



APEC-UNCTAD REGIONAL TRAINING COURSE ON THE CORE ELEMENTS OF INTERNATIONAL INVESTMENT AGREEMENTS IN THE APEC REGION

Presentations

Kuala Lumpur, Malaysia
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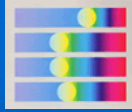
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APEC-UNCTAD Regional Training
Course on the Core Elements of
International Investment Agreements in
the APEC Region



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SCOPE AND DEFINITIONS

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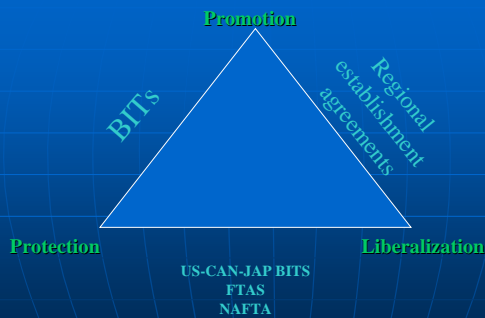
DEFINITIONS

Definitions are key:

- What/who are we talking about?
- Who benefits from investment liberalization policies?
- Who is protected?
- Who is entitled to claim?

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The international framework for investment
BITs/IAs have several possible objectives:



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DEFINITIONS

- Definition of 'investment'
- Definition of 'investor'
- Link investment of an investor: ownership and control
- The laws and regulations of the host country
- Definition of 'territory'
- Other definitions

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DEFINITION OF INVESTMENT

Depending on the purpose of the treaty:

- Open-ended asset-based definition
- Enterprise-based
- Additional criteria
- Closed list and/or exceptions

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Definition of Investment

Open-ended asset-based definition : broad protection

Illustrative list including usually:

- Movable and immovable property rights
- Various types of interest in companies
- Claims to money and claims under a contract having a financial value
- Intellectual Property Rights
- Business concessions and other contractual rights

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Definition of Investment

Example of asset-based definition: art. 1.3 Agreement among the Government of Brunei, Indonesia, Malaysia, Philippines, Singapore and Thailand for the Promotion and Protection of Investments (1987)

For the purpose of this Agreement:

...

3. The term "investment" shall mean every kind of asset and in particular shall include, though not exclusively:

- a) movable and immovable property and any other property rights such as mortgages, liens and pledges;
- b) shares, stocks and debentures of companies or interests in the property of such companies;
- c) claims to money or to any performance under contract having a financial value;
- d) intellectual property rights and goodwill;
- e) business concessions conferred by law or under contract including concessions to search for, cultivate, extract, or exploit natural resources.

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Definition of Investment

Example of asset-based definition: art. 4 ASEAN Comprehensive Investment Agreement

For the purpose of this Agreement:

...

(c) "investment" means every kind of asset, owned or controlled, by an investor, including but not limited to the following:

- (i) movable and immovable property and other property rights such as mortgages, liens or pledges;
- (ii) shares, stocks, bonds and debentures and any other forms of participation in a juridical person and rights or interest derived therefrom;
- (iii) intellectual property rights which are conferred pursuant to the laws and regulations of each Member State;
- (iv) claims to money or to any contractual performance related to a business and having financial value;
- (v) rights under contracts, including turnkey, construction, management, production or revenue-sharing contracts; and
- (vi) business concessions required to conduct economic activities and having financial value conferred by law or under a contract, including any concessions to search, cultivate, extract or exploit natural resources.

The term "investment" also includes amounts yielded by investments, in particular, profits, interest, capital gains, dividend, royalties and fees. Any alteration of the form in which assets are invested or reinvested shall not affect their classification as investment:

Definition of Investment

Enterprise-based definition:

targeted investment liberalization + protection

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JAPAN-INDONESIA EPA ART: X02

For the purposes of this Chapter:

- (a) the term "investments" means every kind of asset owned or controlled, directly or indirectly, by an investor, including:
 - (i) an enterprise;
 - (ii) shares, stocks or other forms of equity participation in an enterprise, including rights derived therefrom;
 - (iii) bonds, debentures, loans and other forms of debt, including rights derived therefrom;
 - (iv) rights under contracts, including turnkey, construction, management, production or revenue-sharing contracts;
 - (v) claims to money and claims to any performance under contract having a financial value;
 - (vi) intellectual property rights, including copyrights, patent rights and rights relating to utility models, trademarks, industrial designs, layout-designs of integrated circuits, new variety of plants, trade names, indications of source or geographical indications and undisclosed information;
 - (vii) rights conferred pursuant to laws and regulations or contracts such as concessions, licenses, authorizations, and permits; and
 - (viii) any other tangible and intangible, movable and immovable property, and any related property rights, such as leases, mortgages, liens and pledges;

Note: Investments also include amounts yielded by investments, in particular, profit, interest, capital gains, dividends, royalties and fees.

A change in the form in which assets are invested does not affect their character as investments.

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DR-CAFTA : CRITERIA

"investment means every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk. Forms that an investment may take include:

- (a) an enterprise;
- (b) shares, stock, and other forms of equity participation in an enterprise;
- (c) bonds, debentures, other debt instruments, and loans;
- (d) futures, options, and other derivatives;
- (e) turnkey, construction, management, production, concession, revenue-sharing, and other similar contracts;
- (f) intellectual property rights;
- (g) licenses, authorizations, permits, and similar rights conferred pursuant to domestic law; and
- (h) other tangible or intangible, movable or immovable property, and related property rights, such as leases, mortgages, liens, and pledges.

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DEFINITION OF INVESTMENT

Key issues:

- > **Claims to money:** will all claims to money be covered? Even those claims to money not related to FDI? What about payments derived from commercial transactions or from the sale of goods and services?
- > **Debt instruments:** will all debt instruments be covered? What about those debt instruments with short-term maturity? Should there be a minimum maturity term specified?
- > **Intellectual property rights (IPRs):** should a reference to a legal framework be included? Would only those IPRs provided in accordance to domestic legislation be considered an investment? Those IPRs existing pursuant international agreements?
- > **State Contracts:** need for special treatment in definitions or substantive parts of the agreement.
- > **Exclusions:** Public debt? Property acquired not for an economic activity (i.e. real estate)?
- > **Criteria:** what about the Salini test? Contribution to development; Malaysian Historical Salvors

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DEFINITION OF INVESTMENT

New trend: the Closed-list: Canada-Peru

Investment means:

- (I) an enterprise;
- (II) an equity security of an enterprise;
- (III) a debt security of an enterprise

...

but does not include a debt security, regardless of original maturity, of a state enterprise;

(IV) a loan to an enterprise

...

but does not include a loan, regardless of original maturity, to a state enterprise;

...

but investment does not mean,

(X) claims to money that arise solely from (i) commercial contracts for the sale of goods or services by a national or enterprise in the territory of a Party to an enterprise in the territory of the other Party, or (ii) the extension of credit in connection with a commercial transaction, such as trade financing, other than a loan covered by subparagraphs (IV) or

...

(XI) any other claims to money, that do not involve the kinds of interests set out in subparagraphs (I) through (IX);

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DEFINITION OF INVESTMENT

Exclusions: Republic of Korea-Singapore FTA, Chapter 10, art. 10-1 (footnote) (2005).

Investment does not mean,

(a) claims to money that arise solely from:

- (i) commercial contracts for the sale of goods or services by a national or enterprise in the territory of a Party to an enterprise in the territory of the other Party,
- (ii) the extension of credit in connection with a commercial transaction, such as trade financing, and

(b) an order entered in a judicial or administrative action and do not involve the kinds of interests set out in subparagraphs (a) to (h).

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Recent Cases

- Issue: Scope of ICSID Convention art. 25
Investment is a necessary condition but not defined

- Double keyhole

- Wording
 - Criteria
- } Should not be contradictory

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Definition of Investor

- Natural persons
- Juridical persons
- The link with investments:
 - Owned and controlled
 - Directly or indirectly

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DEFINITION OF INVESTOR

Natural Persons

- Criteria: Nationals/citizens of the Parties
- Protection for double nationals? dominant and effective nationality criteria
- Permanent residents: Canadian approach
- Nationality criterion more often used than residence criterion. Sometimes combination: NZ/Singapore CEP Agreement.

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Natural Persons - Example

Art. 4. ASEAN Comprehensive Investment Agreement

For the purpose of this Agreement:

...

(d) "investor" means a natural person of a Member State or a juridical person of a Member State that is making, or has made an investment in the territory of any other Member State;

...

(g) "natural person" means any natural person possessing the nationality or citizenship of, or right of permanent residence in the Member State in accordance with its laws, regulations and national policies;

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Juridical Persons

Criteria to determine the nationality of the legal entity/investor:

- country of organization or incorporation
- Country of the seat
- Combination of criteria

The link with investment: ownership and control

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Juridical Persons – Example 1

Traditional approach: definition of the investor
Article 1: Definition (China-Germany BIT of 2003)

The term "investor" means:

- (a) in respect of the Federal Republic of Germany: any juridical person as well as any commercial or other company or association with or without legal personality having its seat in the territory of the Federal Republic of Germany, irrespective of whether or not its activities are directed at profit; (...).
- (b) in respect of the People's Republic of China: economic entities, including companies, corporations, associations, partnerships and other organizations, incorporated and constituted under the laws and regulations of and with their seats in the People's Republic of China, irrespective of whether or not for profit and whether their liabilities are limited or not.

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Juridical Persons

Japan-Indonesia EPA Art.X02

- b) the term "investor of a Party" means a national or an enterprise of a Party, that seeks to make, is making, or has made, investments except branch of an enterprise of a non-Party which is located in [the territory of] the Party;
- (c) the term "national of a Party" means a natural person having the nationality of a Party in accordance with its applicable laws and regulations;
- (d) the term "enterprise of a Party" means any legal person or any other entity duly constituted or organized under the law of a Party, whether for profit or otherwise, and whether privately owned or controlled or governmentally-owned or controlled, including any corporation, trust, partnership, joint venture, sole proprietorship, association, organization, company or branch;
- (e) an enterprise is:
 - (i) "owned" by an investor if more than 50 percent of the equity interests in it is beneficially owned by the investor; and
 - (ii) "controlled" by an investor if the investor has the power to name a majority of its directors or otherwise to legally direct its actions;

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Juridical Persons

Approaches in recent FTAs:

- Definition of investment
- Definition of investor
- Definition of an investment of an investor of a Party: investment owned or controlled directly or indirectly by an investor of such Party
- Definition of ownership and control :

Ex: Australia-India BIT: art 1-h (i) and (ii)

For the purposes of this Agreement, a company is regarded as being controlled by a company or by a natural person, if that company or natural person has the ability to exercise decisive influence over the management and operation of the first-mentioned company, specifically demonstrated by way of:

- (i) ownership of 51% of the shares or voting rights of the first mentioned company, or
- (ii) the ability to exercise decisive control over the selection of the majority of members of the board of directors of the first mentioned company

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Juridical Persons

EX: GATS art. 28 (n)

...

(n) a juridical person is:

- (i) "owned" by persons of a Member if more than 50 per cent of the equity interest in it is beneficially owned by persons of that Member;
- (ii) "controlled" by persons of a Member if such persons have the power to name a majority of its directors or otherwise to legally direct its actions;
- (iii) "affiliated" with another person when it controls, or is controlled by, that other person; or when it and the other person are both controlled by the same person;

...

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- **Direct and indirect control: implications on dispute settlement**
- **Implications on shell companies, third-Party investors,...**
- **On possible technical solution: Denial of benefits clause**

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Juridical Persons

USA BIT Model, 2004

Article 17: Denial of Benefits

1. A Party may deny the benefits of this Treaty to an investor of the other Party that is an enterprise of such other Party and to investments of that investor if investors of a non-Party own or control the enterprise and the denying Party:
 - (a) does not maintain diplomatic relations with the non-Party; or
 - (b) adopts or maintains measures with respect to the non-Party or an investor of the non-Party that prohibit transactions with the enterprise or that would be violated or circumvented if the benefits of this Treaty were accorded to the enterprise or to its investments.
2. A Party may deny the benefits of this Treaty to an investor of the other Party that is an enterprise of such other Party and to investments of that investor if the enterprise has no substantial business activities in the territory of the other Party and investors of a non-Party, or of the denying Party, own or control the enterprise.

Investor

- Key issues in recent FTAs:
- Pre-establishment disciplines
- Definition of the potential investor: treaty coverage for an investor that has made or is in the process of making or is seeking to (or attempts to) make an investment.

Scope of the Agreement

Territorial coverage of the treaty

- Maritime areas
- Airspace
- Reference to international law

Temporal coverage

- Protection of investments made prior to the entry into force
- Protection after termination
- Disputes arising from investments

Explicit limitations or exclusions

- ASEAN Comprehensive Investment Agreement art. 3, 2+3 and art. 4

Scope of the agreement

- Application to different levels of government
- Relevant when one of the negotiating Parties has a federal system.
- The agreement will apply to all levels of government, irrespective of the domestic legal limitations that the federal government may have.
- Federal government will ensure compliance with international obligations.
- The best-in-State treatment.

SCOPE AND COVERAGE

Application *ratione materiae*

- A priori exclusion from the coverage of the agreement of certain economic activities or regulatory areas (such as air transport services, financial services, government procurement, subsidies, etc)
- Application to taxation matters
- Exclusions: portfolio investment not covered (Framework Agreement on the ASEAN Investment Area), limitation to certain sectors (Energy Charter Treaty)
- Critical issue: services/investment.

Investment and Services

Three approaches for investment in services:

- Investment-based approach: investment is exclusively covered by the disciplines of the investment chapter (NAFTA) or by an investment agreement. This approach does not make a difference between services investments and non-services investments. Usual BITs self-contained approach. Also ASEAN Comprehensive Investment Agreement, art. 3.5

Investment and Services

- **Services-based approach: services FDI is exclusively covered by the disciplines of the services chapter of an agreement or an agreement on trade in services: GATs, Asean Framework Agreement on Services**
- **Mixed approach: in most FTAs-RTAs: services investment is covered in both investment and services chapters. Liberalization provisions/protection provisions.
E.g. Thailand-Australia (structure of chapters)**