the opportunity to ensure timely public access to information and public accountability diminishes accordingly. It would also be contrary to the public interest to diminish rather than to enhance public accountability in any governance change.

In short, the likely and significant trade and investment consequences that are triggered by a hasty and ill - considered governance change to the City's W&WW Department are contrary to the public interest and the environmental protection mandate of governments. Given the tragedy in Walkerton, the Hamilton experience with private operators, and the fact that NAFTA and at least 144 foreign service providers and investors could compete for Toronto W&WW service operations at the lowest possible level of environmental and public health protection, it is incumbent upon City Staff and Council to undertake a through analysis of the trade and investment implications of restructuring Toronto's water service system based upon the latest October 21st Staff Report, ***before Council takes a decision to restructure.***

Indeed, it was the threat that NAFTA could limit the region's ability to set water standards that caused the Greater Vancouver District Water Board to reject a June 2001 plan to allow a public-private partnership to design, build and operate a $117 million filtration plant. Moreover, given the anticipated governance changes at the provincial level to local water systems, the public interest is best served by more not less local control over exhaustible water supplies and services.

Based upon the risks that the Walkerton tragedy made clear and almost ten years of experience with NAFTA investor-state disputes, our preliminary findings indicate serious public interests' about the most precious of all exhaustible natural resources - water -are at stake both at the City and provincial levels, requiring more public accountability, not less.

For a copy of the full report, please visit www.cielap.org/whatsnew and for further information, contact Christine Elwell, Senior Legal and Policy Analyst at christine@cielap.org

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