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INTERNATIONAL INVESTMENT ARRANGEMENTS:
Trends and Emerging Issues

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NOTE

As the focal point in the United Nations system for investment and technology, and building on 30 years of experience in these areas, UNCTAD, through DITE, promotes understanding of key issues, particularly matters related to foreign direct investment and transfer of technology. DITE also assists developing countries in attracting and benefiting from FDI and in building their productive capacities and international competitiveness. The emphasis is on an integrated policy approach to investment, technological capacity building and enterprise development.

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The following symbols have been used in the tables:

Two dots (..) indicate that data are not available or are not separately reported.

Rows in tables have been omitted in those cases where no data are available for any of the elements in the row;

A dash (-) indicates that the item is equal to zero or its value is negligible;

A blank in a table indicates that the item is not applicable;

A slash (/) between dates representing years, e.g. 1994/1995, indicates a financial year;

Use of a hyphen (-) between dates representing years, e.g. 1994-1995, signifies the full period involved, including the beginning and end years.

Reference to "dollars" ($) means United States dollars, unless otherwise indicated.

Annual rates of growth or change, unless otherwise stated, refer to annual compound rates.

Details and percentages in tables do not necessarily add to totals because of rounding.

The material contained in this study may be freely quoted with appropriate acknowledgement.

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PREFACE

The secretariat of the United Nations Conference on Trade and Development (UNCTAD) is implementing a programme on international investment arrangements. It seeks to help developing countries to participate as effectively as possible in international investment rule-making. The programme embraces policy research and development, including the preparation of a series of issues papers; human resources capacity-building and institution-building, including national seminars, regional symposia, and training courses; and support to intergovernmental consensus-building.

This paper is part of a new *Series on International Investment Policies for Development*. It builds on, and expands, UNCTAD's *Series on Issues in International Investment Agreements*. Like the previous one, this new series is addressed to Government officials, corporate executives, representatives of non-governmental organizations, officials of international agencies and researchers.

The *Series* seeks to provide a balanced analysis of issues that may arise in the context of international approaches to investment rule-making and their impact on development. Its purpose is to contribute to a better understanding of difficult technical issues and their interaction, and of innovative ideas that could contribute to an increase in the development dimension of international investment agreements.

The Series is produced by a team led by James Zhan. The team members include Victoria Aranda, Amare Bekele, Hamed El-Kady, Anna Joubin-Bret, Joachim Karl, Martin Molinuevo, Anca Radu, Marie-Estelle Rey, Elizabeth Tuerk and Jörg Weber. Khalil Hamdani provided overall guidance. Members of the Review Committee are Mark Kantor, Mark Koulen, Peter Muchlinski, Antonio Parra, Patrick Robinson, Pierre Sauvé, M. Sornarajah and Kenneth Vandevelde.

The present paper was prepared by Roberto Echandi and Kenneth Vandevelde, based on inputs from the Secretariat. The study served as UNCTAD background document for the APEC Investment Facilitation Initiative: A Cooperative Effort with UNCTAD and other Multilateral Institutions, held in Tokyo from 1-2 September 2005. It has been subsequently revised in light of that meeting's discussions and comments received from the participants of that meeting. These comments are gratefully acknowledged.

The contribution of the Government of Japan for this study is gratefully acknowledged.

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UNCTAD's work programme on international investment agreements is implemented by a team of UNCTAD staff members and consultants headed by James Zhan. The team includes Bekele Amare, Hamed El-Kady, Anna Joubin-Bret, Federico Ortino, Anca Radu, Marie-Estelle Rey, Elisabeth Tuerk and Jörg Weber. Administrative support is provided by Séverine Excoffier-El Boutout and Josephine Lamptey. Desktop publishing was done by Teresita Sabico. Khalil Hamdani provides overall guidance.

UNCTAD has carried out a number of activities related to the work programme in cooperation with other intergovernmental organizations, including the Agence pour la Francophonie, Banco Centroamericano de Integración Económica, CARICOM Secretariat, German Foundation for Development, Inter-Arab Investment Guarantee Corporation, Inter-American Development Bank (BTD/INTAL), League of Arab States, Organization of American States, Secretaria de Integración Económica Centroamericana and the Secretaria General de la Comunidad Andina. UNCTAD has also cooperated with non-governmental organizations, including the Centre for Research on Multinational Corporations, the Consumer Unity and Trust Society (India), the Dutch Foundation for Research on Multinationals (SOMO) (the Netherlands), the Economic Research Forum (Egypt), the European Roundtable of Industrialists, the Friedrich Ebert Foundation (Germany), the German Foundation for International Development, the International Confederation of Free Trade Unions, the Labour Resource and Research Institute (LaRRI) (Namibia), Oxfam, the Third World Network and World Wildlife Fund International. Since 2002, a part of the work programme has been carried out jointly with the World Trade Organization (WTO).

Funds for the work programme have so far been received from Australia, Brazil, Canada, France, Japan, the Netherlands, Norway, Sweden, Switzerland, the United Kingdom and the European

Commission. Argentina, Botswana, China, Colombia, Costa Rica, Croatia, Cuba, Czech Republic, Djibouti, Egypt, Gabon, Germany, Guatemala, India, Indonesia, Jamaica, Malaysia, Mauritania, Mexico, Morocco, Namibia, Pakistan, Peru, Qatar, Singapore, South Africa, Sri Lanka, Thailand, Trinidad and Tobago, Tunisia, Venezuela and Yemen have also contributed to the work programme by hosting regional symposia, national seminars or training events.

In pursuing this programme of work, UNCTAD has also closely collaborated with a number of international, regional and national organizations, particularly with the Centro de Estudios Interdisciplinarios de Derecho Industrial y Económico (the Universidad de Buenos Aires), the Indian Institute of Foreign Trade, the Legon Centre of Accra (Ghana), ProInversión (Peru), Pontificia Universidad Católica del Perú, the National University of Singapore, Senghor University (Egypt), the University of Dar Es Salaam (Tanzania), the University de Los Andes (Colombia), the University of Campinas (Brazil), the University of Lima (Peru), the Universidad del Pacífico (Peru), the University of Pretoria (South Africa), the University of Tunis (Tunisia), the University of Yaoundé (Cameroon), the Shanghai WTO Affairs Consultation Center (China) and the University of the West Indies (Jamaica and Trinidad and Tobago). All of these contributions are gratefully acknowledged.

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LIST OF ABBREVIATIONS

AIA	ASEAN Investment Area
AEC	African Economic Community
ASEAN	Association of East Asian Nations
BIMSTEC	Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation
BIT	Bilateral treaty for the promotion and protection of investment (or bilateral investment treaty)
CARICOM	Caribbean Common Market
CCIA	COMESA Common Investment Area
COMESA	Common Market for Eastern and Southern Africa
DTT	Bilateral treaty for the avoidance of double taxation (or double taxation treaty)
ECOWAS	Economic Community of Western African States
ECA	Economic cooperation agreement
ECCAS	Economic Community of Central African States
ECGL	Economic Community of the Great Lakes Countries
PA	Economic partnership agreement
FDI	Foreign direct investment
FTA	Free trade area
GCC	Gulf Cooperation Council
IIA	International investment agreement
LDC	Least developed countries
PTIA	Preferential trade and investment agreement
RTA	Regional trade agreement
SAARC	South Asian Association for Regional Cooperation
SADC	Southern African Development Community
SDT	Special and differential treatment
TNC	Transnational corporation
TRIMs	Agreement on Trade-related Investment Measures
UDEAC	Central African Customs and Economic Union
WAEMU	West African Economic and Monetary Union

EXECUTIVE SUMMARY

The past few years saw a proliferation of international investment agreements (IIAs) at the bilateral, regional and inter-regional levels. Several developments are worth noting in this context. First, the universe of IIAs consisting of bilateral investment treaties (BITs) and other trade and investment agreements continued to expand. Second, a new generation of IIAs is emerging with provisions that tend to be increasingly sophisticated and complex in content, clarifying in greater detail the meaning of certain standard clauses and covering a broader range of issues. Third, economic development policy is becoming increasingly complicated by the web of overlapping commitments arising from IIAs containing a variety of provisions applicable to the same matters. Furthermore, the increasing activity in international investment treaty making has been paralleled by a rise in investor-State disputes. As a result of these developments, countries – and firms – have to operate within an increasingly complicated framework of multi-layered and multi-faceted investment rules.

The new generation of IIAs presents new challenges for policymakers. As global economic integration becomes ever deeper, managing the impacts of integration on the domestic economy becomes more complex and the challenges involved in concluding IIAs correspondingly greater.

This paper provides an overview of this new generation of IIAs, including the recent trends in the new generation of IIAs. The paper will also identify some of the key issues that have emerged in the new generation of IIAs, as well as some of the issues that arise as countries seek to ensure policy coherence in the face of a complex network of overlapping IIA provisions. Finally, the paper will conclude with a consideration of some of the implications for developing countries pertaining to the new generation of IIAs.

INTRODUCTION

More than forty years ago, developed countries began to initiate programmes to conclude IIAs with developing countries for the purpose of protecting investments of developed country investors in the territory of the developing countries. During the past fifteen years, however, a new generation of IIAs has emerged and the number of agreements has increased enormously.[1] This new generation, while continuing to provide protection for international investment stocks, increasingly emphasizes liberalizing access to resources and markets.

IIAs generally fall into two groups. The first group consists of BITs, agreements negotiated between two countries to protect and promote investment of investors of one party in the territory of the other party. These treaties date back to 1959 and traditionally had a relatively uniform content that until recently had not changed markedly since their inception, apart from the introduction of provisions on investor-State dispute resolution in the 1960s (UNCTAD, 1998). Since the mid-1990s, however, the conclusion of investment protection provisions within larger trade agreements has caused some re-examination of the content of the traditional investment provisions that had appeared in BITs. In addition, the submission of a growing number of investment disputes to arbitration under the investor-state arbitration provision also has prompted some re-evaluation of the content of traditional investment protection rules. As a result, the new generation of IIAs has witnessed some innovations in BIT practice and thus there is greater variation among these agreements than in the past.

The second group of IIAs considered in this overview consists of economic integration agreements (EIAs), which are agreements intended to facilitate the cross border movement of goods, services, capital, people or information. EIAs vary enormously and range from agreements that provide only for economic cooperation to agreements that create a common market. Such agreements may be bilateral, plurilateral, regional, interregional, multilateral or supranational (UNCTAD 2005a). They may involve countries at the same or at different levels of economic development. Within this widely divergent group of EIAs, the primary focus in this study will be on preferential

trade agreements that include investment provisions.[2] During the past decade, a number of countries, particularly those on the Pacific Rim, have concluded a new generation of IIAs comprising highly complex free trade agreements that liberalize trade in goods and services, while also containing investment protection provisions similar to those that traditionally have appeared in BITs. This new generation of treaties, like the new generation of BITs, has generated innovations in IIA practice.

The new generation of IIAs presents new challenges for policymakers. All IIAs, of course, limit the regulatory space within which countries can pursue their economic development policies. The new generation of IIAs, however, imposes a wider variety of disciplines touching more areas of host country activity and they often do so in a more complex and detailed way. Further, the interaction of agreements at different levels – including multilateral, plurilateral, regional and bilateral – creates complex interactions among agreements that exacerbate the sophistication found within agreements.

Notes

[1] These agreements have a variety of names, including free trade agreement, regional trade agreement, economic partnership agreement, new-age partnership agreement, economic complementation agreement, agreement for establishing a free trade area, closer economic partnership arrangement, framework agreements. For a detailed analysis, including the definition of these agreements see UNCTAD 2006.

[2] All instruments cited herein may be found in UNCTAD 1996, 2000a, 2001a, 2002, 2004a, 2005b and 2005c (also available on-line at www.unctad.org/iia). For the full texts of BITs, also visit www.unctad.org/iia.

I. RECENT TRENDS IN NEW GENERATION IIAs[1]

The new generation of IIAs has been shaped by a number of trends that have resulted in a growing number of agreements, as well as changes in their complexity and content. This section discusses some of the most important recent trends.

A. Growing universe of agreements

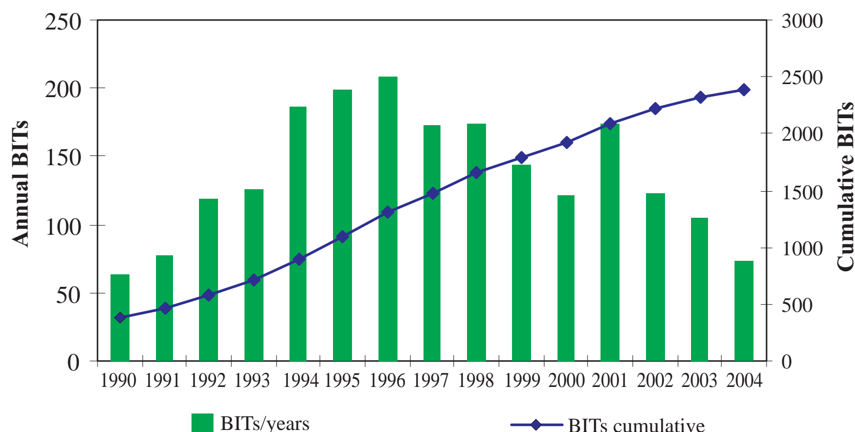
Since the 1990s, the universe of agreements has expanded enormously, although the rate of growth is different for different types of agreements. By the end of 2004, the number of BITs had reached 2,392. Nevertheless, the rate of increase in the number of BITs concluded has been in decline since 1996, when 209 agreements were concluded in one year. By contrast, 73 BITs were concluded in 2004, the smallest number since 1990 (Figure1).

The universe of IIAs includes some renegotiated BITs. Indeed, by the end of 2004, more than 85 BITs were the product of renegotiation. The trend toward renegotiation of BITs is expected to increase further since many BITs were signed in the 1990s with an initial term ranging from 10 to 30 years.

Often, the renegotiated BIT either supersedes or substantially amends the earlier agreement. In many cases, the renegotiation is the result of changed circumstances, especially the conclusion of other international agreements the terms of which must be harmonized with the BITs. For example, the BITs signed by ten Central European countries prior to their accession to the European Union (EU) in 2004 have been affected by these countries' membership in the EU. As a result, in late 2003 and early 2004, the United States and eight then acceding and candidate countries agreed to a package of BIT amendments and interpretations in the interest of avoiding incompatibilities between the requirements of EU membership and the United States BIT obligations. Canada is engaged in a similar exercise. In 2003, China renegotiated its 1983 BIT with Germany with improved levels of protection for the investor, including an investor-State dispute

settlement provision, which was not included in the previous BIT. Negotiations are also underway with several other European countries.

Figure 1. Number of BITs concluded, cumulative and year by year, 1990 – 2004



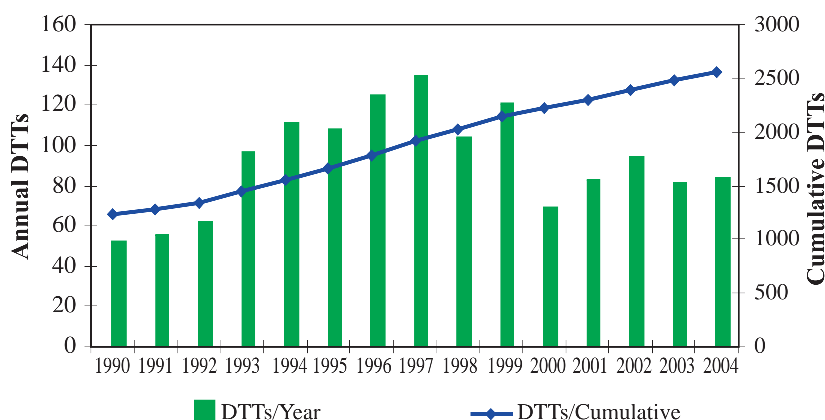
Source: UNCTAD (http://www.unctad.org/iia).

In terms of double taxation treaties (DTTs), in 2004 84 new treaties were concluded between 80 countries. This represents a sustained growth of DTTs, albeit at a slightly slower pace compared to the year 2003. Nevertheless, the total number of DTTs increased to reach 2,559 by the end of 2004 (Figure 2). Unlike BITs, the top 10 economies in terms of number of DTTs signed are all developed economies. About 39 per cent of all DTTs were concluded between developed and developing countries. DTTs among developed countries accounted for 29 per cent. Another 19 per cent involved transition economies, the remaining 13 per cent are between developing economies.

In as far as developing country-DTTs are concerned, a similar but less pronounced trend (as in the case of BITs) of increasing South-South investment cooperation can be observed. After the first South-South DTT was concluded in 1948 (by Argentina and Peru), DTTs proliferated during the second half of the 1990s. During the 1990s, 156 new DTTs were signed between 69 developing countries, bringing the total number of such treaties to 256 by the end of 1999. Growth persisted until 2004, with the number of South-South DTTs reaching 345 treaties between 90 countries.

In recent years, international investment rules increasingly have been adopted as part of bilateral, regional, interregional and plurilateral agreements that address, and seek to facilitate, trade and investment transactions. These agreements, in addition to containing a variable range of trade liberalization and promotion provisions, contain commitments to liberalize, and to protect and/or promote investment flows between the parties.

Figure 2. Number of DTTs concluded, cumulative and year-by-year, 1990-2004



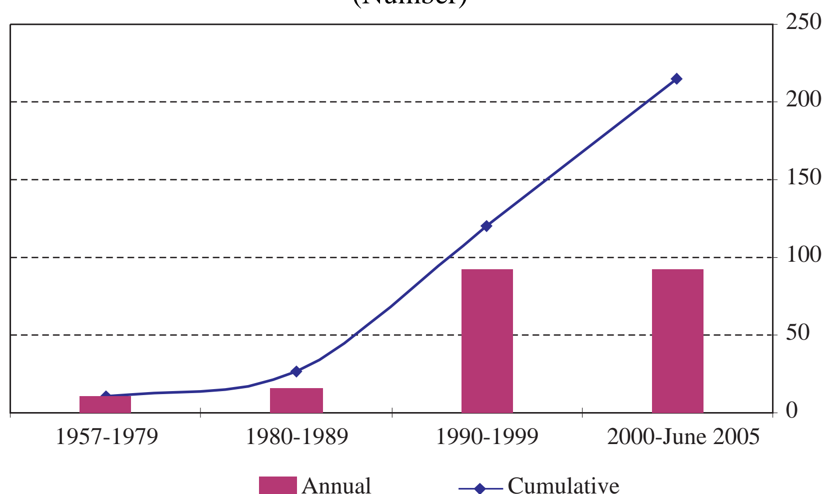
Source: UNCTAD (http://www.unctad.org/iia).

The number of such agreements has been growing steadily and, by June 2005, it exceeded 215. The large majority of these agreements, about 87 per cent, were concluded since the 1990s. Indeed, at least 34 new agreements were concluded in 2004 and early 2005 alone and about 66 others were under negotiation or consultation. Thus, while the rate at which new BITs are being concluded has been slowing, the rate at which new regional trade and investment agreements have been concluded has been increasing (Figure 3).

Initially, most of these treaties were between countries in the same region. Since 1990s, however, countries located in different regions began to conclude agreements with one another, with the result that interregional agreements now account for 44 per cent of the total preferential trade and investment agreements.

Figure 3. The growth of trade and investment agreements, other than BITs, 1957-June 2005

(Number)



Source: UNCTAD (http://www.unctad.org/iia).

The growth in the number of these agreements was accompanied by two important qualitative changes. First, such agreements, previously concluded principally among countries at similar levels of economic development, were concluded with greater frequency between developed and developing countries. By June 2005, 81 such agreements had been signed, including 77 since 1990. Thirty-nine more such agreements were under negotiation. Second, agreements among developing countries also experienced an enormous increase since the 1990s. By June 2005, at least 70 such agreements had been signed, including 59 since 1990. Another 24 agreements among developing countries were under negotiation (UNCTAD 2005e).

B. Expanded range of issues

Numerically, traditional BITs emphasizing the protection of foreign investment continue to dominate the framework of IIAs. This is particularly true in the case of South-South BITs. Nevertheless, a growing number of BITs includes more sophisticated investment protection provisions as well as liberalization commitments.

Investment provisions are increasingly being formulated as part of agreements that encompass a broader range of issues, including notably trade in goods and services, and other factors of production. While BITs continue to be more numerous than other trade and investment agreements, the latter occupy a much more important place in the international investment regime than they did a decade ago. Some countries increasingly prefer to address traditional investment protection as well as newer investment liberalization issues in the context of these broader agreements where investment provisions are only part of a larger framework for economic integration, rather than through the conclusion of traditional BITs.

Compared to BITs, other trade and investment agreements show far more variation in their scope, approach and content. Moreover, recent agreements tend to encompass a broader range of

issues that in the most comprehensive agreements may include not only investment protection and liberalization, but also trade in goods and services, intellectual property rights, competition policy, government procurement, temporary entry for business persons, transparency, the environment, and labor rights. Recent treaties concluded by countries such as Australia, Chile, Japan, Singapore, and the United States are especially comprehensive and detailed.

Not all recent IIAs have followed this pattern, however. Some recent agreements have remained rather narrow in their coverage of investment issues. They limit themselves to establishing a framework for cooperation on promotion of investments. Recent examples include the Free Trade Agreements between the EFTA countries and Romania and Croatia; bilateral Trade and Investment Cooperation Agreements between Canada and South Africa; and the ASEAN Framework Agreements with China and India (2002 and 2003, respectively), which lay down general principles with respect to committing to further investment liberalization, promotion and protection and pave the way for the future creation of a free trade and investment area. Other examples include a number of framework agreements on trade and investment relations between the United States and countries in Africa and the Middle East. The cooperation provided for is typically aimed at creating favorable conditions for encouraging trade and investment, notably through the exchange of information. It is also common for such agreements to set up consultative committees or a similar institutional arrangement between the parties to follow up on the implementation of negotiated commitments and to discuss and study possible obstacles to market access for trade and to the establishment of investment.

C. Increased sophistication and complexity

International investment rules are becoming increasingly sophisticated and complex in content. The greater level of sophistication and complexity, however, does not necessarily imply a

greater degree of stringency. For example, the greater complexity at times may be the result of an effort to define an obligation with greater specificity and thereby to clarify its scope and application.

Some recent IIAs include significant revisions to the wording of various substantive treaty obligations. One major impetus for these revisions stems from the North American Free Trade Agreement (NAFTA) among Canada, Mexico and the United States. Arbitrations under the investor-state dispute resolution provisions of NAFTA raised issues or resulted in awards that prompted the parties to reconsider some of the language used in their IIAs. For example, Canada and the United States subsequently modified the language of their BITs and other investment agreements to clarify the meaning of "fair and equitable treatment" and the concept of indirect expropriation.

The significant revisions can affect procedural provisions as well. As discussed below, some recent IIAs have made important innovations in the investor-state dispute resolution procedures. One purpose of these innovations is to increase transparency, by authorizing open hearings, publication of related documents, and the submission of *amicus curiae* ("friend of the court") briefs by non-disputants who have an interest in the arbitration. Another purpose of the innovations is to promote judicial economy by providing for early dismissal of frivolous claims and by attempting to prevent the presentation of the same claim in multiple forums. Other innovations, intended to foster sound and consistent results, include provisions for an appeal mechanism and for consultation with the treaty parties on certain issues.

As has been noted, other trade and investment agreements tend to address a broader range of economic transactions than BITs. The more issues that are addressed, the more complex is the agreement and the greater the likelihood of overlaps and inconsistencies. At the same time, their greater variation presents an opportunity for adopting different approaches to promote international investment flows that

better reflect the special circumstances of countries at different levels of economic development and in different regions.

D. South-South cooperation

Developed countries seeking to protect the investments of their investors continue to be the largest concluders of BITs. For example, seven of the ten countries that have signed the most BITs are Western European countries: Germany, Switzerland, the United Kingdom, France, the Netherlands, the Czech Republic and Italy (Figure 4).

Figure 4. Top ten economies signatories of BITs, end 2004
(Number)

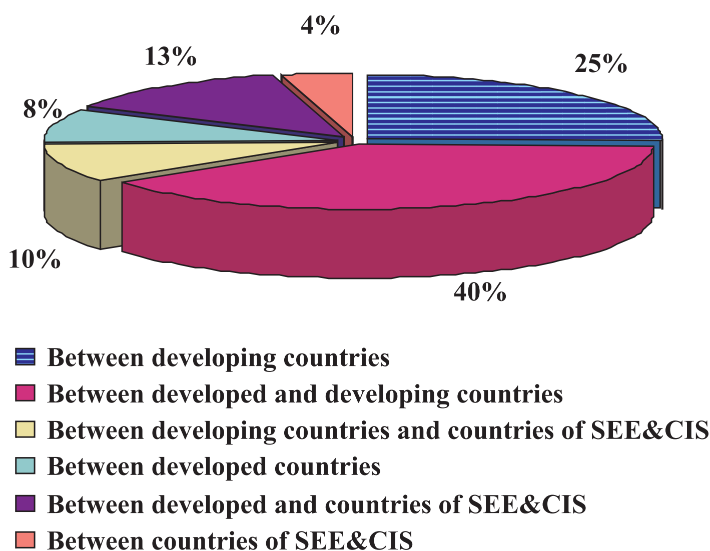
Source: UNCTAD (http://www.unctad.org/iia).

Many developing countries, however, are also extremely active participants in the process of concluding BITs. This reflects in part their desire to attract foreign investment, but also their emerging status as sources of outward investment (UNCTAD 2005e). For example, China

has concluded 112 BITs and is second only to Germany in the number of BITs concluded. Among developing countries, APEC members include many of the most active participants in BIT negotiations. The Republic of Korea has concluded 78 BITs, Malaysia 66 and Indonesia 58.

Indeed, developing countries are parties to the majority of BITs. As of the end of 2004, 40 percent of all BITs were between developed and developing economies, while 25 per cent were between developing economies. Another 10 percent were between developing and transitional economies. Thus, developing countries were one or both parties to 75 per cent of all BITs (Figure 5).

Figure 5. Total BITs concluded, end 2004, by country group
(Percentage)



Source: UNCTAD (http://www.unctad.org/iia).

Further, a clear trend toward increased South-South cooperation is evident. For example, in 2004, the largest number of BITs signed was between developing countries. Specifically, 28 of the 73 new BITs were between developing countries. This trend reflects both a greater emphasis on South-South cooperation on investment and an increase in the quantity of outward foreign direct investment flows from developing countries. Moreover, developing countries in Asia have been among the most active participants in concluding South-South BITs. For example, China, the Republic of Korea and Malaysia all have signed more than 40 BITs with other developing countries. In fact, each of these three countries has signed more agreements with other developing countries than with developed countries.

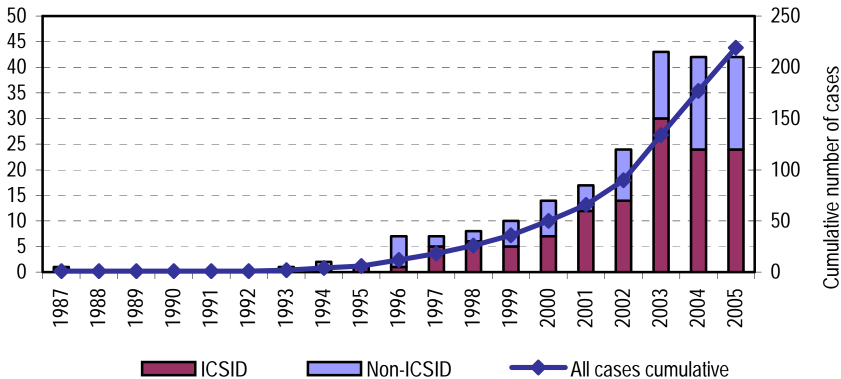
E. Increased number of investor-State disputes

The number of disputes submitted to arbitration has increased substantially in recent years. For example, while as of the end of 1994 only three investment-treaty related disputes had been submitted to the World Bank Group's International Centre for the Settlement of Investment Disputes (ICSID), by November 2005, 132 such disputes had been submitted. Another 87 treaty-based arbitrations not involving ICSID had been instituted as of the end of 2004, compared with two as of the end of 1994. Of the 219 claims known as of the end of 2005, almost 70 per cent had been filed during the prior four years (Figure 6). These figures do not include cases where a party has issued a notice of intent to submit a claim to arbitration, but has not yet actually commenced the arbitration. If these cases are submitted to arbitration, the number of pending claims will grow still further.[2]

The precise number of pending or decided claims is difficult to know. First, while ICSID maintains a public registry of claims, other arbitral mechanisms do not, meaning that no official records of all claims filed are available. Further, in some cases the investors or governments involved in a dispute wish to keep the dispute confidential, with the result that the disputants themselves may not

reveal the existence of a claim. Even where the pendency of a claim has been made public, such as in the case of a claim listed on the ICSID registry, often information about the nature of the claim is greatly lacking. Under typical rules of arbitrations, the award issued by the tribunal is provided to the parties on a confidential basis. The details of the claim and its resolution are likely to become public only if one of the disputants discloses them.

Figure 6. Known investment treaty arbitrations (cumulative and newly instituted cases, by year)
(Number)



Source: UNCTAD.

Because of these difficulties, the actual number of claims instituted is very likely larger than what is known. At least 61 governments – 37 of them in the developing world, 14 in developed countries and 10 in Southeast Europe and the Commonwealth of Independent States – have faced investment treaty arbitration. 42 claims have been launched against Argentina, 39 of which relate at least in part to that country's financial crisis. The number of claims against Argentina peaked in 2003 with 20 claims, and receded to 8 new claims in 2004 and 5 new cases in the first 10.5 months of 2005. Mexico has

the second highest number of known claims (17), most of them falling under NAFTA, and a handful under various BITs. The United States has also faced a sizeable number (11). India (9 claims), the Czech Republic (8), Egypt (8), Poland (7 claims), the Russian Federation (7) and Ecuador (7) also figure prominently, followed by Canada (6) and the Republic of Moldova (5).

The surge in the number of claims can be attributed to several factors. First, increases in international investment flows lead to more occasions for disputes. Second, with larger numbers of IIAs in place, more of these disputes are likely to involve an alleged violation of a treaty provision and more of them are likely to be within the ambit of a dispute settlement provision. Further, as news of large, successful claims spreads, more investors may be encouraged to utilize the investor-State dispute resolution mechanism. Greater transparency in arbitration (e.g. NAFTA) may also be a factor.

Virtually all of these claims have been instituted by investors. Of the cases instituted to date, only one has been instituted by a government (a claim between Chile and Peru). This claim was instituted by Peru following an investor-State claim filed by a Chilean firm against Peru.

Recent cases have involved the whole range of investment activities and all kinds of investments, including privatization contracts and State concessions. Measures that have been challenged include emergency laws put in place during a financial crisis, value added taxes, rezoning of land from agricultural use to commercial use, measures on hazardous waste facilities, issues related to the intent to divest shareholdings of public enterprises to a foreign investor, and treatment at the hands of media regulators. Disputes have involved provisions such as those on fair and equitable treatment, non-discrimination, expropriation, and the scope and definition of agreements. These disputes are yielding awards that interpret the

agreements, which in turn have caused the parties to the agreements to reconsider some of the terms.

Although the financial implications of the investor-State dispute resolution process can be substantial, the information available thus far does not provide a clear picture of the full nature of those implications. Information about the quantum of damages sought by investors tends to be sporadic and unreliable, in part because many claims are still in a preliminary stage and claimants often are not required to quantify their claims until a later stage in the proceedings. Nevertheless, it is known that some claims involve large sums, in some cases in the hundreds of millions of dollars. Further, because the number of awards issued to date is relatively small, it remains unclear how frequently large claims will be successful. Nevertheless, it is known that a tribunal in 2003 awarded $270 million plus interest in a claim against the Czech Republic, while another tribunal in 2002 awarded $71 million in a claim against Ecuador. Even assuming that a claim is unsuccessful, the cost of defense can be significant (on average $1 to 2 million, including attorneys' fees and the costs of the tribunal). Claimants typically incur similar costs.

Notes

[1] This section draws on UNCTAD 2005d.
[2] For a detailed discussion, see UNCTAD 2005a.

II. KEY ISSUES IN NEW GENERATION IIAs

The conclusion of an IIA raises a wide range of policy issues that must be addressed by the parties. This section discusses some of the key issues presented by the new generation of IIAs.

A. Scope of the agreement

Many different provisions affect the scope of an IIA. Within the new generation of IIAs, however, key issues have arisen particularly with regard to two types of provisions: those that define the term "investment" and "investor" and those that create exceptions to take into account governmental policies, including those of developing countries.

1. Definition of "Investment" and "Investor"

BITs typically define the subject matter with which they are dealing. The typical BIT provision defines "investment" as "every kind of asset" and includes an illustrative, non-exhaustive list of assets that fall within the definition (UNCTAD 1999a). In many BITs, the list includes five categories of assets: movable and immovable property, companies and interests in companies (whether direct or portfolio investment), contract rights, intellectual property, and business concessions. This is also the most common definition found in the new generation of other trade and investment agreements.

This definition is very broad. Most BITs are based on model negotiating texts prepared by capital exporting countries, which usually seek to ensure that the agreements protect the widest array of their assets in the territories of their capital importing treaty partners. However, capital-exporting countries did not always anticipate that they would be hosts to significant amounts of investment from such partners. Nevertheless, from the perspective of a developing country, the broad definition potentially can be defended on the ground that virtually any asset can contribute to economic development, that the purpose of the treaty is to promote and protect investments that contribute to economic development, and that to exclude certain assets could risk undermining the purpose of the treaty. This definition is also open-ended to permit

new economic arrangements that the home country may wish to protect or that may contribute to development to fall within the definition without having to amend the treaty (UNCTAD 2001b).

Concerns have been raised about the scope and open-ended nature of this definition. One concern has been that certain assets should be excluded from the definition. In fact, certain assets, such as merchandise held for trade, could fall within the broad definition even though they do not have any of the economic characteristics of an investment. Another concern has been that an open-ended definition could result in coverage of assets that the negotiators of the agreement did not contemplate to include. Accordingly, some recent IIAs have taken other approaches to defining "investment," though the broad, open-ended definition remains by far the most common.

One alternative is to define "investment" as including only those assets that have the economic characteristics of an investment. Article 10.27 of the 2003 Chile-United States Free Trade Agreement, for example, defines "investment" as:

> "… 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."

The definition goes on to list certain forms that investment may take. Though organized differently, the scope is similar to the illustrative list that appears in the typical broad definition of "investment". This definition may be viewed as excluding assets that may be held for economic purposes, but do not contribute to the productive capacity of an economy. An earlier variation of this approach was to adopt a tautological definition of investment, under which "investment" is defined as "every kind of investment." Although tautological definitions are subject to the criticism that they do not add

sufficient meaning, the tautology was intended to emphasize that an asset must have the characteristics of an investment to be covered by the treaty.

A second alternative is to omit the broad, open-ended language and to define "investment" in terms of a finite list of categories of assets. This approach eliminates to some extent the open-ended element of the definition because it limits investment only to those assets listed, although the categories themselves could have an open-ended quality to them. For example, in the new Canada model BIT, investment is defined as an enterprise, certain equity or debt securities of an enterprise, or certain loans to an enterprise. This definition not only limits investment to those assets falling within a finite list, but also requires that the assets be associated in some way with an enterprise. Assets associated with an enterprise are more likely to have the economic character of an investment.

Some countries have been concerned about including portfolio investment within the ambit of an investment protection agreement because they doubt that portfolio investment contributes sufficiently to economic development and believe that its potentially volatile nature can be harmful to development. Thus, some IIAs limit the definition of investment to direct investment. For example, article 45 of the 2000 Free Trade Agreement between the EFTA countries and the United Mexican States provides that:

> "… investment made in accordance with the laws and regulations of the Parties means direct investment, which is defined as investment for the purpose of establishing lasting economic relations with an undertaking such as, in particular, investments which give the possibility of exercising an effective influence on the management thereof."

This definition requires that the assets have not only the character of investment, but the character of direct investment.

The concern about including portfolio investment is sometimes especially present when an IIA creates a right to establish investment in the host country. For example, the 1987 ASEAN Agreement for the Promotion and Protection of Investment, which does not include a right to establish investment, utilizes the broad, asset-based definition. By contrast, the 1998 Framework Agreement on the ASEAN Investment Area, which does include a right of establishment, explicitly excludes portfolio investment from its coverage.

In some cases, the category of assets sought to be excluded from the definition is somewhat narrower. Some countries have sought to limit the definition of investment to assets used for economic purposes. For example, the 2000 BIT between Mexico and Greece defines "investment" as:

> "…every kind of asset acquired or used for economic purposes and invested by an investor of one Contracting Party in the territory of the other Contracting Party. . ."

This definition includes the illustrative list of assets that appears in the broad definition. Essentially, it is intended to exclude assets used for non-business purposes, such as a vacation home.

IIAs often also define the term "investor." Critical issues related to this term include the types of entities that can be considered "investors" and the tests for establishing the nationality of the investor. The latter is particularly critical because the investment generally must have the nationality of a treaty party in order to be protected.

New generation IIAs have not greatly modified the approaches taken on these issues in the past, though two minor trends are noteworthy. First, whereas traditionally corporate nationality was generally ascribed based on one of three tests – place of incorporation, principal place of business, or place of ownership – some new

generation IIAs have used a commercial presence test that ascribes to an investor the nationality of the place where it has a commercial presence. Second, although the place of incorporation test has become more widely used than in the past, it is often accompanied by a clause allowing the host country to deny the benefits of the treaty to an investor who is organized under the laws of another party, but has no substantial business activities in the territory of the home country. This provision, in other words, reserves the right to the host country to limit treaty protection to corporate entities having some significant economic link with the economy of another party (UNCTAD 2001c).

2. Exceptions

The scope of an IIA is also determined by a variety of exceptions, very often included to address specific developmental concerns. These provisions are intended to preserve for host countries sufficient policy space to pursue developmental or other objectives in ways that otherwise may be difficult to reconcile with treaty obligations. The trend within new generation IIAs has been to increase the number of exceptions, again yielding treaties that are more detailed and complex than in the past.

It has been not unusual to exempt matters of taxation from some or all treaty obligations, in part because of the complexity of tax matters and in part because they are often covered by other agreements, such as DTTs. This exception continues to be found in new generation IIAs, although there is a trend toward somewhat more complex provisions, as some countries seek to apply the IIA to at least some aspects of taxation (UNCTAD 2000b).

A common exception in IIAs has been to exempt from the most-favoured nation treatment (MFN) obligation treatment guaranteed under a customs union or free trade agreement. This exception is intended to prevent non-members from free riding on special concessions made to members of a regional economic integration

agreement, typically in exchange for special concessions made by those members (UNCTAD 2005f). Although there are examples of IIAs that do not include this exception, it continues to be common, and in some new generation IIAs it applies to all provisions of the treaty, not merely the MFN provision.

Other common exceptions exclude from IIA obligations measures taken to protect a country's essential security interests or to maintain public order. These also can be found in new generation IIAs.

Some exceptions have become more prevalent within new generation IIAs than in the past. Examples of these include exceptions for measures necessary to protect health, safety or the environment, to regulate financial services, or to preserve cultural patrimony, industries or diversity. The growing number of exceptions reflects the increased awareness of the complexity involved in balancing different policy objectives and the desire of IIA parties to preserve national policy space.

Some exceptions specifically address the special needs of developing countries. For example, some IIAs allow a transitional period during which a developing country or transitional economy assumes obligations gradually. For example, article 7 (4) of the Framework Agreement on the ASEAN Investment Area, as amended in 2001, provides that:

> "… the Temporary Exclusion List for the manufacturing sector shall be progressively phased out by all Member States by 2003, except the Kingdom of Cambodia, the Lao People's Democratic Republic and the Socialist Republic of Viet Nam which shall do so not later than 2010."

A second approach is to allow existing exceptions to the principles of the IIA to remain in place. This approach is evident in the agreements, discussed elsewhere, in which the right of establishment is

made subject to exceptions set forth in an annex to the treaty. The exceptions may be permitted indefinitely or they may be allowed only for a limited period of time.

A third approach is to authorize special and differential treatment for developing countries with respect to the implementation of the substantive obligations of the agreement. This approach goes beyond allowing existing exceptions and contemplates treating some parties differently than others throughout the process of implementing the agreement. For example, article 85 (1) of the 2000 partnership agreement between the African, Caribbean and Pacific countries and the European Community provides that:

> "The least-developed ACP States shall be accorded a special treatment in order to enable them to overcome the serious economic and social difficulties hindering their development so as to step up their respective rates of development."

A fourth approach is to establish permanent exceptions that permit deviation from the principles of the treaty on a temporary basis. The most common such provision is one allowing denial of the right of free transfers in the event of balance of payments difficulties, a provision that is discussed below in the section on currency transfers.

B. Liberalization

Traditionally, the great majority of IIAs protected investment only after it was established in the territory of a party. IIAs typically did not grant to covered investors the right to establish investment in the territory of the other party. The new generation of IIAs, however, increasingly provides for liberalization of investment flows. Liberalization provisions are generally of two types. One type, which began to appear in BITs in the 1980s, requires each party to permit investors of the other party to establish investment within the territory of the first party. The other type, which traces its origin to the GATS

agreement, guarantees service providers of one party access to the market of the other parties. Because services are often supplied through the establishment of a commercial presence, these provisions in effect also create a right of establishment of investment. This subsection discusses some of the issues raised by these provisions in the new generation of IIAs.

1. Admission and establishment of investment

Under customary international law, no country is required to permit the acquisition or establishment of investment by nationals or companies of another country within its territory. A country is unlikely to permit foreign investors an unrestricted right to invest in its territory (UNCTAD 1999b). A country may regard foreign investment in certain sectors of its economy as contrary to vital national interests, whether they be military, cultural or economic. Thus, when a right of establishment appears in an IIA, it is generally limited in some way. Four basic approaches are evident.

The strongest approach from the perspective of the foreign investor is to provide that covered investors have a right to establish investment in the host country, though usually subject to exceptions in an annex. For example, article 7(1) of the 2001 Framework Agreement on the ASEAN Investment Area provides that:

> "Subject to the provisions of this Article, each Member State shall: (a) open immediately all its industries for investments by ASEAN investors;"

The remainder of the article, however, provides for a list of temporary exclusions from the right of establishment, which is to be phased out gradually by 2010. The right of establishment is further qualified by an emergency safeguards provision, article 14 (1), which provides that:

> "If, as a result of the implementation of the liberalization programme under this Agreement, a Member State suffers or is threatened with any serious injury and threat, the Member State may take emergency safeguard measures to the extent and for such period as may be necessary to prevent or remedy such injury. The measures taken shall be provisional and without discrimination."

A second approach is to guarantee to covered foreign investors national and MFN treatment with respect to the right to establish investment in the host country. These guarantees are sometimes described as "pre-establishment" guarantees of national and MFN treatment. They are to be distinguished from "post-establishment" guarantees (discussed in section II.C.2 below), which do not liberalize investment flows because they impose no obligation on the host country to permit investment, but merely provide for non-discriminatory treatment for investment after it has been established. In some agreements, the only pre-establishment obligation is to provide MFN treatment. The pre-establishment right is generally qualified by a provision that allows the host country to specify sectors of the economy in which the right does not apply, the so-called "negative list" approach.

The negative list approach has been utilized in these agreements because it tends to result in more extensive liberalization, since it creates a presumption in favor of liberalization by liberalizing all sectors not explicitly excluded, and because of its advantages for transparency, in that it puts investors on notice of all sectors in which liberalization commitments have not been made. As more agreements utilizing this approach have been concluded, the annexes have also become somewhat more complex. For example, some agreements concluded in recent years include separate annexes, one for reservations to the right of national treatment and another for reservations to the right of MFN treatment.

Other agreements have an even more complex structure of annexes. For example, the 2004 United States model BIT includes one annex listing existing non-conforming measures in regard to which a party reserves the right to maintain and to modify them, as long as the modification does not increase the non-conformity of the measure, and a separate annex listing sectors of the economy in which a party reserves the right to impose future non-conforming measures. Still more complex is the approach, seen for example in the Japan-Republic of Korea BIT, under which one annex sets forth sectors in which a party reserves the right to maintain non-conforming measures and another annex sets forth sectors in which a party reserves the right to maintain existing non-conforming measures that may not be modified in any way that increases their non-conformity and that the party shall endeavor to progressively reduce or eliminate. In addition, new non-conforming measures may be introduced only when exceptional financial or industrial circumstances exist.

A third approach, which remains the most common one, requires each party to admit investment "in accordance with its laws." Under this approach, the right to establish investment is limited to whatever is permitted under the laws of the host country, which the host country may change at any time. Thus, this provision protects the foreign investor against a host country's denial of the right to establish only where such denial is in violation of the host country's own laws.

A fourth approach is simply to provide for future liberalization. This approach does not result in any liberalization upon entry into force of the agreement. Its significance depends entirely upon the actions of the parties in the future. Examples of this approach include the Framework Agreements between ASEAN and China and between ASEAN and India, concluded in 2002 and 2003, respectively.

2. *Market access for services*

During the Uruguay Round of trade negotiations, many IIAs began to include provisions on trade in services. Because one of the modalities by which services are delivered is through a commercial presence and a commercial presence usually falls within even a narrow definition of investment, agreements regarding trade in services very often affect investments. More specifically, agreements that guarantee market access for trade in services provide what, in effect, is a right of establishment in the services sector. Four general approaches are evident with respect to providing market access for services.

The first approach is to include in the IIA a chapter on services that is structured similarly to the GATS. Several countries, including Australia, Chile, Japan, Singapore and the United States, have recently begun to conclude agreements adopting this approach. Illustrative is the 2002 Agreement between the Republic of Singapore and Japan for a New-Age Economic Partnership Agreement (EPA). Under article 59, the parties are to inscribe in a schedule commitments to permit market access in certain service sectors with respect to certain modes of supply, the so-called "positive list" approach because it guarantees market access only to the extent set forth in the schedule. Under article 60, the parties may make specific commitments to provide national treatment with respect to measures affecting the supply of services. article 64 contains disciplines on domestic regulation of trade in services similar to those in the GATS. Article 65 requires the parties to ensure that monopoly suppliers of services in their territories do not act in a manner inconsistent with a party's specific commitments, while article 66 calls for consultations to eliminate business practices that may restrain competition and thereby restrict trade in services. Under articles 67 and 68, restrictions on transfers for current transactions relating to specific commitments are prohibited, subject to an exception for serious balance of payments and external financial difficulties.

A second approach is to include market access commitments structured differently from those that appear in the GATS. Illustrative of this approach is the NAFTA, which guarantees national and MFN treatment with respect to the supply of services, subject to exceptions contained in an annex. It further requires the parties to set forth in an annex their commitments to liberalize quantitative restrictions, licensing requirements, performance requirements or other non-discriminatory measures. The NAFTA approach is to create a general rule of market access in all service sectors, subject to exceptions contained in an annex, the "negative list" approach.

A third approach, which appears in the Euro-Mediterranean Agreements concluded by the European Communities,[1] is to affirm or incorporate the parties' commitments under the GATS. This approach does not result in any liberalization, since it affirms only the already existing liberalization under the GATS. This provision is not necessarily without effect, however. To the extent that it incorporates by reference the parties' commitments under the GATS, one could argue that GATS commitments become commitments under the IIA as well and that any violation of those GATS commitments also would violate the IIA and be subject to any applicable dispute resolution mechanism under the IIA as well as under the GATS.

The fourth approach is to include a general commitment to future liberalization of trade in services. For example, article III of the 1995 ASEAN Framework Agreement on Services provides that:

> "Member States shall liberalize trade in services in a substantial number of sectors within a reasonable time-frame by:
>
> (a) eliminating substantially all existing discriminatory measures and market access limitations amongst Member States; and

(b) prohibiting new or more discriminatory measures and market access limitations."

Article IV provides that the members shall enter into negotiations "directed toward achieving commitments which are beyond those inscribed in each Member State's schedule of commitments under the GATS and for which Member States shall accord preferential treatment to one another on an MFN basis." These commitments are to be set out in a schedule. Under article X, these commitments may be modified or withdrawn after three years, provided that compensatory adjustments are made. Adoption of this fourth approach by itself also does not result in any liberalization, but does bring the parties on a course toward future liberalization.

C. General standards of treatment

1. Fair and equitable treatment

The meaning of the "fair and equitable treatment" standard has become an issue in recent IIAs. More precisely, the issue is whether the fair and equitable treatment standard incorporates the international minimum standard required by customary international law or whether it imposes other, possibly more stringent, obligations on the host country (UNCTAD 1999c).

As a result of concerns about the potential scope of the fair and equitable treatment standard, some recent IIAs have adopted language that either explicitly or implicitly indicates that the standard requires no more than is required under customary international law. An example of this explicit language is contained in the 2004 BIT between the United States and Uruguay (not yet in force), which provides in article 5.1 that:

> "Each Party shall accord covered investments treatment in accordance with customary international law, including fair and equitable treatment..."

Article 5.2 goes on to state that:

> "… paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments. The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights."

An example of the implicit language is that contained in the 2000 BIT between Mexico and Sweden, article 3(2) of which provides that:

> "Investment by investors of a Contracting Party shall at all times be accorded fair and equitable treatment in accordance with the relevant international standards under International Law. Neither Contracting Party shall impair by arbitrary or discriminatory measures the management, maintenance, use, enjoyment or disposal of such investments."

This seems to imply that fair and equitable treatment is a principle of customary international law, not a separate treaty-based right.

Some IIAs, however, define fair and equitable treatment in such a way as to strongly suggest that they do not equate the standard with the requirements of customary international law. For example, article 3 of the 2002 BIT between France and Uganda characterizes as impediments to fair and equitable treatment "…any restriction to free movement, purchase and sale of goods and services, as well as any

other measures that have a similar effect." This goes well beyond the requirements of customary international law. In contrast, Appendix A of the Trade and Economic Cooperation Agreement between the CARICOM countries and Cuba on the reciprocal promotion and protection of investments requires "fair and equitable treatment of Investments of Investors of the other Party under and subject to national laws and regulations," which seems to limit fair and equitable treatment to compliance with domestic law.

Another approach, used by some APEC economies in their BITs, is to combine in one single clause the fair and equitable treatment standard, which is an absolute standard of protection, with the national and MFN treatment standards, which are relative and contingent parameters of treatment. For example, article III.1 of the 1997 BIT between Denmark and the Philippines states that:

> "Each Contracting Party shall accord to investments made by investors of the other Contracting Party fair and equitable treatment which in no case shall be less favourable than that accorded to its own investors or to investors of any third state, whichever is more favourable to the investor."

Similar provisions can be found in article 4.2 of the 1995 BIT between Thailand and Philippines, and article IV.2 of the 1987 Agreement among the Governments of Brunei Darussalam, Indonesia, Malaysia, Philippines, Singapore and Thailand for the promotion and protection of investments. Providing that the fair and equitable treatment shall in no case be less favorable than national or MFN treatment suggests that the parties do not visualize the fair and equitable treatment standard as the international minimum standard according to customary international law.

None of these elaborations upon the meaning of the fair and equitable treatment clause will necessarily end the debate about its meaning. Those formulations that link it explicitly to customary

international law could be characterized as making explicit what had been intended in similar "fair and equitable treatment" clauses, while other clauses could be characterized as applying a special meaning to the clause in the context of a particular treaty.

2. Most-favoured nation (MFN) and national treatment

Although the majority of BITs since long have required MFN and national treatment with respect to investment once established, in recent years a number of countries, including a number of those in APEC, have omitted the national treatment standard from at least some of their BITs. Among those countries that have omitted this standard from some BITs concluded since 1995 are Australia, Brunei Darussalam, Indonesia, Malaysia, and Singapore. A number of other BITs involving APEC economies have included the national treatment standard, but subordinated it to the domestic law of the host country. Thus, the host country does not need to provide national treatment except to the extent required by domestic law, which the host country is free to change at any time. The practical significance of omitting this standard or subordinating it to domestic law might be limited because often these countries have concluded at least one other IIA that includes a national treatment provision and, if so, then such a standard of treatment could be applicable to investors of any country covered by an international investment agreement with an MFN clause (UNCTAD 2000c, 1999d).

Recent IIAs have also seen some variation in the scope of the MFN and national treatment clauses. Whereas IIAs traditionally applied MFN and national treatment to covered investments or investors or both, some recent IIAs apply MFN and national treatment only to specified activities concerning the investment. For example, the 2002 BIT between the Russian Federation and Thailand guarantees MFN and national treatment to investors "as regards their management, maintenance, use, enjoyment or disposal of their investments…" language that is perhaps narrower than the usual formulation. Similar

language appears in BITs concluded by a number of APEC economies, including the United States, Canada, Australia, Brunei Darussalam, and the Republic of Korea.[2]

IIAs may also narrow the scope of the MFN clause by excluding from this standard treatment provided by specific other agreements. For example, Annex III of the Canadian model BIT provides that the MFN article "shall not apply to treatment accorded under all bilateral or multilateral international agreements in force or signed prior to the date of entry into force of this Agreement".

Some recent IIAs also permit the parties to narrow the scope of MFN or national treatment clauses by exempting certain sectors or matters from the scope of theses clauses. One approach is to include an annex to the treaty in which the parties may list sectors or matters to which the MFN or national treatment standard does not apply. The model BITs currently used by Canada and the United States categorically exclude from MFN treatment government procurement and subsidies and grants provided by a party, including government supported loans, guarantees and insurance. Another approach, typified by the 2001 BIT between China and the Netherlands, exempts from China's MFN and national treatment obligations existing non-conforming measures as well as any amendment to any non-conforming measure that does not increase the non-conformity of the measure.

Some IIAs add language that may tend to broaden the scope of the MFN or national treatment standard. For example, the 1998 BIT between Japan and Bangladesh guarantees national treatment "…in respect of investments, returns and business activities in connection with the investment." This BIT goes on to define "business activities in connection with investment" to include the maintenance of various establishments appropriate to the conduct of business activities, the management of companies, the employment of certain personnel, the making and performance of contracts, and the use, enjoyment and disposal of investments.

D. Expropriation

A major impetus for the negotiation of IIAs is to obtain protection for FDI against expropriation by the host country. Capital exporting countries seek to ensure through IIAs that an expropriation would be lawful only if it was for a public purpose, non-discriminatory, consistent with due process, and accompanied by compensation, generally at fair market value. The standard of compensation generally was the issue of the greatest concern in the negotiation of the expropriation provision (UNCTAD 2000d).

The classic example of an expropriation is an act that transfers ownership or possession of the investment to the state. An act that completely destroys the value of an investment is also typically regarded as an expropriation. Because expropriations sometimes occur through a series of actions rather than a single act, many IIAs have defined expropriation to include measures that, taken together, are equivalent to, or have the same effect as, an expropriation. Such language, however, still leaves unclear what degree of interference with the rights of ownership is required for an act or series of acts to constitute an expropriation. Acts that only partially devalue an investment, however, may be viewed by the host country as merely routine regulatory acts that are not the equivalent of an expropriation. Following the conclusion of the NAFTA, a number of investment arbitrations were commenced in which claimants argued that various regulatory acts were expropriations that entitled them to compensation. Many host countries feared that if arbitral tribunals required compensation for such "regulatory expropriations," the cost of regulating in sensitive areas such as health or environmental protection could become prohibitive.

Recent IIAs have begun to address this concern by attempting to clarify what is meant by the term "expropriation." For example, Annex 10-D of the 2003 Chile-United States Free Trade Agreement states that:

> "An action or a series of actions by a Party cannot constitute an expropriation unless it interferes with a tangible or intangible property right or property interest in an investment."

It then goes on to explain that the expropriation article "addresses two situations. The first is direct expropriation, where an investment is nationalized or otherwise directly expropriated through formal transfer of title or outright seizure." A separate paragraph attempts to define more carefully what types of actions beyond these traditional forms of expropriation might constitute an expropriation. It states that:

> " (a) The determination of whether an action or series of actions by a Party, in a specific fact situation, constitutes an indirect expropriation, requires a case-by-case, fact-based inquiry that considers, among other factors:
>
> > (i) the economic impact of the government action, although the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred;
> >
> > (ii) the extent to which the government action interferes with distinct, reasonable investment-backed expectations; and
> >
> > (iii) the character of the government action.
>
> (b) Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations. "

The language in paragraph (b) asserts that regulatory actions do not typically constitute an expropriation, but it does not exclude this possibility entirely. This language again illustrates the trend in some new generation IIAs to clarify with greater specificity the meaning of traditional IIA provisions in response to concerns arising from claims filed through the investor-State dispute resolution process.

E. Transfers of funds

A common provision in IIAs guarantees to investors the right to transfer their investment and any returns from their investment into a freely convertible or freely usable currency (UNCTAD 2000e). Some IIAs specify in more detail the kind of transfers protected by the agreement. For example, article 46 of the 2000 Free Trade Agreement between the EFTA States and the United Mexican States provides that:

> "The EFTA States and Mexico shall with respect to investments in their territories by investors of another Party guarantee the right of free transfer, into and out of their territories, including initial plus any additional capital, returns, payments under contract, royalties and fees, proceeds from the sale or liquidation of all or any part of an investment."

Typically, those IIA provisions that apply only to specified transfers are quite broad and include in the list most types of payments that an investor would wish to make.

In some cases, like in the above example, the provision applies to transfers into, as well as out of, the host country. That is, it creates a right not only to repatriate capital but also to bring capital into the host country's territory. Once an investment has been established, the investor has the right, under this language, to transfer funds relating to the investment into the territory. Such provisions reflect the fact that international production has become increasingly integrated and that

permitting transfers of payments between related facilities in different countries is of growing importance to investors.

Transfer provisions in IIAs may raise serious concerns on the part of host countries. One concern is that an investor may seek to transfer a large sum at a time when foreign exchange reserves are low, thereby depleting exchange reserves needed for other purposes. Another concern is that permitting free transfers might result in massive capital flight during times of economic difficulty, thus exacerbating the host country's problems. For these reasons, recent IIAs often limit the right of free transfers.

One approach is to implement the right of free transfers gradually. This approach, which is typical of the association agreements between the European Union and the transition economies, provides the host country with the ability to maintain existing currency restrictions for a period of time, while also reassuring investors with the promise of the eventual elimination of those restrictions. This approach, however, does not provide any flexibility for the host country once the transitional period has ended.

A second approach is to include an exception to the transfer provision during periods of balance of payment difficulties. Such provisions typically allow a party to restrict transfers when foreign currency reserves reach low levels, provided that certain conditions are met. Examples of such conditions are that the restrictions be no greater in scope or duration than is necessary, be progressively eliminated, and be applied on a non-discriminatory basis.

A third approach is to explicitly subordinate the right of transfer to the parties' exchange restrictions, which may change at any time. Thus, this last provision protects the investor only against restrictions on transfers that violate host country laws.

Finally, as IIAs increasingly include provisions on financial services, some recent agreements have included provisions that exempt payments by financial institutions from the transfer provision. Such provisions are intended to allow countries the freedom to regulate financial services, a sector that is usually heavily regulated. For example, article 17.1 of the 2003 BIT between Japan and Viet Nam states:

> "Notwithstanding any other provisions of this Agreement, a Contracting Party may adopt or maintain prudential measures with respect to financial services, including measures for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by an enterprise providing financial services, or to ensure the integrity and stability of its financial system."

F. Performance requirements

Host countries sometimes impose requirements on foreign investment that are intended to mandate the behavior of investments in order to shape their economic consequences. For example, to ensure that the investment contributes to employment or has a favorable impact on the balance of payments, the host country may seek to require the investment to hire local employees, purchase its inputs locally, or export at least some percentage of its product. Such requirements are often referred to as "performance requirements." In many cases, performance requirements are imposed as a condition of permitting the investment to be established or as a condition of receiving a special benefit or advantage. Such requirements may interfere with the investor's prerogative to manage its investment and may impair the value of the investment. They also may distort trade by preventing the importation of goods or services or by requiring the exportation of goods or services, a consequence that could be of concern in negotiating an agreement to liberalize trade (UNCTAD 2001c). Finally, they may function as a mechanism for discriminating

among investments, by subjecting some investments to more burdensome requirements than others.

In general, IIAs adopt one of three models in addressing performance requirements.

The first model, which is by far the most prevalent, is to include no explicit provisions on performance requirements. The prevalence of this model reflects the strong desire of many developing countries to utilize performance requirements in at least certain cases. In this model, of course, performance requirements still would be prohibited to the extent that they violate more general IIA provisions, such the national treatment standard, or are contrary to the WTO TRIMs Agreement, provided that the countries concerned are WTO members. In other words, this model does not usually include any special exception to general treaty obligations to allow performance requirements. To the extent that the agreement included only post-establishment national treatment obligations, however, performance requirements imposed as a condition of establishment might very well be consistent with those obligations. Further, a host country could reserve the right to impose performance requirements that violated the national treatment standard if the agreement was one that allowed the host country to maintain exceptions to national treatment that are specified in an annex and the host country had made the necessary specifications.

The second model, which is most often found in IIAs concluded by the European Union, requires one or both parties to comply with the WTO TRIMs Agreement, which prohibits certain performance requirements that are inconsistent with the provisions on national treatment and quantitative restriction in the GATT. To the extent that the parties affected are already parties to the TRIMS agreement, these provisions impose no further obligations on them. They do, however, incorporate the existing obligations into the IIA and thus may make those same obligations enforceable through any dispute

resolution mechanism contained in the IIA, and not only the WTO dispute resolution procedures.

The third model, found in a number of new generation IIAs, is to include prohibitions on performance requirements beyond those addressed by the TRIMs Agreement. Because the concept of a performance requirement is potentially quite broad and not well defined, the prohibition on performance requirements in these agreements usually applies only to certain specified performance requirements. The list that most commonly appears in recent IIAs, particularly those concluded by the United States, is based on article 1106 of the NAFTA. It includes export requirements, domestic content requirements, requirements to use domestic suppliers, technology transfer requirements, or requirements that relate the volume or value of imports or the quantum of domestic sales to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment.

Recognizing, however, that performance requirements are regarded by some host countries as an important element of their economic development policy, recent IIAs that contain disciplines on performance requirements nevertheless have employed various means to leave the host country with some discretion to use them and thereby to strike a balance between the host country's economic development policy and the protection of foreign investment. One approach, for example, is to allow the parties to maintain exceptions to the prohibition on performance requirements set forth in an annex to the treaty. Another approach is to distinguish between two categories of performance requirements. The first category, which consists of those performance requirements deemed to be the most undesirable, may not be imposed on investment for any reason. The second category, which consists of those performance requirements deemed somewhat less undesirable, may be imposed on investment as a condition to the receipt of an advantage. That is, the host country may offer a special incentive to an investment in exchange for a commitment by the investment to

observe certain performance requirements, if those performance requirements fall into the second category. Under this approach, the prohibitions on both categories of performance requirements typically are subject to exceptions set forth in an annex.

One unusual feature that appears in some recent IIAs, which follow the third model is a provision that the prohibition on performance requirements applies to all investments, not merely to those of investors of the parties to the agreement. Such a provision is intended to prevent performance requirements from becoming a method of discriminating among investments of different nationalities.

G. Intellectual property rights

Intellectual property generally falls within the definition of "investment" and thus is protected against many forms of host country interference by the various investment protection provisions of the IIAs. Recent IIAs move beyond this basic approach and generally have one of three types of provision on intellectual property protection: They may require adherence to international intellectual property protection agreements, require that a certain minimum standard of protection be provided, or require non-discrimination with respect to protection of intellectual property rights.

The first approach is to ensure that the protection of intellectual property rights meets existing international standards. This approach typically requires the parties to adhere to certain existing multilateral conventions on intellectual property.

A second approach, often seen in IIAs negotiated by the EFTA countries with transition economies and North African countries, includes a similar provision, but also provides for national and MFN treatment, subject to exemptions in accordance with the WTO TRIPS Agreement. Other agreements do not provide for any absolute standards

of protection of intellectual property rights, but do provide for national treatment or non-discrimination.

IIAs may also create their own substantive rules for the protection of intellectual property rights. For example, the 2004 Australia-United States Free Trade Agreement requires adherence to certain international conventions, but sets forth, in a series of articles in chapter 15, detailed protection that the parties are required to provide with respect to matters such as trademarks, geographical indications, domain names on the Internet, copyright, encrypted program-carrying satellite signals, and patents. IIAs that set their own substantive standards in some cases provide protection that go beyond the requirements of the WTO TRIPs Agreement. The significance of specific provisions on intellectual property protection is that they do protect intellectual property against private interference.

A few recent IIAs have also sought to exclude explicitly certain interferences with intellectual property rights from the definition of "expropriation". For example, article 10.13 of the 2003 Chile-Republic of Korea Free Trade Agreement provides that the expropriation article "…does not apply to the issuance of compulsory licenses granted in relation to intellectual property rights, or to the revocation, limitation or creation of intellectual property rights, to the extent that such issuance, revocation, limitation or creation is consistent with the TRIPS agreement."

Thus, even while IIAs are including increasingly elaborate provisions to protect intellectual property rights against private infringement, they are circumscribing slightly the protection against host country interference.

H. Competition

Numerous IIAs concluded by European countries include provisions that prohibit, or require the parties to prohibit, agreements or

concerted practices that may affect trade between the parties and that have as their object or effect the prevention, restriction or distortion of competition (UNCTAD 2004b). In the new generation of IIAs, extensive provisions on competition policy have also begun to appear in IIAs that do not involve a European country. For example, the Australia-Thailand Free Trade Agreement contains a separate chapter on competition policy, article 1202 of which provides that:

> "Each Party shall promote competition by addressing anti-competitive practices in its territory, and by adopting and enforcing such means or measures as it deems appropriate and effective to counter such practices."

Article 1201 defines "anti-competitive practices" to mean "business conduct or transactions that adversely affect competition" and offers as examples anti-competitive horizontal or vertical arrangements, misuse of market power, including predatory pricing, and anticompetitive mergers and acquisitions. Similarly, article 12.2 of the competition chapter of the 2004 Australia-United States Free Trade Agreement provides that:

> "Each Party shall maintain or adopt measures to proscribe anticompetitive business conduct and take appropriate action with respect thereto . . ."

The agreement requires each party to maintain an authority responsible for enforcing its national competition laws.

Competition provisions are unusual in certain respects. First, while most IIA provisions seek to insulate foreign investment from wrongful conduct on the part of the host country, competition provisions require the host country to impose restrictions on private parties to prevent injury to covered investment. Second, while most IIA provisions apply only to foreign investment, competition provisions by their terms apply equally to foreign and domestic investment. Where

the host country fails to restrict the anticompetitive behaviour of a foreign investment, however, an injured domestic investor generally would not have any remedy under the treaty and the investment's home country is unlikely to complain. Thus, despite its even-handed language, the provision may in practice actually favour foreign investors, because they could invoke the provision in case of an anti-competitive behaviour of domestic companies of the host country. In the case of an IIA with more than two parties, one of the parties other than the home or host country might object if the host country fails to restrict anticompetitive behavior by a foreign investment. This is one instance in which the practical application of the agreement may be different depending upon whether or not it is bilateral.

I. Transparency

Transparency provisions in IIAs traditionally require the host country to make certain kinds of existing information available. This type of transparency provision often appears in IIAs as a form of economic cooperation. It may impose a variety of specific obligations. One is to make public or at least available a party's laws and perhaps other information concerning investment (UNCTAD 2004c). Another is to provide the information to the other parties. For example, article 7 of the 2003 BIT between Japan and Viet Nam provides:

> "1. Each Contracting Party shall promptly publish, or otherwise make publicly available, its laws, regulations, administrative procedures and administrative rulings and judicial decisions of general application as well as international agreements which pertain to or affect investment activities.
>
> 2. Each Contracting Party shall, upon request by the other Contracting Party, promptly respond to specific questions and provide that other Contracting Party with information on matters set out in paragraph 1 above.

> 3. The provisions of paragraphs 1 and 2 of this Article shall not be construed so as to oblige either Contracting Party to disclose confidential information, the disclosure of which would impede law enforcement or otherwise be contrary to the public interest, or which would prejudice privacy or legitimate commercial interests."

Such provisions have become more common than in the past.

In the new generation of IIAs, however, there also has been an important change in the nature of transparency required by the treaties. More recent IIAs have begun to impose on the parties a general obligation of transparency in all their dealings with investment. This obligation may include a requirement that the host country allow investors to participate in domestic rule making procedures that affect their investments.

In some cases, the obligation is defined in relatively general terms. For example, article 39 of the EFTA Free Trade Agreement with Singapore states that:

> "Each Party shall, in accordance with the provisions of this Chapter, create and maintain stable, equitable, favourable and transparent conditions for investors of the other Parties to make investments in its territory."

Although at first glance this type of clause at first glance may seem weak because it does not impose a very specific obligation, it is potentially the most sweeping of the transparency provisions because it could apply to a wide variety of circumstances. This type of provision thus requires not simply making existing information available, but a certain mode of behaviour by the host country in dealing with covered investment. This provision, for example, might be cited by an investor as a basis for requesting an explanation of a government decision

affecting its investment or a right to participate in some way in government decision-making processes.

In other cases, the obligation explicitly includes a right to participate in decision-making. For example, the 2003 Free Trade Agreement between Singapore and the United States requires each party to ensure that in its administrative proceedings:

> "(a) wherever possible, persons of the other Party that are directly affected by a proceeding are provided reasonable notice, in accordance with domestic procedures, when a proceeding is initiated, including a description of the nature of the proceeding, a statement of the legal authority under which the proceeding is initiated, and a general description of any issues in controversy;
>
> (b) such persons are afforded a reasonable opportunity to present facts and arguments in support of their positions prior to any final administrative action, when time, the nature of the proceeding, and the public interest permit; and
>
> (c) its procedures are in accordance with domestic law."

The 2003 Singapore-United States Free Trade Agreement also requires each party to maintain systems that provide for appeals of administrative decisions regarding matters covered by the agreement, that the parties be given a reasonable opportunity to support their positions, and that the decision be based on the evidence and the submissions of those parties. By providing not only for notice of certain proceedings, but also an opportunity to be heard and a right to appeal, the Singapore-United States Free Trade Agreement stretches the concept of transparency to include elements of due process.

Increasing the scope of the transparency obligations in IIAs, however, has not always been accompanied by provisions that would

make those obligations enforceable through investor-State dispute resolution. For example, in the United States-Singapore FTA, some transparency obligations are set forth in a separate chapter and thus are not subject to the investor-State dispute resolution procedure, which is limited principally to disputes involving the investment chapter of the agreement.

J. Investor-State dispute settlement

Many IIAs include a provision authorizing arbitration of disputes involving the treaty between investors and host countries without the involvement of the investor's home country. Such provisions typically specify the mechanisms available to the investor for arbitrating the dispute (most often ICSID and/or UNCITRAL rules), describe the procedures for appointing arbitrators, and include provisions to ensure the finality and enforceability of awards (UNCTAD 2003a).

Investor-State dispute settlement is one of the key areas where significant developments in treaty making have taken place over the last decade. New generation IIAs have incorporated various innovative provisions intended to achieve four general objectives, described below.

1. Promotion of greater predictability and Contracting Parties' control over arbitral procedures

First, some of the innovations in investor-State arbitration provisions in IIAs are geared toward promoting greater predictability and control by the Contracting Parties over arbitral procedures. New generation IIAs have tended to go beyond ICSID and UNCITRAL rules, addressing in advance a series of specific matters related to the arbitral proceedings that are often left for agreement between the disputing parties on a case-by-case basis.

The most elaborate provisions for investor-State arbitration may be found in the NAFTA and in recent IIAs that follow the NAFTA model. These provisions address a number of issues on which other provisions found in IIAs are silent, such as the submission of the same dispute to local courts, the place of arbitration, appointment of experts, and remedies available, including interim measures.

This trend continued in recent IIAs, such as 2003 Chile-United States Free Trade Agreement and the 2004 Canadian model BIT, which have included specific provisions ensuring the involvement of the Contracting Parties in arbitration proceedings addressing certain specific subject matters, such as financial services, taxation measures or the interpretation of a non-conforming measure. These IIAs contain provisions that foresee the possibility of specialized competent authorities of the Contracting Parties to make interpretations of certain matters or provisions of the agreement, which will be binding on the arbitration tribunal. For example article 17 of the 2004 Canadian model BIT provides that where an investor submits a claim to arbitration related to financial services, and the disputing Contracting Party invokes as a defence the general exception based on prudential reasons included in articles 10(2) or 14(6) of the agreement, the arbitral tribunal

> "… shall, at the request of that Party, seek a report in writing from the Parties on the issue of whether and to what extent the said paragraphs are a valid defence to the claim of the investor. The tribunal may not proceed pending receipt of a report under this Article…the Parties shall proceed… to prepare a written report, either on the basis of agreement following consultations, or by means of an arbitral panel. The consultations shall be between the financial services authorities of the Parties. The report shall be transmitted to the Tribunal, and shall be binding on the Tribunal."

2. Promotion of judicial economy

Another set of innovations in investor-State arbitration provisions is geared toward promoting the principle of judicial economy in investment-related disputes.

One such provision is designed to deal with potential "frivolous claims" submitted by an investor. In this regard, article 10.19, paragraph 4, of the 2003 Free Trade Agreement between Chile and the United States provides that an arbitral tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favour of the claimant may be made. In deciding an objection under this procedure, the tribunal shall assume that the claimant's factual allegations in support of the claims are true and, if the respondent so requests, shall issue a decision or award on the objection on an expedited basis. Clearly, the objective of this expedited procedure is to avoid spending time and resources by arbitrating claims lacking a sound legal basis.

Other mechanisms fostering judicial economy that have been included in IIAs are those which prevent a particular investment dispute from being addressed in more than one forum, which would require the host country to respond to the same claims more than once and would raise the risk of inconsistent decisions. Of special concern is the possibility that the investor may submit a dispute to the domestic courts of the host country and to international arbitration. Two approaches have been used in IIAs to deal with this issue. Some agreements force the investor to decide, *ab initio*, whether the dispute shall be resolved in domestic tribunals or through international arbitration. According to this approach, once the dispute is submitted to either forum, the election shall be definitive. An example of this technique is illustrated by article IX.3 of the 1999 BIT between Indonesia and Chile, which provides that:

> "Once the investor has submitted the dispute to the competent tribunal of the Contracting Party in whose territory the investment was made or to international arbitration, that election shall be final."

Another approach used by some IIAs is to provide the investor with the possibility of choosing the venue to solve the quarrel at a later stage, even after the investor has submitted the dispute to the administrative or judicial tribunals of the host country. IIAs applying this technique allow the investor to opt for international arbitration even after domestic remedies have been sought, so long as such remedies are waived once arbitration is initiated. Article XIII.3 of the 1997 BIT between Canada and Thailand illustrates this approach, and provides that an investor may submit a dispute to arbitration only if:

> "… the investor has waived its right to initiate or continue any other proceedings in relation to the measure that is alleged to be in breach of this Agreement before the courts or tribunals of the Contracting Party concerned or in a dispute settlement procedure of any kind."

This approach also forecloses another situation in which the same dispute could be submitted to multiple fora, specifically, the case of an investor who first submits the dispute to arbitration and, depending on the outcome, then submits it to local courts.

Another way to reduce the number of claims arising out of the same dispute is to limit the number of parties who can file claims. For example, the 2003 Chile-Republic of Korea Free Trade Agreement provides that an investor, but not an investment, may submit a claim under the investor-State dispute resolution mechanism. This provision, however, does not entirely prevent the submission of the same dispute to multiple fora because an investment may have many investors, and not all of them may have the same nationality.

Another mechanism included in some IIAs to foster judicial economy – as well as to avoid inconsistent results – is a provision that allows the consolidation of separate claims that have a question of law or fact in common and arise out of the same events or circumstances. Most of the IIAs concluded by Mexico, as well as most free trade agreements negotiated by the United States, include provisions which authorize the formation of a special tribunal to assume jurisdiction over all or part of separate claims meeting the above-mentioned criteria.

3. Promotion of a consistent and sound jurisprudence on international investment law

As the number of arbitrations under IIAs has increased, some disputes have yielded awards that are inconsistent or adopt controversial interpretations of IIA provisions or of international law generally. Accordingly, some new generation IIAs have included provisions to foster a consistent and sound application of the substantive provisions of the IIAs.

One approach has been to include in the IIAs more detailed and clear provisions on several key substantive issues the interpretation of which has been controversial in arbitral proceedings. For example, the United States and Canada have recently modified the language of their IIAs to clarify the meaning of "fair and equitable treatment" and the concept of indirect expropriation.

Another approach has been to lay the groundwork for the creation of an appellate body or similar mechanism. For example, the 2003 Chile-United States Free Trade Agreement provides that within three years after entry into force of the agreement, the parties shall consider whether to establish a bilateral appellate body to review awards. The agreement also provides that, if the parties adhere to a multilateral agreement that establishes an appellate body to review awards by tribunals set up pursuant to an international trade or investment agreement, the parties shall strive to reach an agreement that

would permit that appellate body to review awards under the investor-State dispute resolution mechanism of the free trade agreement. The 2003 Free Trade Agreement concluded by the Central American States, the United States and the Dominican Republic (CAFTA) provides for establishment of a negotiating group to draft an amendment to the agreement authorizing an appellate body within one year of the formation of the group.

4. Promotion of transparency of investor-State dispute resolution

Some provisions included in new generation IIAs are geared toward promoting the transparency of investor-State arbitrations. For example, Article 10.20 of the 2003 Chile-United States Free Trade Agreement requires the respondent to transmit to the home country and to make available to the public certain documents, including the notice of arbitration, the memorials, the transcripts of hearings, and the awards of the tribunal. This article also requires that the hearings be open to the public, though provisions are made for the protection of confidential business information. It does not require the parties to make public any settlement discussions, nor does it interfere with the confidentiality of the tribunal's deliberations. Further, it authorizes the tribunal to consider *amicus curiae* submissions from any source, not merely the parties to the dispute or the parties to the agreement.

Transparency provisions serve important goals, but may also increase the burden on the parties to the dispute and circumscribe their discretion. For example, parties may feel the need to submit additional materials responding to arguments made in the *amicus curiae* briefs. Public knowledge of the disputes may result in public pressure on the parties to settle or to refuse to settle certain disputes.

Notes

[1] The European Community concluded Euro-Mediterranean Association Agreements with Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, the Palestinian Liberation Organization and Tunisia. Negotiations with Syria are now formally completed.

[2] This narrower language is of special significance in light of the much discussed recent arbitral decision in *Emilio Agustin Maffezini v. Kingdom of Spain*. In that case, the claimant submitted a claim against Spain to arbitration under the BIT between Spain and Argentina, which required that any investment dispute be submitted to local courts before being submitted to arbitration, something that the claimant admitted he had not done. The tribunal accepted his argument that he need not submit the dispute to local courts because Spain's BIT with Chile did not require submission of a dispute to local courts and the MFN clause of the BIT between Spain and Argentina entitled him similarly to submit a claim to arbitration without invoking local remedies first. The case made clear that an MFN clause can apply to procedural as well as substantive rights, a result that some states do not favour. The language quoted above from the 2002 BIT between the Russian Federation and Thailand would seem to avoid the result in the *Maffezini* case.

III. INTERACTIONS AND COHERENCE

Maintaining the coherence of a country's economic development policy could be complicated by the conclusion of a network of IIAs containing a variety of provisions applicable to the same matters. These provisions may be within the same IIA or in different agreements. This section surveys some of the issues that arise as countries seek to ensure policy coherence in the face of a complex network of overlapping IIA provisions.

In general, provisions of IIAs may interact in any of at least five different ways. First, they may interact in such a way as to create and define a particular right or duty, an "explication" interaction. Second, separate IIA provisions may create or enforce the same right or duty, a "reinforcement" interaction. Third, they may create different rights or duties applicable to the same subject matter, a "cumulation" interaction. Fourth, one provision may limit, diminish or extinguish the rights or duties created by another provision, a "contradiction" interaction. Finally, one provision may enlarge the impact of a right or duty created by another provision, an "amplification" interaction.

These interactions may undermine policy coherence. Policy coherence in general requires that provisions of a country's IIAs be consistent with the country's investment policy. In particular, the IIAs should not be significantly overinclusive (meaning that that they go farther than the underlying policy requires) or significantly underinclusive (meaning that they do not go as far as the underlying policy requires). Policy coherence also requires that a country's IIAs be consistent with each other. Not only should it be possible for a party to comply with all applicable IIA provisions, but compliance with one IIA provision should not impair furtherance of the policy underlying another IIA provision.

Because of the potential for IIA provisions to undermine policy coherence, IIAs have adopted a number of solutions intended to maintain it in the face of overlapping IIA provisions. At least five different solutions can be identified in existing agreements. The "definition" solution defines the terms of a provision in such a way to

eliminate any inconsistency with another provision. The “scope” solution limits the scope of a provision so as to avoid inconsistency with another provision. The “hierarchy” solution specifies which provision shall prevail in the event of an inconsistency. The “election” solution allows a specified actor to choose which provision shall prevail in the event of an inconsistency. Finally, the “agreement” solution specifies that any inconsistency shall be resolved by agreement of the parties.

The following discussion describes some of the most common interactions in existing IIAs, and identifies examples of solutions that have been employed to maintain policy coherence.

A. Interactions among provisions within IIAs

The most common interaction among provisions within an IIA is the explication interaction. In any IIA, the definitions provisions, exceptions provisions, substantive provisions, and dispute resolution provisions all interact in ways to establish the overall impact of the agreement. For example, the expropriation provision found in many IIAs requires payment of compensation for the expropriation of investment, but the nature of the assets protected by this provision typically can be identified only with reference to the definition of the term “investment.” The greatest challenge to policy coherence presented by this interaction may arise from the complexity of the agreement. The larger the number of provisions involved in the interaction, the greater the likelihood that the negotiators will not be able to anticipate all the consequences of the interaction.

An increasingly common interaction in new generation IIAs, as they become more comprehensive, is the cumulation interaction. One situation where the potential for inconsistency is clear in such an interaction may be found in agreements that have a chapter on investment and a separate chapter on trade in services. As has been noted, investment chapters sometimes have provisions on establishment

utilizing a negative list approach, while services chapters sometimes have provisions on market access utilizing a positive list approach. Another situation occurs in agreements that have a chapter on trade in services generally and additional chapters on trade in certain service sectors, such as financial services.

Existing agreements have addressed the potential for inconsistency in such interactions in at least three ways, all of which are exemplified by NAFTA. First, they have utilized definition solutions. For example, NAFTA article 1213 provides that the term "cross-border trade in services" does not include the provision of services by an investment. Thus, an investment of one party that provides services in the territory of another party is covered by the investment chapter, not the services chapter. Second, they have utilized scope solutions. For example, NAFTA article 1101(3) provides that "[t]his Chapter [on investment] does not apply to measures adopted or maintained by a Party to the extent that they are covered by Chapter Fourteen (Financial Services)." Thus, the scope of the investment chapter was narrowed to exclude matters covered by the financial services chapter. Third, they have utilized hierarchy solutions. For example, NAFTA article 1112(1) provides that "[i]n the event of any inconsistency between this Chapter [on investment] and another Chapter, the other Chapter shall prevail to the extent of any inconsistency." Thus, the investment chapter is subordinated to another chapter if there is an inconsistency with that other chapter.

A cumulation interaction may occur not only with respect to substantive provisions in the same agreement, but with respect to dispute resolution provisions as well. For example, some IIAs include an investment chapter with an investor-State resolution mechanism that is cumulative to the more general dispute resolution mechanism in the agreement. The issue may arise as to whether disputes concerning other chapters of the agreement may be brought under the investor-State dispute resolution mechanism. Some IIAs use a scope solution to specify that the investor-State resolution mechanism applies only to

disputes involving alleged breaches of specified provisions of the agreement. For example, article 10.15.3 of the 2003 Chile-United States Free Trade Agreement states that:

> "… no claim may be submitted under this Section [relating to the Investor-State dispute resolution mechanism] that alleges a violation of any provision of this Agreement other than an obligation under Section A [of the Investment Chapter] or Annex 10-F."

Provisions of an IIA sometimes amplify the impact of other provisions within the same IIA. For example, a host country that concludes an IIA with a chapter on trade in services may commit itself to granting market access to service providers in a particular sector of the economy. Once a service provider has established a commercial presence in the host country in accordance with the market access commitment, the commercial presence may also be considered an investment within the meaning of the investment chapter and, therefore, entitled to all of the protections afforded to investment generally. The solutions used to prevent undesired amplification interactions are essentially the same definition, scope and hierarchy solutions as those used to prevent inconsistency in cumulation interactions. Countries negotiating an IIA must be careful to consider the combined effect of different provisions. The effect of implementing one provision may be to trigger the application of other provisions, perhaps in other chapters of the agreement.

B. Interactions with other IIAs

1. Reinforcement interactions

Provisions of different IIAs often have reinforcement interactions. Several approaches may be found in existing agreements.

First, IIAs sometimes require the parties to conclude another agreement. For example, some intellectual property provisions require the parties to accede to certain multilateral intellectual property agreements. Here, the threat to policy coherence is minimal because, once the parties have acceeded, the provision in the first agreement largely ceases to have any practical significance.

Second, IIAs sometimes include provisions in which the parties reaffirm commitments under other treaties to which they are already parties. This occurs, for example, in services-related provisions in which parties reaffirm their commitments under the GATS. Similarly, Article 12(1) of the Framework Agreement on the ASEAN Investment Area provides that the member countries affirm their existing rights and obligations under the 1987 ASEAN Agreement for the Promotion and Protection of Investments and its 1996 Protocol. In this type of provision, the potential threat to policy coherence depends upon the extent to which a violation of the first agreement in time is considered a violation of the agreement that reaffirmed it. If so, then the violation may give rise to multiple dispute resolution proceedings, which, as discussed below, may result in incoherence.

Third, IIAs sometimes require the parties to observe obligations under another agreement. Examples include various IIAs requiring the parties to abide by the TRIMs agreement. The effect of such a provision in an IIA could well make a violation of the other agreement a violation of the IIA. This, in turn, could permit submission of a dispute involving an alleged violation of the other agreement to the dispute resolution mechanism of the IIA, again leading to the possibility of parallel dispute resolution proceedings.

Fourth, IIAs may incorporate obligations under other agreements. For example, article 35 of the EFTA Free Trade Agreement with Singapore provides that "Articles XI and XII of the GATS shall apply to payments and transfers, and to restrictions to safeguard the balance-of-payments relating to trade in services." The

incorporation may also be quite broad, going beyond a few specific provisions. The 1999 Free Trade Agreement between the Central American countries and Chile incorporated five BITs already concluded between Chile and individual Central American countries. Again, the clearest threat to policy coherence lies in the possibility of multiple dispute resolution proceedings.

One very common provision in IIAs that can serve, in effect, to incorporate the provisions of numerous other treaties is the MFN clause, requiring the host country to provide covered investment with treatment no less favorable than that provided to any other foreign investment. Depending on how the MFN clause is drafted, the host country may be obligated under the IIA to honor with respect to covered investments commitments made with respect to foreign investment in any other agreements.

In some respects, the incorporation under an MFN clause may be slightly narrower than incorporation under a more explicit incorporation provision, such as that discussed above. First, MFN clauses often require not identical treatment, but treatment “no less favourable” than that provided to another investment, thus allowing the host country to offer different treatment as long as it is not less favorable. Second, MFN clauses apply – expressly or tacitly – only to investments “in like situations,” allowing the host country to disregard the commitments made under another IIA if the covered investment is in a situation unlike that of investments covered by the other IIA.

In other respects, however, the incorporation under an MFN clause is far broader than that under any other reinforcement interaction. An MFN clause incorporates not merely the obligations under a specified other IIA, but those under every other investment-related agreement that a party has concluded. It also incorporates obligations under agreements that a party concludes in the future. Commitments made under other agreements, of course, are made as part of an overall balance of obligations assumed and concessions

granted. An MFN clause, however, incorporates the party's commitments under other agreements unaccompanied by the concessions for which those commitments were exchanged. The risk is that commitments incorporated outside the context in which they were originally made may result in over-inclusiveness.

To address this problem, existing IIAs utilize a number of scope solutions to limit the reach of the MFN clause. One approach is to draft the MFN clause narrowly. For example, the 2002 BIT between the Russian Federation and Thailand guarantees MFN treatment to investors "as regards their management, maintenance, use, enjoyment or disposal of their investments." Thus, for example, dispute resolution procedures created by another IIA presumably would not be incorporated into the BIT by virtue of this MFN clause as long as they do not relate to the management, maintenance, use, enjoyment or disposal of investments. A second solution is to include an annex to the IIA in which the parties may list sectors or matters to which the MFN standard does not apply. The current model BITs used by Canada and the United States categorically exclude all government procurement and government subsidies and grants from the MFN obligation. A third solution is to exclude certain agreements from the application of the MFN provision. For example, Annex III of the current Canadian model BIT provides that the MFN standard "shall not apply to treatment accorded under all bilateral or multilateral international agreements in force or signed prior to the date of entry into force of this Agreement."

Reinforcement interactions may exist with respect to procedural provisions as well. Thus, IIAs sometimes rely upon institutional arrangements created by other agreements. For example, the ASEAN agreements on investment and services provide that the ASEAN dispute settlement mechanism, created under a separate agreement, shall be utilized to resolve disputes arising under those agreements.

2. Cumulation interactions

Cumulation interactions between provisions of different IIAs are very common For example, most IIAs apply to investments that are means of providing cross-border services and such investments would also be governed by the GATS, to the extent that the investments could be described as constituting a commercial presence in the host country.

Again, several solutions have been employed to avoid inconsistency between cumulative provisions in different IIAs. First, some IIAs use a hierarchy solution to specify which agreement prevails. One approach is for an agreement to provide that it is subordinate to other agreements. For example, article IX(1) of the ASEAN Framework Agreement on Services provides that "[t]his Framework Agreement or any action taken under it shall not affect the rights and obligations of the Member States under any existing agreement to which they are parties." An IIA, however, may also assert that it prevails over any other agreement. For example, article 91 of the Partnership Agreement between the African, Caribbean and Pacific States and the European Community states that "[n]o treaty, convention, agreement or arrangement of any kind between one or more Member States of the Community and one or more ACP states may impede the implementation of this Agreement."

Second, some IIAs use an election solution under which the investor may choose which provision shall prevail. For example, article 2 of chapter 8 of the Singapore-Australia Free Trade Agreement provides that a natural person who is covered by another investment agreement may invoke the free trade agreement only if he or she has not invoked the protection of the other agreement. Third, some IIAs use an agreement solution, under which the parties shall resolve any inconsistency later. For example, article 5 of chapter 17 of the Singapore-Australia Free Trade Agreement provides that "[i]n the event of any inconsistencies between this Agreement and any other

agreement to which both Parties are party, the Parties shall immediately consult with each other with a view to finding a mutually satisfactory solution in accordance with customary rules of public international law."

Cumulation interactions between different IIAs can also involve procedural provisions. This is particularly true where services provisions in an IIA create obligations similar to those under the GATS and that may therefore give rise to disputes that could fall within the WTO dispute resolution mechanism and the IIA dispute resolution mechanism. Similarly, investor-to-State dispute resolution mechanisms in IIAs could potentially be invoked to enforce provisions of other agreements, as long as those disputes relate to covered investment.

Whether they involve provisions of the same agreement or of different agreements, multiple dispute resolution proceedings can greatly threaten policy coherence. First and foremost, they can produce interpretations of the agreements that are inconsistent. Even where the results are consistent, redundant resolutions of the same claim would cause unnecessary expenditures.

Again, hierarchy, election and agreement solutions have been utilized to maintain policy coherence. For example, article 56 of the free trade agreement between EFTA and Singapore uses an election solution that gives the complaining party the choice of forum. It provides that "[d]isputes on the same matter arising under both this Agreement and the WTO Agreement, or any agreement negotiated thereunder, to which the Parties are party, may be settled in either forum at the discretion of the complaining party. The forum selected shall be used to the exclusion of the other." A solution involving both hierarchy and agreement is that in article 17(4)(c) of the free trade agreement between the United States and Jordan, which provides that "[e]xcept as otherwise agreed by the Parties, a Party may invoke a panel under paragraph 1(c) of this Article for claims arising under Article 4 only to the extent that the claim would not be subject to

resolution through the WTO Understanding on Rules and Procedures Governing the Settlement of Disputes." That is, WTO procedures must be followed, unless the parties agree otherwise.

3. Contradiction interactions

Occasionally, provisions of different IIAs are in a contradiction interaction. The Vienna Convention on the Law of Treaties addresses the situation where provisions of different agreements are inconsistent. In general, that convention provides that the later agreement prevails as among the parties to both agreements. Where the two agreements are not among the same parties, the earlier agreement prevails among those who are party only to the earlier agreement. The Vienna Convention also provides that these rules may be modified by agreement of the parties. And, as has been noted already, in some cases, IIAs do include provisions specifying which agreement shall prevail in the event of an inconsistency.

In some cases, an IIA explicitly provides for termination of a prior, potentially inconsistent agreement. For example, article 21.4 of the 2003 Free Trade Agreement between Chile and the Republic of Korea provides that upon entry into force of the Free Trade Agreement, the BIT between the two parties shall no longer be in effect.

C. Interactions with State contracts

Interactions also occur between the provisions of an IIA and the provisions of a contract between the host country and the investor, such as an investment authorization. In some cases, the interaction is a reinforcement interaction. This occurs, for example, where the IIA has a so-called "umbrella clause," which requires the host country to observe obligations into which it has entered with respect to an investment. Under this clause, a violation of the State contract also violates the IIA. If the State contract includes a choice of forum clause specifying that disputes shall be resolved in a particular form, the

investor may seek to submit the dispute both to that forum and to any forum provided by the IIA, such as an investor-State dispute resolution mechanism. Some IIAs include provisions that seek to avoid multiple dispute resolution proceedings in that situation, such as by requiring that the State contract dispute resolution mechanism be invoked first (in the hope that the dispute will be resolved in that forum) or, alternatively, by providing the investor with the choice of mechanisms, but specifying that the choice is irreversible.

Provisions of IIAs sometimes risk to have contradiction interactions with provisions of State contracts. For example, IIA prohibitions on performance requirements may limit the host country's ability to include certain requirements in a State contract. Similarly, IIA provisions on non-discrimination may limit the ability of the host country to guarantee preferential treatment to a particular investor in a State contract.

To prevent a party from claiming a contradiction where none was intended, some IIAs include non-derogation clauses, stating that the provisions of the IIA shall not derogate from State contracts providing for a higher level of protection. Such provisions add nothing to the State contract, but they make clear that the IIA takes nothing away from the State contract either.

IV. IMPLICATIONS

A. General implications

The number of IIAs has grown enormously since 1990. This development has resulted in an increasingly complicated framework of multi-layered and multi-faceted investment rules. On the one hand, this system of international investment rules contributes to the predictability, transparency and stability of international investment relations, which forms a crucial ingredient to the enabling framework for attracting FDI, and benefiting from it. On the other hand, the current approaches at the bilateral and regional level increase the complexity of the international investment rule system, resulting in the risk of overlapping and inconsistent obligations.

This raises a number of implications that need to be addressed in the process of future international investment rule setting.

- First, the complexity of negotiations increases as more and more countries, and more and more issues, are involved. This raises questions of how broad the agenda of any particular set of negotiations should be, and how ambitious parties want to be concerning the nature of commitments.

- Second, the negotiation of IIAs includes interrelated, difficult policy issues that at least in principle touch upon a whole range of domestic concerns, comprising, increasingly, social and environmental matters. Indeed, such agreements reflect the growing internationalization of the domestic policy agenda. Failure to take related issues of national policy properly into consideration may have serious development implications for the host countries. Therefore, IIAs should reflect a certain balance between rights and responsibilities – either by including them within the same instrument or by establishing bridges with other binding and non-binding international instruments.

- Third, while IIAs by definition contain obligations that, by their very nature, limit to some extent the autonomy of contracting

parties, the need for a certain degree of flexibility to allow countries to pursue their development objectives in light of their specific needs and circumstances should be addressed. The more investment agreements go beyond protection issues and in particular attempt to include commitments to liberalize, the more complicated their negotiation becomes. Where liberalization is sought, progressive liberalization of investment regulations may be more acceptable than up-front and all-embracing commitments to liberalize.

- Fourth, transparency in the conduct of IIA negotiations plays a key role in securing the necessary support and legitimacy for them. The awareness, understanding and input of all development stakeholders are important.

B. Challenges for developing countries

While the above issues are important to all countries at whatever level of development, developed, developing and transitional alike, they are more pertinent for developing countries that have less capacity to deal with them. In particular, developing countries are faced with four main challenges in this regard:

- First, developing countries need to ascertain how best to integrate these agreements into their economic development policy. IIAs are intended to promote economic development by providing a stable, predictable and transparent environment for foreign investment. Yet, all international agreements circumscribe the discretion of the parties. Developing countries need to retain sufficient policy space to promote economic development, without undermining the effectiveness of the IIA.

- Second, developing countries need to establish and maintain policy coherence in the face of a large number of interacting IIAs. As an initial matter, this entails creating a coherent

national development approach that integrates investment, trade, competition, technology and industrial policies. As new IIAs are negotiated, each should be reviewed carefully to ensure that it is consistent with and, in fact, promotes the state's economic development. Establishing and maintaining policy coherence has become more challenging for developing countries in recent years because of at least two factors. One factor is that many developing countries are now both capital importing and capital exporting economies. Thus, an IIA may have implications for a developing country as both host and home state. The other factor is the sheer number and complexity of the agreements.

- Third, developing countries need to ensure that they have sufficient capacity to analyze the scope of obligations into which they are entering when they conclude an IIA. They also need to improve their capacities to understand the economic and social implications of the commitments contained in IIAs.

- Fourth, developing countries need to implement the treaty commitments they have assumed. Implementation entails completing the ratification process, bringing national laws and practices into conformity with treaty commitments, informing and training local authorities that actually have to apply the IIA, managing the disputes that arise under IIAs, and re-evaluating national investment policies in light of national development strategies and past experience.

Finding a development-oriented balance in future IIAs that adequately addresses these issues remains a challenge. In the pursuit of the development dimension of IIAs, more attention also needs to be paid to commitments by home countries and to the contributions TNCs can make to advance the development impact of their investment in developing countries (UNCTAD 2005g, 2001b and 2001g). As already noted, the burden of addressing these challenges is likely to weigh

disproportionately on developing countries, especially the least developed, because they often lack the human and financial resources to implement agreements. This underlines the importance of capacity-building technical cooperation to help developing countries in assessing various policy options before entering into new agreements and to assist them in implementing the commitments made. International organizations can play a role in this regard.

* * *

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