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**INVESTMENT PROVISIONS  
IN  
ECONOMIC INTEGRATION  
AGREEMENTS**



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## NOTE

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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. The programme seeks to help developing countries to participate as effectively as possible in international investment rule-making. It embraces research and policy analysis, including the preparation of a series of policy issues papers; human resources capacity-building and institution-building, including national seminars, regional symposia and training courses; and support to intergovernmental consensus-building. The programme is implemented by a team lead by James Zhan. The members of the team include Amare Bekele, Hamed El-Kady, Severine Excoffier-El Botout, Anna Joubin-Bret, Joachim Karl, Josephine Lamptey, Anca Radu, Marie-Estelle Rey and Jörg Weber. Khalil Hamdani provides overall guidance. The study entitled *Investment Provisions in Economic Integration Agreements* is part of the programme's research and policy analysis on international investment rules.

Besides bilateral investment treaties (BITs), international investment rules are increasingly being adopted as part of bilateral, regional, interregional and plurilateral agreements that address and seek to facilitate inter alia trade and investment, referred to in this study as “economic integration investment agreements” (EIAs). The number of EIAs has been growing steadily since the early 1990s, reaching 218 by June 2005. In 2004 and early 2005 alone, at least 32 EIAs were concluded, and 66 others were under negotiation or consultation, thus promising further expansion. Recent EIAs tend to address an expansive set of investment issues in provisions that are increasingly elaborate.

Given the growing significance of EIAs for international investment rule-making, this study takes stock of these agreements, their incidence and geographical distribution, as well as their main characteristics related to their investment provisions. It is intended to serve as a comprehensive reference volume to help negotiators, policymakers, business executives, academics and other interested groups dealing with these treaties, and, in particular, to contribute to a better understanding of the issues involved in their negotiation, conclusion and application.

The study was prepared by Kenneth Vandavelde, Victoria Aranda and Hamed El-Kady. Comments were provided by Roberto Echanty, Anna Joubin-Bret, Mark Kantor, Joachim Karl, Samuel Laird, Padma Mallampally, Peter Muchlinski, Marie-Estelle Rey and Jörg Weber. Desktop publishing was done by Teresita Ventura.

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## 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 West African States
ECA	economic cooperation agreement
ECCAS	Economic Community of Central African States
ECGL	Economic Community of the Great Lakes Countries
EPA	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

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# I. INTRODUCTION

## A. Background and Scope of the Study

International investment rules are increasingly being adopted as part of agreements that address *inter alia* trade and investment. The large majority of these agreements belong to a category of agreements that, under different names, seek to facilitate international trade and cross-border movements of the factors of production, generally referred to in this study as “economic integration agreements” (EIAs).<sup>1</sup> The recent expansion of EIAs covering a variable range of economic transactions has been identified in the literature as a major new phenomenon with potentially profound implications for international economic relations.<sup>2</sup> An important characteristic of recent EIAs is that, while trade remains their principal component, they increasingly address an expansive set of investment issues. By June 2005, the number of EIAs dealing with investment (referred to as “economic integration investment agreements” (EIIAs) in this study) had reached 218. Most countries, both developed and developing, are signatories to one or more EIIAs, and new negotiating initiatives are under way, thus promising further expansion. Indeed, no country can escape today from the systemic effects of EIIAs, either as an active participant or as an outsider. From the perspective of international investment law, the proliferation of EIIAs is changing the configuration of the investment relations landscape worldwide and creating important new challenges for investment rule-making and implementation.

In spite of the growing importance of EIIAs, however, there is no comprehensive study that focuses specifically on the investment component of these agreements. This study seeks to fill the research and policy analysis gap in the specialized literature. Its purpose is to contribute to a better understanding of the changes that are taking place in the international normative framework on investment through EIIAs, surveying the latter’s growth and geographical expansion, analysing their approaches to investment issues, and examining the interactions between their provisions and those of other agreements. In this manner, it is hoped that the study will assist policymakers in making informed decisions regarding the negotiation and application of all types of international investment agreements (IIAs).

The scope of the study is confined to EIAs dealing with investment (EIIAs) concluded after 1945. Thus, for the purposes of the study, an EIIA means an EIA that deals with *inter alia* trade, and contains at least one provision directly setting out a specific commitment on investment.<sup>3</sup> The investment commitment or commitments in an EIIA may be narrow or extensive, and may address issues related to the promotion, protection, liberalization and/or

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<sup>1</sup> The term “economic integration agreement” has been used in, among other instruments, the WTO Agreement on Trade in Services (GATS) (Article V) in relation to agreements that cover trade in services, and also in the Energy Charter Treaty in relation to agreements that cover *inter alia* trade and investment. The definition of “economic integration agreement” in this study is broader than that used in the GATS, as it encompasses all sectors. It therefore includes also “preferential trade agreements” dealing with trade in goods, referred to in article XXIV of GATT. For seminal studies on the phenomenon of economic integration and related definitions, see, among others, Viner (1950), Balasa (1961) and Bhagwati and Panagariya (1996). For a comprehensive bibliography on issues related to economic integration see OECD (2001, pp. 133-144).

<sup>2</sup> See OECD (2001 and 2003) and World Bank (2005), among the recent studies that were prompted by the increasing importance of various types of EIAs in international economic relations.

<sup>3</sup> Some agreements that seek to facilitate trade and investment flows but do not aim specifically at economic integration have also been considered in this study, as have stand-alone investment agreements that are part of a broader economic integration scheme.

regulation of investment.<sup>4</sup> Moreover, the substantive analysis of these agreements is limited to their investment provisions. Provisions related to the movement of goods, services, people or information are not examined, except to the extent that they affect investment provisions directly. Two other categories of agreements are also excluded. The first is the category of multilateral EIAs, notably WTO agreements. These have been widely discussed in the literature and, in fact, some familiarity on the part of the reader with the GATS, the TRIPS and the TRIMS agreements is assumed in this study. Another category which is excluded from this study — and indeed falls outside the definition of an EIA — is that of the more than 2,400 bilateral investment treaties (BITs) that have been concluded since 1959. Although BITs have influenced the investment provisions of many EIAs, they have been analysed extensively elsewhere, notably in UNCTAD's study entitled *Bilateral Investment Treaties in the Mid-1990s* (UNCTAD, 1998a). Finally, the study examines the texts of the relevant treaties, but does not address the interpretation or application of the treaties through State practice or the decisions of arbitral tribunals.

The study is divided into six chapters. By way of introduction to the topic, the present chapter discusses briefly the nature of EIAs and the theoretical economic and policy rationales behind their adoption, distinguishing EIAs from other types of EIAs. Chapter II reviews the historical evolution of EIAs, describing briefly the main features of each agreement. In this overview the agreements are grouped by geographical regions and presented in chronological order, so as to highlight key developments from their origins to their present status. The purpose of this overview is to give the reader a comprehensive picture of the agreements included in the study, before proceeding to a more detailed comparative analysis of their features. Chapter III examines in detail the universe of EIAs, namely their numbers and geographical distribution, and identifies several patterns in EIAs in relation to the investment issues they address. Chapter IV discusses first broad differences and similarities between EIAs and with other investment agreements, and then looks in further detail at the main provisions on investment found in EIAs, explaining their meaning and policy implications. Chapter V examines the question of EIA interactions, both among investment-related provisions within individual agreements and between agreements. The role of these interactions in shaping the present framework of investment rules has become a particularly important issue in recent international discussions, especially in the light of the increasingly complex network of agreements that is emerging across countries and regions. Finally, the concluding chapter provides some insights regarding the challenges facing policymakers in relation to the adoption and implementation of EIAs.

## **B. EIAs: Nature, Types and Rationale**

As noted, economic integration agreements (EIAs) may be defined as agreements that facilitate international trade and cross-border movement of the factors of production. EIAs may address one, some or all these types of economic transactions in various combinations, with trade being the central component, and foreign investment activity one possible ingredient (in the latter case EIAs). They may cover transactions that take place between countries and they may also address activities that occur inside the borders of a country that may affect such international flows. EIAs may be established at the multilateral, regional, interregional, plurilateral or bilateral levels. The fundamental difference between multilateral EIAs and those at other levels is that the latter offer reciprocal (and sometimes non-reciprocal) treatment on a preferential basis to their

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<sup>4</sup> Agreements falling under the broad denomination of EIAs are given different names, including, for example, free trade agreements, free trade and investment agreements, preferential trade agreements, regional integration agreements, partnership and cooperation agreements, association agreements, economic partnership agreements, and framework agreements on trade and investment relations. For the sake of convenience, in this study all of these agreements are referred to as economic integration investment agreements (or EIAs).

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member countries. Thus, the adoption of a non-multilateral EIA creates two levels of rules: one level of rules that apply to the countries that are members of the group, and another level of rules, typically less favourable than the first, applying to non-members. Such preferential EIAs are concluded by two or more countries in an effort to expand and deepen their economic relations in a limited and flexible setting. This allows them to move beyond the minimum common denominator established by the existing multilateral system and undertake new and complex policy initiatives that are difficult to broach at the multilateral level. (Given that multilateral EIAs are not addressed in this study, unless otherwise stated, throughout the study the term “EIA” or “EIIA” means non-multilateral EIA or EIIA.). The depth of market and economic integration sought by an EIA, in terms of the types of the restrictions or obstacles it tries to remove and the range of activities it covers, can vary considerably among agreements. Several different types of EIA models have been identified, although there may be numerous variations of each. An example of a typology of agreements in relation to the depth of market integration they seek is described in box I.1.

**Box I.1. Types of agreements in relation to the depth of market integration they seek**

- **Sectoral trade agreements.** They provide for lower tariffs or duty free treatment among their members on a limited number of sectors.
- **Non-reciprocal preferential trade agreements.** They grant access to a larger market without a demand for reciprocity.
- **Free trade agreements.** Member countries eliminate substantially all tariff and non-tariff barriers between themselves.
- **Customs unions.** Member countries eliminate substantially all tariff and non-tariff barriers among themselves and establish a common external tariff for goods from third countries.
- **Common markets.** A custom union is supplemented by the removal of barriers to factor movement.
- **Economic unions.** The members integrate all or most of their economic policies.

Source: Amponsah (2001).

As this typology suggests, in theory the evolution from shallow to deep integration may be described as proceeding through various stages (UNCTAD, 1993, ch. VII, pp.160-164). The reduction or elimination of tariffs and other border barriers to trade in goods among EIA country members remains the central component of any process of economic integration and, hence, of many EIAs. This approach alone, however, represents a limited and “shallow” type of integration. The simple removal of border barriers to trade in goods, while other internal barriers remain in place, might not be sufficient to provide greater access to the markets of one country even for some goods of another country. To take account of this, an EIA may incorporate more complex measures aimed at reducing internal barriers to imports, measures such as harmonization of product standards among its members. However, if an EIA leaves external trade policy to the discretion of individual member countries, third country imports into the area are likely to be redirected to exploit the tariff differences among EIA members. To avoid this problem, countries may decide to integrate further by creating a common external trade policy or customs union. The transition from a free trade area to a customs union involves a deeper level of policy commitment and institution building. Even then, the integration of goods markets, while other aspects of cross-border economic integration are left outside the scope of an EIA, may frustrate the objectives of such integration. One major aspect is that of international transactions in services, which are an important part of most economies today. Another is that of investment by which firms extend their production activities beyond national borders, seeking markets or access to resources and created assets. The inclusion of these (and other) aspects in EIAs may help to better achieve the objectives of integrating markets and economies.

In practice, however, the passage from a limited and shallow model to broader and deeper levels of integration as described above is not necessarily reflected in the design of existing EIAs. Rather, the picture that emerges from EIAs, old and new, in terms of the extent and depth of their coverage of specific types of transactions, is rather mixed. Thus, for example, some EIAs that seek to eliminate internal tariffs and non-tariff barriers, but do not contemplate reaching the stage of a customs union, nevertheless contain comprehensive rules on investment (table I.1).

**Table I.1. EIAs do not follow a clear integration pattern**

Agreement	Trade in goods	C.E.T*	Standards**	Trade in services	Investment	Labour
United States - Central American Free Trade Agreement (CAFTA) (2004)	Yes	No	Yes	Yes	Yes	Yes
Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) (2004)	Yes	No	Yes	Yes	Yes	No
South Asian Free Trade Area (SAARC) (2004)	Yes	No	No <sup>a/</sup>	No	No <sup>a</sup>	No
European Community (EC) - Mediterranean partners (1995-2004)	Yes	No	No	Yes	Yes	No
United States-Singapore (2003)	Yes	No	Yes	Yes	Yes	Yes
Chile-Republic of Korea (2003)	Yes	No	Yes	Yes	Yes	Yes
Economic Cooperation Organization Trade Agreement (ECO) <sup>1</sup> (2003)	Yes	No	No	No	No <sup>b</sup>	No
European Community (EC) - Mexico (2001)	Yes	No	Yes	Yes	Yes	No
United States-Jordan (2000)	Yes	No	No	Yes	Yes	Yes
European Community (EC) - South Africa (1999)	Yes	No	No	No	Yes	No
Chile-Canada (1996)	Yes	No	No	Yes	Yes	Yes
North American Free Trade Agreement (NAFTA) (1994)	Yes	No	Yes	Yes	Yes	Yes
European Community (EC) - Russian Federation (1994)	Yes	No	Yes	Yes	Yes	Yes
The Southern Common Market (MERCOSUR) (1994)	Yes	Yes	Yes	Yes	Yes	Yes
Commonwealth of Independent States Free Trade Agreement (CIS) <sup>2</sup> (1994)	Yes	Yes <sup>c</sup>	Yes	Yes	No	No
Common Market for Eastern and Southern Africa (COMESA) (1993)	Yes	Yes	Yes	Yes	Yes	Yes
European Free Trade Association (EFTA) -Turkey (1991)	Yes	No	Yes	No	No	No
South Pacific Forum Cooperation Agreement (1980)	Yes	No	No	No	No	No
Southern African Customs Union (SACU) (1969)	Yes	Yes	Yes	No	No	No
Andean Community (1969)	Yes	Yes	Yes	Yes	Yes	Yes
Treaty Establishing the European Community (1957)	Yes	Yes	Yes	Yes	Yes	Yes

Source: UNCTAD.

\* CET: Common external tariff.

\*\* Product standard regulation.

<sup>a</sup> The parties agree to consider the adoption of additional measures aimed at, inter alia, the harmonization of standards and the removal of barriers to intra-SAARC investment.

<sup>b</sup> The agreement deals with the protection of intellectual property rights.

<sup>c</sup> The free trade area is considered a transitional stage in the formation of a customs union.

<sup>1</sup> Members of ECO are: Afghanistan, Azerbaijan, the Islamic Republic of Iran, Kazakhstan, Kyrgyzstan, Pakistan, Tajikistan, Turkey, Turkmenistan and Uzbekistan.

<sup>2</sup> Members of the CIS Trade Agreement are: Azerbaijan, Armenia, Belarus, Georgia, Kazakhstan, the Republic of Moldova, the Russian Federation, Ukraine, Uzbekistan, Tajikistan and Kyrgyzstan.

Each increasingly deeper integration stage entails potential economic and policy gains as well as costs for the countries involved. A comprehensive assessment of the economic and policy implications of the integration stages reflected in different types of EIAs, and in particular in EIIAs, would require a thorough empirical analysis of all the elements at work, which is beyond the scope and purpose of this study. A number of recent studies have looked in detail at these issues<sup>5</sup> and, while there is no consensus in the literature as to the economic and policy benefits and costs of these agreements, there is wide recognition of the theoretical rationales behind the adoption of EIAs, including EIIAs. In terms of the economic rationale, the formation of economically-integrated areas is a natural step in the process of geographical expansion of markets from local to national to international, which is driven by efficiency considerations, as larger markets “allow gains from specialization (division of labour), differences in resource endowments, and from economies of scale in manufacturing and technology” (Kobrin, 1995, p. 21). The removal of barriers to international trade in goods is a major step towards obtaining the economic gains mentioned above. But the removal of barriers to other types of international transactions, including services transactions and investment, expands the extent and range of such benefits.

In the case of trade in services, the economic rationale for their inclusion under an EIA's coherent liberalization and regulatory processes is explained, to a significant extent, by the complex nature of services and their strategic importance for national economies. Many services are inputs to other economic activities and, consequently, their orderly functioning can have a significant effect on the entire economy. Moreover, undertaking cross-border trade in services often requires the establishment of a facility in the country whose market is being supplied. This adds a foreign-direct-investment dimension to many international services transactions that further increases their complexity. These characteristics of services have traditionally justified the existence of more formal and informal barriers to market access by service enterprises — and the establishment locally of production facilities by foreign firms in particular — than probably in any other economic sector. The efficient reduction and monitoring of such barriers may be seen as a necessary step when moving to a “deep” level of economic integration. However, this is also a difficult and sensitive policy task that can be facilitated if it is carried out through the concerted intergovernmental efforts of an EIA.

The economic rationale for dealing with investment in EIAs, and hence for EIIAs, is also compelling. Foreign direct investment has become an important mode of delivering goods and services to foreign markets,<sup>6</sup> and integrated international production systems through foreign investment have become an increasingly important means for firms to improve their efficiency.<sup>7</sup> Indeed, one of the economic effects expected — and to some extent realized (UNCTAD, 1998b, ch. IV) — from EIAs dealing with trade is an increase in investment flows into and within the EIA area. This increase is driven by two main types of economic effects of EIAs on foreign direct investment.<sup>8</sup> The first effect is linked to the removal of trade barriers, which enlarges the

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<sup>5</sup> For recent discussions of the economic and policy implications of various types of EIAs, see for example World Bank (2005), Abugattas (2004), Sampson and Woolcock (2003), Okamoto (2003), Inter-American Development Bank (2002), OECD (2001) Gilbert, Scollay and Bora (2001), Laird (1999) and UNCTAD (1998).

<sup>6</sup> For example, in 2003, world sales of foreign affiliates were estimated to be nearly twice the value of world exports of goods and services (UNCTAD, 2004a, p.9).

<sup>7</sup> This discussion assumes a basic understanding of the potential benefits and costs of foreign direct investment in general, and integrated international production in particular, for host and home countries. Detailed analyses of the various effects of FDI and their implications for host and home countries can be found in the 14 volumes already published of the World Investment Report Series (1991-2005).

<sup>8</sup> For a more detailed discussion of the effects of EIAs on investment, see, for example, OECD (2001), Brewer and Young (2000, pp.167-170) and UNCTAD (1998a).

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market and allows firms to benefit from greater scale. This effect helps attract market-seeking production activities, from within and outside the EIA area, for which scale is an important consideration (OECD, 2001, p. 7; UNCTAD, 1998, ch. IV). The second effect of EIAs is linked to the facilitation of changes in the location of production within EIA member countries. Relocation is driven by comparative advantage and helps increase intra-EIA efficiency-seeking investment. Relocation is related to the adoption of investment rules that relax market entry restrictions and provide for legal protection. Thus, to ensure the combined efficiency effects of scale and comparative advantage, lowering tariffs alone is not sufficient, although it is a necessary precondition. Little can be gained, in fact, if the countries within an EIA area maintain substantial investment barriers between themselves. There is, therefore, an incentive for addressing investment facilitation issues in EIAs — resulting in EIAs — if countries seek a “deeper” level of economic integration (box.I.2).

On the other hand, EIAs can generate potential economic costs for individual member countries. In the case of EIAs between developed and developing countries, for example, the burden of services and investment liberalization is likely to fall asymmetrically on the less developed countries members of the EIA (Abugattas, 2004). In addition, different parties may stand to benefit asymmetrically from the efficiency-motivated relocation effects of an EIA. For example, while relocation effects can be an instrument of convergence of income levels among the countries members of an EIA, in certain circumstances, relocation of production can also be a cause of severe job losses for the countries with less competitive labour markets (OECD, 2001, p. 8). Job losses in a member country due to relocation can impose heavy economic and social costs on some sectors within the economy, while other sectors may expand, resulting in an unequal distribution of any gains from the EIA to the economy as a whole. The process of adjustment may be quite prolonged and there is no guarantee that those displaced in contracting sectors will easily be absorbed back into expanding activities, especially when there is large-scale unemployment, as in many developing countries. This suggests that, in order to fully capture the gains from EIAs, liberalization and integration efforts may need to be accompanied by policy measures — such as social safety nets and retraining programmes — that facilitate the adjustment process.

Certain well-recognized broader policy effects of EIAs may also act as important motivations or rationales for the conclusion of these agreements. Although these policy effects apply in principle to all types of EIAs, they would tend to be stronger as the level of integration deepens, for example when investment and services are made an integral part of an EIA, resulting in an EIA. One of the first important potential policy effects of EIAs relates to the locking-in effect in relation to national policy (World Bank, 2004; OECD, 2001). Thus, while countries can undertake unilateral liberalization of investment and trade in services, the lock-in effect of making investment and services liberalization commitments a part of an EIA adds credibility to these commitments. This in turn contributes to providing policy stability, transparency and reliability, which are the hallmarks of a favourable foreign investment climate. The investment-related provisions in EIAs signed by Central, Eastern and South-Eastern European countries during their transition towards market economies were mainly intended to achieve this effect. It may be argued in this respect that investment and services liberalization, protection or promotion can also be pursued in stand-alone investment agreements, independently from an EIA. However, the counter-argument in favour of the inclusion of investment provisions in an EIA addressing trade (or trade and other components) — or as part of separate agreements which are linked to the main EIA — is that this model contributes to policy coordination, coherence and an orderly process in the design and implementation of trade and investment policy, thus minimizing the cost of conflicting approaches.

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**Box I.2. Effects of EIAs on international production**

By addressing investment issues, an EIIA facilitates FDI flows between member countries with potential benefits for the countries involved.

It improves access to markets within the EIIA area for firms established in countries within the area that produce goods and services for which proximity between producers and customers — and hence local establishment of production facilities — is an advantage. In competitive markets, this can lead to increased competition, lower prices and/or improved quality of products for consumers in the host countries, as well as improved competitiveness of the firms involved.

Furthermore, an EIIA creates increased opportunities for firms operating in EIIA countries to establish or participate in the establishment of facilities for the exploitation of natural resources, and thereby obtain better access to such resources. This can lead to increased export-oriented extraction of natural-resource products (and related employment and income) in countries within the EIIA area endowed with such resources, improved conditions of supply of products, wherever they may be sold, and improved competitiveness of the firms involved.

An EIIA also increases opportunities for firms established in EIIA countries to engage in efficiency-oriented international production, dispersing their production activities within their integrated international production systems and fragmenting their activities more closely in accordance with the comparative advantages of different locations in the EIIA area (UNCTAD, 1996 p. 112). This can contribute to increased export-oriented production (and related employment and income) in the host countries in segments of goods and services production for which they have comparative advantage, improved conditions of supply of the final products based on them, wherever they may be sold, and improved competitiveness of the firms involved.

In a world with significant economic integration through trade, many of the potential benefits from EIAs arise from the strong interrelationship between FDI and trade as firms increasingly seek to locate their activities and functions wherever the latter contribute most to their efficiency. They also arise from the fact that in the services sector, where many products still have limited tradability and where proximity of customers is still an advantage, foreign direct investment remains the dominant mode of delivery of products to international markets. Thus, investment has increasingly followed trade as a component of EIAs.

Of course, the degree to which FDI increases between participant countries as a result of the conclusion of an EIIA depends on a number of factors. Notable among these factors is the pre-existing level of investment barriers between the countries involved before joining an EIIA and, consequently, the changes that actually take place in national investment regimes as a result of membership. In some cases, the policy climate created in anticipation of the conclusion of an EIIA may be sufficient to bring about some of the expected benefits.

*Source:* UNCTAD.

The locking-in quality of EIAs would be beneficial to individual member countries when the EIIA is an instrument that supports their national policy objectives. However, as EIAs embody an increasingly wider range of policies and activities, they may also preclude policy options otherwise available to national Governments. This is particularly challenging for developing countries that embrace EIAs as a development option. Hence, while EIAs are in principle aimed at promoting competitiveness and the effective integration of national economies into the international economy, they can reduce significantly the policy space available for individual policy initiatives and options.

A second policy effect of, and motivation for, EIAs is the strengthening of the bargaining power of the group vis-à-vis third countries. For example, it has been observed that the launching of negotiations on NAFTA was aimed at spurring European countries into acting on the Uruguay Round of multilateral trade negotiations (World Bank, 2005, p. 32). EIA members can also use their bargaining strength to prevent the adoption of certain decisions at the multilateral level, as exemplified by the reluctance of the Economic Community to make certain concessions to advance on the liberalization of agricultural trade in WTO negotiations. In principle, this bargaining effect would be particularly beneficial for countries that lack the political critical mass of their own necessary for imposing or substantially influencing positions in international policy discussions and negotiations. South-South EIAs can also enhance the collective bargaining power of developing countries in multilateral forums, especially when their membership confers significant numerical superiority.

On the other hand, EIAs, especially North-South EIAs, can also be used by the stronger parties to exercise their bargaining strength vis-à-vis weaker members, and put pressure on them regarding internal group policies as well as external agendas and negotiations. This potential effect is of particular concern to less developed country members of EIAs, as they may see their ability to promote their own national developmental strategies, and to play a developmental role in multilateral forums, reduced.

A third policy effect of, and motivation for, EIAs (and all EIAs) noted by authors (World Bank, 2005; OECD, 2001, pp. 6-7), is the improvement of political relations between the members. This effect emphasizes the EIAs' dimension as providers of public goods. Thus, in many cases, the creation of an EIA is a part of larger efforts to strengthen political relations among the parties, as economic integration increases regular political interaction and helps build trust in other areas. This was a motivation behind the creation of the European Community shortly after the Second World War, and is also behind the European Community's bilateral agreements with countries in Central, Eastern and South-Eastern Europe (World Bank, 2005, pp. 34-35). A related motivation is to limit migration from poorer countries by raising the living standards in those countries. This motivation was behind NAFTA and is behind the Euro-Mediterranean agreements. Here again, the bargaining power of the strong parties vis-à-vis the weaker ones may be used to impose policy options that are not always favourable to the national policy interests of the latter.

In short, there are significant potential economic and policy gains as well as costs for the countries participating in EIAs, which may increase as integration deepens (as in the case of EIAs). One overarching potential policy cost of deeper integration for the countries involved is a greater loss of policy autonomy. This is a particularly important concern for developing countries parties to EIAs, which may see their policy space for individual development strategy design and implementation reduced as a result of their EIA membership. For example, this may cause national Governments to forgo the use of policy instruments for development purposes where externalities are involved (e.g. in basic services). Another overarching policy cost of EIAs is more complex policymaking for national Governments. For example, the relatively recent inclusion of trade in services as part of EIAs (since the Uruguay Round negotiations) has added a new dimension to the rules, the implementation of which is not yet fully gauged through experience and practice.<sup>9</sup> The intrinsic additional complexity of managing deeper integration rules is further aggravated in the present context by the proliferation of EIAs with overlapping membership of countries and regions. The web of overlapping EIAs (and corresponding rules) that are in existence today resembles an "spaghetti bowl" (figure I.1) (World Bank, 2004, p. 38-

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<sup>9</sup> See Abugattas (2004) for a discussion of the issues raised by the new wave of EIAs dealing with services.



39 and figure 2.2; OECD, 2001) and is in constant change. The simultaneous implementation of multiple EIIA processes at different stages of evolution in which many countries are currently involved, and the administration of the procedures that it entails, can be a daunting task even for the most sophisticated institution, let alone for many developing countries that lack the necessary institutional backing. However, the administration of EIAs at both national and group levels is an important matter since the test of success of an EIIA is ultimately determined by its effective and timely implementation.

The creation of economically integrated areas through EIAs (and EIAs) can also entail potential economic gains as well as costs for countries outside the integrated area. With respect to gains, an EIIA (or EIA) that improves efficiency and increases real income within the area can expand the size of its market for goods and services (whether served through trade or foreign direct investment), including products imported from, or provided through, FDI by firms from non-member countries, thereby benefiting the latter. As for costs, EIAs, like all EIAs, normally introduce a degree of “discriminatory” (i.e. less favourable) treatment between their member countries and non-members. Even when such “discrimination” is not significant (i.e. when national non-discriminatory investment regimes have already established a “level playing field”), in a world of fierce competition for resources and markets, every inch of preferential treatment matters. In fact, a strong motivation for countries to participate in EIAs (and EIAs) is to counteract the potential negative effects of discrimination and marginalization as other countries conclude them. This raises the question of whether EIAs are complementary to broader national or multilateral efforts that seek to facilitate trade and investment flows across a broader spectrum of countries, or whether they create additional external artificial barriers to trade and investment, thus exacerbating economic exclusion and marginalization. While the countries that tend to benefit most from preferential trade and investment provided by an EIIA are usually the least developed of the EIIA group, poorer countries also stand to be the main losers when they are excluded from such preferences. This study looks briefly at various patterns found in EIAs with respect to the treatment they provide to non-parties in the area of investment (chapter III.B.3). However, the overall impact of the differential treatment resulting from an EIIA is a larger empirical question that impinges on many variables and its consideration exceeds the scope of this study.<sup>10</sup>

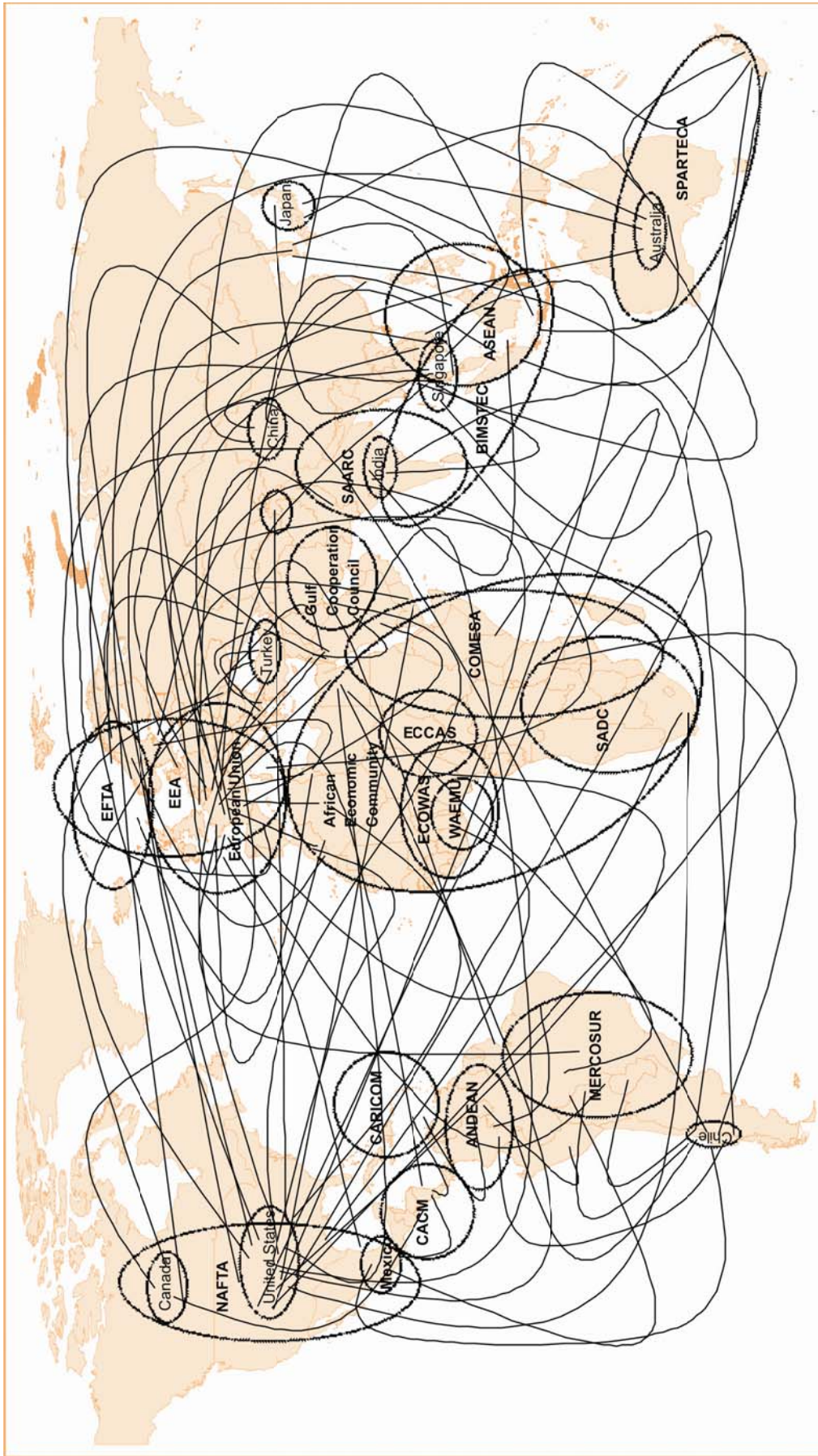
More broadly, the beneficial or prejudicial effects of EIAs depend to a certain extent on their relationship with the existing multilateral framework on trade and investment.<sup>11</sup> In the area of trade, the parameters are clearly established by the WTO multilateral trading system. In fact, one of the preconditions for allowing economic integration schemes under GATT is that they do not raise barriers to trade with third parties, or that any such effect is offset by at least a proportionate degree of trade liberalization (GATT, article XXIV). In the area of investment, however, there is no comparable road-map, as no comprehensive multilateral system exists, except for certain specific trade-related areas such as services, TRIMS and TRIPS. The question

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<sup>10</sup> The economic effects of EIAs on third countries have been examined predominantly with regard to trade. The debate has focused on the issue of whether EIAs result in trade creation or trade diversion with respect of non-EIA member countries (Viner, 1950). For a recent empirical study of the welfare impact of EIAs (including EIAs), see, for example, OECD (2003). The study reviews 40 empirical studies and finds *inter alia* that the welfare impact of EIAs is positive, but small; that trade diversion “can be an issue”; and that deep integration generates larger welfare gains than does integration through trade in goods only. The study concludes that economic theory cannot provide clear-cut conclusions, and therefore the determination of the net impact of a given EIA (or EIIA) is ultimately an empirical issue.

<sup>11</sup> The relationship between multilateralism and regionalism in relation to trade has been widely discussed in the literature; see, for example, Laird (1999) for a review, Bhagwati (1993), Kobrin (1995) and Lawrence (1995).

Figure I.1. The “spaghetti bowl”: Multiple overlapping EIAs, June 2005



Source: UNCTAD, based on World Bank, 2005, figure 2.2.

thus is whether the explosion of EIAs contributes to the creation of a clear, transparent, stable and fair framework of international rules in the area of investment, or whether these agreements result in an increasingly complex and intractable web of opaque, unclear, unpredictable and (sometimes) conflicting investment rules, the full implications of which are difficult to ascertain. Some efforts are already under way in the direction of clarity and order, including through provisions dealing with the interrelations between provisions and agreements. These are discussed in chapter V of this study, not to mention the contribution that the study as a whole may make in that direction.

In spite of the potential economic and policy costs of deeper integration, the number of EIAs that have moved beyond the shallow phase to increasingly deeper phases of integration is expanding rapidly: they address activities that occur inside the borders of a country and they address transactions other than trade in goods, notably, trade in services and investment. But while the inclusion of investment rules in EIAs, resulting in EIAs, is a logical step in a gradual process of deeper integration of markets, there are great variations among EIAs in terms of their coverage of investment issues. Thus, some EIAs provide for liberalization and non-discrimination, while other EIAs include also protection standards, often following closely BIT provisions in this area. Some include separate provisions on services, while others introduce provisions regulating investment activity (e.g. prohibition of anti-competitive practices and corporate governance). Yet other agreements do not go that far and limit themselves to a fairly light set of commitments to promote investment between the countries. The different approaches to investment in EIAs are discussed in detail in chapters III and IV below.

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## II. HISTORICAL EVOLUTION OF EIAs: AN OVERVIEW<sup>12</sup>

### A. EIAs before the 1990s

The incorporation of investment provisions in EIAs has a long history. In the pre-war world, EIAs were typically bilateral and they were concerned primarily with the liberalization of trade in goods. However, provisions relating to foreign investment were found in bilateral commercial treaties already in the late eighteenth century when the United States — and to a lesser extent Japan and a few European countries — began to negotiate a series of bilateral treaties known as Friendship, Commerce and Navigation (FCN) Agreements. These agreements created a right to trade on a most-favoured-nation (MFN) basis and included over time an increasing number of property protection or investment-related provisions.

After the Second World War, bilateral commercial agreements lost significance owing to the establishment in 1947 of a multilateral trading system under the General Agreement on Tariffs and Trade (GATT) that was intended to achieve the widest possible membership. Prior to the GATT, an attempt to create a multilateral agreement covering trade and investment issues, instrumented in the Havana Charter, failed. The GATT itself was the outcome of the failure to ratify the Havana Charter. After the adoption of the GATT, the process of integration of international trade became primarily multilateral and separated itself from the process of investment integration. Behind this separation was the recognition that an international investment regime is more intrusive than an international trade regime, reaching further into traditional domestic economic processes, and making negotiations technically and politically more difficult (Kline and Ludema, 1997). Even in the area of trade, at the time, countries were not prepared to go much further than negotiating tariff reductions. This explains the relatively narrow scope and limited authority of the original GATT (Kline and Ludema, 1997).

Some countries, however, wished to achieve among themselves a level of economic integration that went beyond the commitments they were making to the world at large through the GATT, and they concluded customs union or free trade agreements. Such “preferential” agreements were permitted by article XXIV of GATT. That article allows a waiver of the MFN treatment for third countries provided that the group is willing to eliminate substantially all of its trade barriers. In fact, in all these years since the adoption of article XXIV, GATT has never blocked the formation of a preferential agreement under this article (Kline and Ludema, 1997). From the outset, many EIAs addressed investment issues, either as part of the main agreement’s provisions or in separate agreements subsequently adopted by their members.

#### 1. Europe

The first EIIA of the post-GATT era was launched in Europe with the adoption, in 1957, of the Treaty Establishing the European Community (EC) (Treaty of Rome).<sup>13</sup> The original main purpose of the EC was to create a borderless internal market. To achieve that goal, the Treaty of Rome stipulated the free movement of goods, services, capital and persons, including the right of establishment of individuals and enterprises within the Community. It also guaranteed national and MFN treatment for goods, services, capital and persons from a Community member after

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<sup>12</sup> Most instruments reviewed in this study are reproduced in total or in part in the UNCTAD Compendium; see UNCTAD (1996-2005). Titles of instruments are sometimes abridged for ease of reading.

<sup>13</sup> The original founding members of the European Community were Belgium, France, Germany, Italy, Luxembourg and the Netherlands. Denmark, Ireland and the United Kingdom acceded in 1973, Greece in 1981, and Portugal and Spain in 1986, thus bringing the EC membership at the end of the 1980s to 12.



entry in another Community member. Competition rules completed the scheme, to guarantee the proper functioning of EC markets. Through these basic principles, investment activity within the EC became an integral part of the integration model sought by the Treaty of Rome. In 1960, another group of European countries founded the European Free Trade Association (EFTA).<sup>14</sup> Originally, EFTA applied to trade in goods only.

## 2. *Developed countries*

The main institutional framework for cooperation on trade and investment facilitation amongst developed countries, the Organization for Economic Co-operation and Development (OECD), was established in 1960.<sup>15</sup> In the area of trade, the OECD was to complement GATT's liberalization efforts.<sup>16</sup> In the area of investment, the OECD initiated a process of liberalization and integration with the adoption in 1961 of the Code of Liberalization of Capital Movements and the Code of Liberalization of Current Invisible Operations. The Codes constitute legally-binding rules, stipulating progressive, non-discriminatory liberalization of capital movements and current invisible transactions (mostly services) through stand-still (prohibition on adoption of new restrictive measures) and roll-back (commitments to dismantle existing restrictive measures) provisions. All non-conforming measures must be listed in country reservations against the Codes. They are implemented through policy reviews and country examinations, relying on "peer pressure" to encourage unilateral rather than negotiated liberalization. Over the years, the Codes were revised and expanded in scope. Important recent additions were the right of establishment (1984) and cross-border financial services (1992). In addition, the OECD members adopted in 1976 the Declaration on International Investment and Multinational Enterprises. The Declaration complements the Codes by elaborating provisions on the treatment of foreign investment, and on the behaviour of TNCs, after entry in a host country. The Declaration includes decisions on national treatment, incentives and disincentives, and conflicting requirements imposed on TNCs. The Guidelines for Multinational Enterprises were adopted as a set of recommendations addressed to enterprises.<sup>17</sup>

Regional economic integration agreements began soon to proliferate in other regions. Many of them incorporated investment provisions.

## 3. *Arab and Islamic countries*

The Arab countries were the first group among developing countries to create an EIA addressing investment issues when, in 1957, the members of the League of Arab States signed the Agreement on Arab Economic Unity.<sup>18</sup> Among other things, the agreement guaranteed freedom of movement of persons and capital, and the exercise of economic activities within the group. In

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<sup>14</sup> The original founding members of EFTA were Austria, Denmark, Norway, Portugal, Sweden, Switzerland and the United Kingdom. Later, Iceland, Finland and Liechtenstein acceded to this Convention. Denmark, the United Kingdom, Portugal, Austria, Finland and Sweden withdrew at different stages from the EFTA Convention as a result of their accession to the European Union.

<sup>15</sup> The original members of the OECD were Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Italy, Ireland, Israel, Japan, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom and the United States.

<sup>16</sup> All original OECD members were also original members of GATT.

<sup>17</sup> While the OECD investment instruments are not part of a broader economic integration scheme in the strict sense, they have been mentioned in this study because they represent a model of liberalization and integration in the area of investment that has been broadly followed in EIAs.

<sup>18</sup> The founding members of the Arab Economic Unity were Egypt, Iraq, Jordan, Kuwait, Sudan, the Syrian Arab Republic and Yemen.

1970 the members of the Arab Economic Unity adopted the Agreement on Investment and Free Movement of Arab Capital among Arab Countries, intended to promote and protect investment between capital-exporting and capital-importing Arab countries. The parties agreed to give preferential treatment to Arab capital, and to grant to Arab investments national treatment and treatment no less favourable than foreign investments received. Covered investment was entitled to fair and effective compensation in the event of expropriation. Investors had a right to transfer certain payments related to their investments and to reside in the host country in order to carry out investment activities. Complementing these provisions, in 1971, the group established the Inter-Arab Investment Guarantee Corporation to provide insurance guarantee to capital flowing between their members. As the membership of the Arab League expanded,<sup>19</sup> it adopted in 1980 the Unified Agreement for the Investment of Arab Capital in the Arab States. The new agreement reflected most of the policies of the 1970 Agreement providing for preferential treatment for Arab investors in certain cases. It also contained a provision for conciliation or arbitration of disputes between the parties arising under the agreement. Shortly thereafter, in 1981, the members of the Organization of the Islamic Conference,<sup>20</sup> in implementation of their Agreement on Economic, Technical and Commercial Cooperation, signed the Agreement on Promotion, Protection and Guarantee of Investments, which contains investment protection provisions similar to those in the 1980 Arab League agreement.

#### 4. Africa

Sub-Saharan African countries had also an early start in the process of trade and investment-related integration. The first economic integration area was created in 1964 with the adoption of the Treaty Establishing the Customs and Economic Union of Central Africa (UDEAC or CEUCA), which later became the Monetary and Economic Union of Central Africa (CEMAC).<sup>21</sup> In 1965, the members of UDEAC signed the Common Convention on Investments. It contained only a few, relatively unique protection provisions applying to all foreign investors. These included a provision guaranteeing the acquired rights of any kind of undertakings lawfully established in the countries of the union; a guarantee of free transfer of capital and profits “within the framework of [members’] exchange restrictions”; the right of foreign investments to acquire rights deemed necessary for the exercise of their activities, such as real property, concessions and authorizations; a right of national treatment for foreign employers and workers with respect to their professional activities and taxation; and a right of national treatment for foreign investments with respect to intellectual property protection and access to courts. Most of the agreement, however, established a mechanism for granting preferences to certain Community investments. The Convention included four schedules of preferences that might be granted, and identified the criteria for selecting those proposed investments that might be granted preferences. These provisions on investment were complemented by the signing by the members of UDEAC, in 1972, of the Joint Convention on the Free Movement of Persons and the Right of Establishment. That agreement dealt principally with the right of UDEAC individuals to move freely within the

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<sup>19</sup> As of 1980, the members of the League of Arab States were Algeria, Bahrain, Comoros, Djibouti, Egypt, Iraq, Jordan, Kuwait, Lebanon, the Libyan Arab Jamahiriya, Mauritania, Oman, Palestine, Qatar, Saudi Arabia, the Syrian Arab Republic, Somalia, Sudan, Tunisia, the United Arab Emirates and Yemen.

<sup>20</sup> As of 1995, the members of the Organization of the Islamic Conference were Afghanistan, Albania, Algeria, Azerbaijan, Bahrain, Bangladesh, Benin, Brunei Darussalam, Guinea-Bissau, Indonesia, the Islamic Republic of Iran, Iraq, Jordan, Kuwait, Kyrgyzstan, Lebanon, the Libyan Arab Jamahiriya, Maldives, Malaysia, Mali, Mauritania, Morocco, Mozambique, Niger, Nigeria, Oman, Pakistan, Palestine, Qatar, Saudi Arabia, Senegal, Sierra Leone, Somalia, Sudan, the Syrian Arab Republic, Tajikistan, Tunisia, Turkey, Turkmenistan, Uganda, United Arab Emirates, the United Republic of Tanzania and Yemen.

<sup>21</sup> The original members of UDEAC were Cameroon, the Central African Republic, Chad, Congo, Equatorial Guinea and Gabon.

Union, and to engage in professional or craft-related occupations, or to set up and manage enterprises, but only subject to the laws of the member countries. The investment framework of UDEAC was further expanded, in 1975, with the adoption of a Multinational Companies Code, granting a series of advantages to companies established in two or more member countries with a certain proportion of contributions from Community investors.

The Great Lakes countries established their own Economic Community (CEPGL)<sup>22</sup> in 1976, and, in 1982, adopted the Community Investment Code defining the guarantees, rights and obligations of joint enterprises and community enterprises, applicable principally, but not exclusively, to investors of Community members. This agreement is reminiscent in some respects of the 1965 UDEAC Common Convention on Investments, notably with respect to the recognition of acquired rights and similar guarantees. A right of free transfers was also granted, subject to existing legislation. Foreign investments were also guaranteed the same protection as enterprises with inter-Community capital, including with respect to intellectual property rights, and were not to be subject to discrimination under the law. Most of the Great Lakes Community agreement established a mechanism for providing preferences, such as tax advantages, to certain investments with Community capital.

In 1983 the original UDEAC and CEPGL members created a wider community under the Treaty for the Establishment of the Economic Community of Central African States (ECCAS).<sup>23</sup> The ECCAS treaty sought to eliminate gradually obstacles to the free movement of people, goods, services and capital, and to the establishment of enterprises between its member countries.

West African countries, for their part, signed in 1975 the Treaty Establishing the Economic Community of West African States (ECOWAS),<sup>24, 25</sup> whose article 2 called for the abolition by stages of obstacles to the free movement of persons, services and capital. A few years later (in 1979), they adopted Protocol A/P.1/5/79 on Free Movement of Persons, Right of Residence and Establishment to give effect to article 2. Another protocol relating to community enterprises, adopted in 1984, provides certain guarantees and privileges to enterprises that are totally or partially owned by nationals of member countries and meet certain specified criteria. Community enterprises may not be expropriated except upon payment of fair and adequate compensation, and benefits granted under the approval agreement may not be altered to the investor's disadvantage, except in certain circumstances. The agreement provides for arbitration of disputes between community enterprises and the Community through ICSID.

In Southern Africa, the Treaty for the Establishment of the Preferential Trade Area of Eastern and Southern African States,<sup>26</sup> signed in 1981, introduced the Charter on a Regime of Multilateral Industrial Enterprises, aimed at encouraging the establishment of regional enterprises meeting certain development-oriented conditions. The PTA was superseded in 1993 by the

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<sup>22</sup> The members of the Economic Community of the Great Lakes are Burundi, the Democratic Republic of the Congo and Rwanda.

<sup>23</sup> The members of the Economic Community of Central African States are Burundi, Cameroon, the Central African Republic, Chad, Congo, the Democratic Republic of the Congo, Equatorial Guinea, Gabon, Rwanda, and Sao Tome and Principe and Zaire.

<sup>24</sup> The members of ECOWAS are Benin, Burkina Faso, Cape Verde, Côte d'Ivoire, Gambia, Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone and Togo.

<sup>25</sup> ECOWAS replaced the Economic Community of West Africa (ECWA), established in 1973.

<sup>26</sup> The original members of the Southern African Development community were Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, the United Republic of Tanzania, Zambia, and Zimbabwe. Namibia, South Africa, Mauritius, the Democratic Republic of the Congo and Seychelles joined during the 1990s.



Treaty Establishing the Common Market for Eastern and Southern Africa (COMESA) (see below).

Other sub-Saharan African EIAs signed between 1960 and 1989 contained no or very limited investment-related provisions. These included the East African Community, established in 1967.

## 5. America

The treaty that created the Latin American Free Trade Association (LAFTA) in 1960 was the first attempt, after the establishment of GATT, to develop a long-term process of economic integration within the Latin American subregion. The LAFTA did not address investment issues. Only when it was replaced in 1980 by the treaty of Montevideo, establishing the Latin American Integration Association (LAIA or ALADI), did some provisions on investment begin to appear (article 48 of ALADI granted MFN treatment to capital originating from member countries).<sup>27</sup> As part of the process of economic integration, ALADI envisaged the adoption of bilateral “economic complementation agreements” (ECAs) between its members, which would be open to the participation of other members. In many cases, ECAs signed under the aegis of ALADI contain provisions on investment. In 1969, the group of five Andean countries (and Chile)<sup>28</sup> signed the Cartagena Agreement, aimed at the creation of an Andean Common Market (also known as the Agreement of Andean Sub-regional Integration), which in 1992 became known as the Andean Community. Among other things, the Cartagena Agreement envisaged the development of programmes and measures that facilitated the flow of investment within the subregion (article 89) and, in particular, the promotion of Andean multinational enterprises. The main manifestation of the Andean approach to regional and third-party investment in those days was the Andean Pact Commission Decision 24, adopted in 1970, on Common Regulations governing Foreign Capital Movement, Trade Marks, Patents, Licenses and Royalties, and Andean Pact Commission Decision 244 establishing a Uniform Code on Andean Multinational Enterprises. Decision 24 granted preferential treatment for foreign investment made in the form of joint ventures with Andean capital participation. It also introduced a system of controls and conditions on foreign investment and foreign technology from third countries. Decision 244 established a system of preferences for companies comprised under the definition of Andean multinational enterprises. Both decisions were superseded in the 1990s (see below).

Meanwhile, in the Central American subregion, a group of five Central American countries signed in 1958 the Multilateral Treaty on Free Trade and Economic Integration.<sup>29</sup> Among other things, the treaty granted, in article XVII, national treatment for the establishment of enterprises from other member countries. It also guaranteed fair and non-discriminatory treatment for the transfer of capital and funds. This agreement was the precursor of the General Treaty of Central American Integration signed in 1960. In the area of investment, the Central American integration system endorsed the pre-established “Regime for the Central American Integration of Industries”, granting preferential treatment to Central American enterprises engaging in certain priority industries (e.g. infrastructure). In the same year 1960, Guatemala, Honduras and El Salvador signed an Economic Association Agreement committing the parties to

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<sup>27</sup> The members of the Latin American Integration Association were Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Paraguay, Peru, Uruguay and Venezuela.

<sup>28</sup> The members of the Andean Community are Bolivia, Colombia, Ecuador, Peru and Venezuela. Chile was a founder member but later withdrew.

<sup>29</sup> The members of the Central American Free Trade and Economic Integration Agreement were Costa Rica, Guatemala, Honduras, El Salvador and Nicaragua.

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guarantee the free movement of goods, capital and persons. The Caribbean countries, for their part, signed in 1973 the Treaty of Chaguaramas with the purpose of creating a Caribbean Common Market (CARICOM).<sup>30</sup> Prior to the conclusion of the CARICOM Agreement, the Dickenson Bay Agreement Establishing the Caribbean Free Trade Association,<sup>31</sup> signed in 1966, committed its members to grant national treatment to other members' enterprises and avoid restrictions that jeopardized such treatment. The CARICOM Treaty itself committed the parties, among other things, to refrain from applying new restrictions on the establishment and operations of economic enterprises of CARICOM origin. In addition, a preferential regime for CARICOM enterprises was adopted in 1987.

In North America, Canada and the United States signed a Free Trade Agreement in 1987 which was the precursor of NAFTA. In particular, its chapter on investment contained a number of liberalization and protection provisions that were later developed and expanded in NAFTA.

## 6. Asia

The process of regional economic integration in the area of investment in Asia began with the creation of ASEAN in 1976.<sup>32</sup> The first formal manifestation of such integration was the Basic Agreement on ASEAN Industrial Joint Ventures adopted in 1983, which was revised in 1987. These agreements granted a number of preferences for companies that produced certain products in any of the participating countries, had equity participation from nationals of at least two participating countries and satisfied the equity ownership provisions specified in the agreement. Also in 1987, the members of ASEAN adopted the Agreement for the Promotion and Protection of Investments. This agreement follows the basic structure of a traditional European BIT and reflects most of its standard provisions, albeit with a few but significant departures. It was revised in 1996.

Investment issues were also included in the Unified Economic Agreement between the Countries of the Gulf Cooperation Council (GCC)<sup>33</sup> adopted in 1981. The agreement provides for national treatment among its members with respect to the free movement of capital and persons, right of ownership and freedom to exercise economic activity. On the other hand, until recently, investment issues were left outside the scope of the South Asian Association for Regional Cooperation established in 1985.<sup>34</sup>

In the Pacific, the South Pacific Regional Trade and Economic Cooperation Agreement (SPARTECA), signed in 1981 by the members of the South Pacific Forum, featured the promotion of investment among its objectives.<sup>35</sup>

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<sup>30</sup> The members of CARICOM are Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, and Trinidad and Tobago.

<sup>31</sup> The members of the Caribbean Free Trade Association were Antigua, Barbados and British Guiana.

<sup>32</sup> The founding members of ASEAN were Indonesia, Malaysia, the Philippines, Singapore and Thailand. Brunei Darussalam joined in 1984, thus bringing the membership to six at the end of the 1980s.

<sup>33</sup> The members of the Gulf Cooperation Council are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates.

<sup>34</sup> The members of the South Asian Association for Regional Cooperation are Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka.

<sup>35</sup> The founding members of the South Pacific Forum were Australia, the Cook Islands, Fiji, Kiribati, Nauru, New Zealand, Niue, Papua New Guinea, the Solomon Islands, Tonga, Tuvalu and Western Samoa.

A principal common characteristic of the early EIAs was that, typically, they were signed between countries sharing similar economic and social conditions, usually in the same region and at similar level of economic development. Exceptions to this trend were the cooperation agreements signed by the European Community, starting in the late 1960s, with a number of developing countries and groups (many of which have been superseded by more recent and advanced EIAs),<sup>36</sup> the Agreement for the Establishment of a Free Trade Agreement between Israel and the United States of America, and SPARTECA. The coverage of investment issues in most of these agreements is, however, very limited.

At the same time, there were clear differences in the approach to investment issues in the early EIAs signed between developed countries and those signed between developing countries. The developed countries' EIAs sought mainly to liberalize foreign investment among their members. The processes of liberalization were typically followed up and monitored by common institutional mechanisms. While they normally did not restrict investments from outside the EIA area, investment relations with third countries were often left outside the scope of the EIA to be decided by the individual member countries, either through national investment regimes or through bilateral investment treaties. Similarly, specific investment protection issues were not normally spelt out by earlier developed country EIAs.

In contrast, most EIAs signed between developing countries between 1960 and 1989 emphasized promotion of investments within the member countries, with many of them granting various types of regional preferences to companies originating (at least in part) and operating within the group. Such preferences were, however, restricted to investment in strategic sectors or activities, and were subject to detailed approval procedures and controls spelt out in the agreements. A level of investment protection, especially against expropriation, was also often granted. The mechanisms for implementation of the agreements tended to be weak. This resulted in poor follow-up on their commitments and programmes. With respect to investment from third countries, early agreements that explicitly addressed it sometimes established controls and restrictions, including compulsory joint ventures, technology licensing, fade-out requirements and performance requirements, as conditions for investing in the area and, in particular, for participating in the Community's preferential regime (e.g. the Andean Pact through its Commission Decisions 24 and 244). Other agreements, such as the UDEAC and Great Lakes countries' Investment Codes, extended certain legal guarantees to all foreign investors. Those agreements reflected the development concerns of that era, which included some caution about the potential negative effects of foreign direct investment from developed countries and some hope of stimulating development through cooperation among developing countries.

### **B. EIAs in the 1990s and early 2000s**

The pattern that had emerged in the post-war era changed in very important ways during the 1990s. The first important change was the dramatic increase in the number of EIAs concluded, together with the increase in the number of countries that became party to such treaties in all parts of the world, reflecting both the expansion of the membership of existing regional EIAs and the adoption of new EIAs at bilateral, regional, plurilateral and interregional levels. The new developments were partially the result of an important qualitative change that took place during this period: EIAs that previously had been reserved only for countries at similar levels of economic development started to be concluded between developed and

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<sup>36</sup> For example, the agreements signed by the EC with the East African States, ASEAN, China, Cyprus, the Syrian Arab Republic and the countries of the Gulf Cooperation Council, and, of course, the Lomé Conventions with the ACP countries.

developing countries. One early notable example was the North American Free Trade Agreement (NAFTA), concluded by two highly developed countries, Canada and the United States, and a developing country, Mexico. The change was also reflected in the movement by the EC and EFTA towards negotiating various types of EIAs with an increasing number of transitional economies and developing countries and groups. The trend was later followed by developed and developing countries in all regions.

Simultaneously with these quantitative and qualitative changes, the process of economic integration already initiated in various EIAs continued to deepen during this period through the incorporation, expansion and elaboration of provisions aimed at facilitating foreign investment. Thus, the process of investment liberalization initiated under inter alia the EC treaty, the OECD codes of liberalization and CARICOM continued its course. Other EIAs that had not significantly addressed investment at the outset were revised or new provisions were adopted dealing with investment issues. Examples include ECOWAS, the Central American Common Market and EFTA. Still other EIAs that had originally set out restrictive regimes on foreign investment originating from non-member countries changed their approach in the direction of liberalizing and facilitating such investment. Changes in the Andean Community reflected this trend. At the same time, an increasing number of EIAs, new or revised, began to incorporate — often in addition to their liberalization provisions — detailed provisions on the legal protection of investment between their members, including notably provisions for the settlement of investment disputes between investors and their host countries. NAFTA, for example, included investment provisions similar in scope and depth to the provisions of the United States BITs.

The expansion of EIAs containing increasingly comprehensive and detailed provisions on investment reflected not only the convergence of several trends moving in the same direction, but also changes in the nature of economic activity itself. Whereas trade and investment had once been seen as substitutes, they were increasingly seen as complementary. Investment did not necessarily take the place of trade; it might promote trade as well. If trade and investment were intertwined, agreements relating to each inevitably would become interrelated.

The new approach was reflected in the renegotiation of the GATT itself. The Uruguay Round of GATT negotiations ended with the formation of the World Trade Organization (WTO) in 1995 and, more importantly for the purposes of this study, the conclusion of the General Agreement on Trade in Services (GATS), the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) and the Agreement on Trade-Related Investment Measures (TRIMs). These developments meant that the strengthened multilateral trading system that had emerged under the WTO had added to its responsibilities at least some investment-related matters, principally those dealing with the delivery of services through the establishment of investment, the protection of investment in the form of intellectual property and the treatment of investment (i.e. preventing host countries from imposing certain trade-distorting performance requirements on foreign investment). Thus, the intermingling of trade- and investment-related concerns within the WTO paralleled the willingness of countries to mix trade and investment commitments in bilateral, regional, interregional and plurilateral agreements concluded outside the WTO. Indeed, the decision to conclude an agreement on trade in services, given that services are often delivered through the establishment of foreign direct investment, meant that trade and investment inevitably and unavoidably would be addressed by the same agreements.

The old boundaries, in short, were largely gone. EIAs were now being concluded between two countries or many countries. The countries were similar or dissimilar in economic circumstances and they were in the same or in different regions. The agreements addressed trade in goods, trade in services, investment, or any combination of the three. Any permutation of

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these features could also appear in any given agreement. The review of developments in EIAs concluded during this period bears this out.

### *1. Intraregional EIAs*

#### *a. Europe*

In Europe, the EC continued its geographical expansion, with the addition of three new members in 1995, and ten in 2004, reaching a total of 25 members. In 1992, the members of the EC adopted the Treaty of the European Union (Maastricht Treaty) which, among other things, advanced the process of investment liberalization and integration between its members. It also prohibited all restrictions to the free movement of capital between its member countries and third countries. Some pre-existing restrictions applying to third countries were however allowed to apply.

The EFTA Convention of 1960 was also revised during this period. With the 2001 Vaduz Convention, the EFTA States draw up comprehensive chapters aimed at a general liberalization of investment and trade in services among themselves. The revised Convention establishes *inter alia* a right of establishment, subject to exceptions in a negative list contained in an annex, and provides for consultations to address restrictive business practices. Other provisions grant a right of free movement of persons and require that laws be made public. A parallel chapter on trade in services prohibits restrictions on the right to supply services and provide for national treatment with respect to trade in services. Regarding the protection of investment, the agreement guarantees national treatment after establishment and obligates the parties to provide protection for intellectual property.

The process of European integration was further expanded in 1992, with the adoption by the member countries of the EC and EFTA of the Agreement on the European Economic Area. The agreement provides for a right of establishment, post-establishment national treatment and free transfer of capital, and requires the parties to restrict certain anticompetitive practices.

Also during the 1990s the EC and EFTA concluded EIAs with a number of transition economies in Central and Eastern Europe. The association agreements concluded by the EC with Central and South-Eastern European countries establish a framework for the liberalization of investment and trade in services to be completed in several stages. In many cases, these agreements are considered preliminary steps towards full accession to the Community and are to be superseded upon accession. With the Russian Federation, the Balkan countries and the countries members of the Commonwealth of Independent States (CIS), the EC has signed partnership and cooperation agreements intended mainly to provide institution-building and technical assistance to implement free market reforms. They contain commitments to promote and gradually liberalize trade in services and investment with a view to creating, in some cases, a free trade area at a later stage.

The EFTA countries signed free trade agreements with Central, Eastern and South-Eastern European countries. These agreements include a general commitment to progressively open markets for investment and trade in services. A joint committee is set up to follow up on these commitments. They also include commitments to protect intellectual property rights and to limit anticompetitive practices. An expanded version of the agreement includes a right to make transfers related to an investment. The EFTA agreements with third European countries have inspired the adoption of bilateral free trade agreements the investment provisions of which are



similar in scope and content. After the first Central European countries joined the European Community, other less advanced European countries have continued to sign this type of bilateral free trade agreements between themselves as preliminary steps towards national economic reform, to prepare for EC- and EFTA-consistent regulatory approaches to investment and services.<sup>37</sup>

## **b. America**

The North American Free Trade Agreement (NAFTA), signed in 1992 by Canada, Mexico and the United States, contains some of the most advanced and detailed provisions for the liberalization and protection of investment found so far in EIAs. Thereafter, Canada and Mexico concluded additional EIAs with Latin American countries that follow the NAFTA model closely in their investment chapter. Other American developing countries and groups also concluded NAFTA-type EIAs between themselves. Since 2002, the same practice has been followed by the United States.

In 1994, the four Southern Latin American countries signed the Agreement Establishing the Southern Common Market (MERCOSUR), which was complemented by two protocols dealing with investment issues. The Colonia Protocol on Reciprocal Promotion and Protection of Investments within MERCOSUR resembles the United States BIT model, granting national and MFN treatment at the pre-establishment and post-establishment levels. The Protocol on the Promotion and Protection of Investments coming from States not Parties to MERCOSUR, on the other hand, follows the European BIT pattern in that it does not grant rights of establishment. Thus, national and MFN treatment applies only after entry. Both protocols provide for investor-State dispute mechanisms. A few years later, the Protocol of Montevideo on Trade in Services added further depth to the integration efforts within MERCOSUR. In 1998, the four countries members of MERCOSUR and Canada signed the Trade and Investment Cooperation Arrangement establishing a framework for enhancing trade and investment relations. The Arrangement contains a plan of action which foresees the conclusion of bilateral investment agreements and the identification of trade- and investment-distorting measures. The plan of action also provides for consultations on the negotiation and implementation of rules in multilateral and regional forums.

Other pre-existing EIAs in the Americas were revised, updated and/or expanded during this period to bring their investment provisions into line with recent approaches. For example, the Central American Group consolidated its earlier (1960) free trade and investment area with the adoption of the Agreement on Trade in Services and Investment (2002). Also, the CARICOM countries adopted in 1997 the Protocol Amending the Treaty Establishing the Caribbean Community on Establishment, Services and Capital. The protocol amendments of the provisions on investment and services reflect recent liberalization trends elsewhere. In 2001, the Treaty of Chaguaramas was further revised to establish the CARICOM Single Common Market and Economy and consolidate the previous reforms. Among other things, it contains provisions creating mechanisms for removal of existing restrictions on investment and services. The CARICOM countries also signed free trade and investment agreements with the Dominican Republic and with Venezuela. Moving in the same direction, the 1991 amendments to the Andean Community instruments on foreign investment and transfer of technology (Commission Decisions 291 and 292 superseding Decisions 24 and 244 respectively) replaced earlier more

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<sup>37</sup> Among the European countries that have recently signed these bilateral free trade agreements are Albania, Bulgaria, Croatia, Macedonia, Romania, and Serbia and Montenegro.

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restrictive regulations. And, with the adoption of Decision 439 in 1998, the Andean Community established a general framework for the liberalization of trade in services within the Community. Subsequently, a Framework Agreement for the Creation of a Free Trade Area was signed between MERCOSUR and the Andean Community. In 1999 the countries of the Andean Community signed a Trade and Investment Cooperation Arrangement with Canada similar in content to the Arrangement between MERCOSUR and Canada. The Central American countries and Canada for their part signed in 1998 a Memorandum of Understanding on Trade and Investment to strengthen their cooperation with a view to liberalizing trade and investment between the parties and prepare the ground for the completion of the Free Trade Area of the Americas. The parties agreed on a series of investment promotion activities, including the adoption of BITs.

Latin American countries have also continued the practice of concluding bilateral economic complementation agreements (and in some cases also between a group and a third country) under the aegis of ALADI, in order to advance the various ongoing processes of economic integration within the subregion. These ECAs vary considerably in terms of their coverage of investment issues.

Recently, most countries in the American continent embarked on the negotiation of the Free Trade Area of the Americas (FTAA). Launched in 1997, and still under negotiation, the FTAA, should it be adopted, is expected to establish an American economic integration area covering most of the American continent, and incorporating detailed rules on investment, trade in services, competition and intellectual property protection and dispute resolution.

### c. Asia

Meanwhile in Asia, the membership of ASEAN was extended to include Myanmar, the Lao People's Democratic Republic and Cambodia. In 1995, they adopted the ASEAN Framework Agreement on Services providing for the liberalization of trade in services in a substantial number of sectors within a reasonable time frame. This was to be accomplished through negotiations directed towards achieving market access commitments beyond those specified in the GATS. The Protocol Establishing the ASEAN Dispute Settlement Mechanism applies to trade and investment disputes under the various ASEAN agreements. More recently, the Framework Agreement on the ASEAN Investment Area, adopted in 1998, addresses the admission of investment. The Framework Agreement applies only to direct investment, explicitly excluding portfolio investment as well as investments covered by the ASEAN Framework Agreement on Services. The agreement commits the parties to open all industries to investments by ASEAN investors, subject to a negative list of exclusions that is to be revised biennially with a view to achieving complete liberalization by 2010. For non-ASEAN countries, 2020 is the date for investment liberalization. The Framework Agreement grants ASEAN investors and their investments both pre-establishment and post-establishment national and MFN treatment. It also has transparency provisions. The ASEAN Dispute Settlement Mechanism also applies to disputes under this agreement.

In recent years ASEAN has started to conclude association and framework agreements with other Asian countries. The framework agreements signed with India and China commit the parties to promote investment through inter alia entering into negotiations with a view to progressively liberalizing their investment regimes, improving the transparency of investment rules and providing for the protection of investments. A similar framework agreement has been signed by ASEAN with Japan.

In addition, individual Asian countries have concluded bilateral EIAs among themselves in recent years, pursuing various levels of integration through trade and investment. Through the 1990s and early 2000s, Australia concluded trade and cooperation agreements with, for example, China, Fiji, Japan and Papua New Guinea. India has signed a free trade agreement with Thailand which is similar to the framework agreements signed by ASEAN with India and China. The agreement also contains commitments on services. The Trade and Economic Framework Agreement between Australia and China is somewhat narrower in scope, the parties agreeing to cooperate by exchanging information, improving the investment climate through the protection of investments and building institutional linkages. Provisions on services are also included. Especially noteworthy are also some comprehensive and elaborate bilateral EIAs which, with different titles, have been concluded by Australia, Japan, the Republic of Korea, New Zealand, Thailand and Singapore. Although these agreements vary, they represent — along with similar interregional agreements discussed below — the cutting edge in EIAs in terms of the number of investment-related topics covered and the level of detail of the investment-related provisions.

Finally, several subregional Asian groups that until recently had remained outside this treaty practice have started to build their own EIA processes. In 2004, the member countries of the South Asian Association for Regional Cooperation (SAARC)<sup>38</sup> signed the Framework Agreement on the South Asian Free Trade Area, in which they agreed to consider the adoption of measures for the removal of barriers to intra-SAARC investments and rules for fair competition. Also in 2004, the countries members of the Bay of Bengal Initiative for Multi-Sectoral and Economic Cooperation<sup>39</sup> (BIMST-EC) adopted the Framework Agreement on the BIMST-EC Free Trade Area, in which they agreed to provide for the promotion and protection of investment, strengthen cooperation to facilitate investment, improve transparency of investment rules and enter into negotiations in order to progressively liberalize the investment regime through a positive-list approach.

#### **d. Africa**

In Africa, a number of new EIAs were adopted, and some existing ones were revised or expanded during the 1990s. The Treaty Establishing the African Economic Community (AEC), signed in 1991, contains provisions under which the parties agree to ensure the free movement of capital within the Community through the elimination of restrictions on capital transfers in accordance with a timetable to be adopted. It also contemplates the progressive granting of rights of residence and establishment for nationals within the Community. Detailed provisions on establishment are to be formulated in a protocol. In 2001, the Community was transformed into the African Union, pursuing further its economic integration goals. In another regional effort, the Common Market for Eastern and Southern Africa (COMESA),<sup>40</sup> signed in 1993 to replace the Preferential Trade Area for Eastern and Southern African States, contains framework provisions on investment promotion, with some general principles on investment protection, but not dispute settlement. Also in 1993, the earlier (1975) ECOWAS Treaty was revised. The purpose of the Revised Treaty of ECOWAS is to establish a common market through the removal of obstacles to the free movement of goods, services, persons and capital, and to the right of establishment. It

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<sup>38</sup> The members of the South Asian Association for Regional Cooperation are Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka.

<sup>39</sup> Members of BIMST-EC are Bangladesh, Bhutan, India, Myanmar, Nepal, Sri Lanka and Thailand.

<sup>40</sup> The members of COMESA are Angola, Burundi, Comoros, Djibouti, Egypt, Ethiopia, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Rwanda, Somalia, Sudan, Swaziland, Uganda, the United Republic of Tanzania, Zambia and Zimbabwe.

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envisages the adoption of a regional agreement on cross-border investments to promote joint ventures. The members of ECOWAS have also undertaken to complete, within five years following the creation of a customs union, an economic and monetary union. In 2003, the members of ECOWAS signed the Protocol on Energy (A/P4/1/03). The Energy Protocol contains a chapter (chapter III) on investment promotion and protection in the energy sector similar to a BIT, including provisions on investor-State settlement of disputes.

Other African regional integration agreements adopted during this period contain framework programmatic commitments on investment liberalization that have yet to be articulated into operational provisions. These include the Agreement establishing the West African Economic and Monetary Union (WAEMU or UEMOA)<sup>41</sup> (formerly WAMU or UMOA), adopted in 1994 to implement a customs and monetary union among its members with a single currency (the Franc of the Communauté Financière Africaine or F, CFA). Among the stated objectives of WAEMU are to guarantee the free flow of persons, goods, services and capital and the right of establishment. The treaty creates a Capital Issues Committee to promote the elimination of controls on the transfer of capital among the member countries. The Southern Africa Development Community (SADC)<sup>42</sup> was established in 1992 to replace the Southern African Development Coordination Conference (SADCC) in existence since 1980. SADC commits its members to develop and harmonize policies to gradually establish the free movement of goods, services, capital and persons within the Community. Similarly, the Treaty for the Establishment of the East African Community,<sup>43</sup> signed in 1999 to revive the earlier EAC (1967), contains a commitment by which the States parties agreed to adopt measures to achieve the free movement of persons and services, and to grant the right of establishment and residence to their citizens.

New investment cooperation and integration efforts through EIAs by Arab countries in the 1990s have proceeded more in the context of the geographical regions where the relevant countries are located (mainly Middle East Asia and Africa) than through the adoption of new Arab or Islamic agreements, expanding also through various interregional and bilateral EIAs.

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Since the early 1990s EIAs have been concluded in every region of the world. At the same time, there are significant differences between agreements concluded by each region.

Agreements signed by the European Community, including the European Community Treaty itself, are concerned more with liberalization of investment flows than with investment protection. They often confer a right to establishment or at least contain a commitment to future liberalization. Provisions guaranteeing a right of free transfer are also common. Thus, these agreements are concerned with the flow of capital into and out of the host country. Provisions to ensure the proper functioning of markets by limiting anticompetitive practices are also very common among EC EIAs.

The EC agreements, on the other hand, have few investment protection provisions. This may be explained in part by the division of labour between the European Commission and the

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<sup>41</sup> The members of the West African Economic and Monetary Union are Benin, Burkina Faso, Côte d'Ivoire, Mali, Niger, Senegal, Togo and Guinea-Bissau. All of them share a common currency, the CFA Franc.

<sup>42</sup> The original founder members of SADC are Angola, Lesotho, Botswana, Malawi, Mozambique, Swaziland, the United Republic of Tanzania, Zambia and Zimbabwe. South Africa joined in 1994, followed by Mauritius (1995), the Democratic Republic of the Congo (1997) and Seychelles (1997).

<sup>43</sup> The members of the East African Community are Kenya, Uganda and the United Republic of Tanzania.

member States with respect to the negotiation of third party trade and investment issues. While the European Commission, which typically negotiates EC trade agreements with third parties, has authority to negotiate market access issues, including investment liberalization, the negotiation of investment protection issues remains vested in individual EC members (and they have typically negotiated mainly through BITs).<sup>44</sup> The most common protection provision in EC agreements is one intended to protect intellectual property rights. Some EC agreements also provide for national treatment of investment once established. However, EC agreements do not provide for investor-State dispute resolution. Instead, investment disputes under these agreements are normally dealt with under the general dispute settlement provisions that cover all matters under the agreement at the State-to-State level. Some EC agreements with transition economies include provisions for investment promotion, principally through economic cooperation. Until recently, EC agreements with developing countries contained limited provisions on investment which typically address investment promotion. However, this trend is being revised in particular in a number of agreements signed with advanced developing countries (see next section).

Recent EIAs concluded by States in the American region have been greatly influenced by NAFTA, which contains an investment chapter that follows the United States' BITs rather closely in substance, albeit with some notable differences. The NAFTA investment chapter contains comprehensive and detailed provisions on investment liberalization as well as investment protection. In addition, the NAFTA includes chapters that liberalize trade in services, restrict anticompetitive behaviour and protect intellectual property rights. Many EIAs in the Americas have provisions similar to those in NAFTA, although sometimes they also have important differences.

A significant deviation from the NAFTA approach in the America region is the CARICOM agreement, in which the investment provisions are more concerned with liberalization than investment protection. CARICOM, however, assumed investment protection commitments similar to those in a BIT in its 1998 free trade agreement with the Dominican Republic and its 2004 free trade agreement with Costa Rica.

On the other hand, bilateral ECAs signed between Latin American countries in the context of ALADI do not seem to follow a homogeneous approach to investment that is particular to this regional scheme. Instead, investment promotion, protection and liberalization provisions appear in different combinations in individual ECAs.

EIAs in Asia also tend to emphasize both investment liberalization and investment protection. This is particularly evident in the various stand-alone but complementary ASEAN agreements dealing with investment and trade in services. This emphasis is also evident in the series of comprehensive and detailed bilateral EIAs that have been recently concluded between Asian countries. Another group of recent Asian agreements commits only to further negotiations to liberalize and protect investments in the future.

Recent EIAs in Africa are also moving in the direction of liberalizing and protecting investments, and away from the preferential investment regimes provided for in earlier agreements. Some of the new agreements, however, have not yet reached the stage at which specific operational provisions on investment are formulated beyond some general commitments and principles.

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<sup>44</sup> The issue of shared competence between the EC Commission and its member States on investment issues is explicitly addressed in the European Constitution Treaty signed in 2004, articles III-216 and III-217.

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## 2. *Interregional EIAs*

The foregoing picture is further complicated by the superposition of an increasingly complex web of agreements concluded between countries and groups situated in different geographical regions.

In 1994, the Energy Charter Treaty was adopted by a group of 50 countries that included most OECD countries, Central and Eastern European countries and members of the Commonwealth of Independent States (CIS) (former USSR republics). Three additional countries — Australia, Japan and Mongolia — joined recently. The Charter is a sectoral agreement covering trade, investment, transit and efficiency in the key energy industry. Its investment provisions are fairly elaborate and deal mostly with treatment and protection standards after entry of investment. Reference is also made to the observance of relevant provisions of WTO agreements such as TRIMs and TRIPS. The treaty is to be complemented by a second agreement dealing with issues of admission, to be adopted at a later date.

In terms of geographical coverage, one of the broadest interregional agreements is the Non-Binding Investment Principles adopted in 1994 by the members of Asia-Pacific Economic Cooperation (APEC).<sup>45</sup> The principles were adopted in the context of a gradual process of trade and investment liberalization in the spirit of APEC's underlying "open door" approach to regionalism based on MFN treatment. Being of a non-legally binding nature, the Principles are intended to guide investment relations between member countries. They address key investment issues such as transparency of national law, non-discrimination, national treatment, investment incentives, performance requirements, expropriation and compensation, repatriation of funds and currency convertibility, settlement of investment disputes, entry of foreign personnel, avoidance of double taxation, investor behaviour and removal of barriers to capital movements.

Also in the early 1990s, the EC began to negotiate with non-member countries in different regions a new generation of trade agreements addressing investment issues. With countries in North Africa and the Middle East, the EC has concluded Euro-Mediterranean association agreements. These agreements were part of the Euro-Mediterranean initiative launched in 1995 aimed at creating a free trade and investment area by 2010. They include commitments to create a right of establishment at a future date, to avoid new restrictions on capital movements and to curb anticompetitive behaviour. With respect to several Asian (e.g. Nepal) and Latin American countries and groups of countries (e.g. MERCOSUR and the Andean Community), the EC has continued to conclude partnership and/or cooperation agreements, under which the parties agreed to participate in various forms of investment promotion. Moreover, since 2000, the European Community has concluded economic partnership agreements with several advanced developing countries, notably with Mexico and Chile. They deal extensively with trade in services. In the area of investment, the parties commit to liberalization at a future date.

The agreement concluded by the EC with the widest geographical reach is the Partnership Agreement between the Members of the African, Caribbean and Pacific Group of States of the One Part, and the European Community and its Members States, of the Other Part, also known as the "Cotonou Agreement". It was signed in 2000 as the successor to the four Lomé Conventions that date back to 1975. The Cotonou Agreement does not provide for rights of establishment or national treatment after establishment but affirms the importance of private investment for

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<sup>45</sup> The members of APEC are Australia, Brunei Darussalam, Canada, Chile, China, Indonesia, Japan, the Republic of Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, the Philippines, the Russian Federation, Singapore, Taiwan Province of China, Thailand and the United States.

economic development and calls upon individual members to conclude reciprocal economic partnership agreements covering trade in goods and services, as well investment promotion and protection agreements. The Cotonou Agreement does contain detailed commitments on the part of the European Community to promote investment flows to APC countries through a variety of measures, such as provision of information on investment opportunities and technical and financial assistance for institution- and infrastructure-building, as well as making available risk insurance for private investment. In addition, the Cotonou Agreement underlines the importance of trade in services, reaffirms the parties' commitments under the GATS, includes a commitment to implement national and regional rules to protect competition, and recognizes the importance of adhering to the TRIPS agreement and certain other international conventions.

Pursuant to the mandate established by the Cotonou Agreement — and in view of the fact that under the enabling clause of GATT article XXIV the waiver for the preferential system of Cotonou is due to expire in 2007 — the European Community embarked after 2003 on the negotiation of reciprocal economic partnership agreements with existing regional groupings within ECP countries. These agreements are aimed at encouraging liberalization of trade in goods and services as well as protecting investment. However, the specific issue outline of these agreements is currently under discussion (World Bank, 2005, p. 31 and box 2.3).

During the late 1990s and early 2000s, EFTA also continued to conclude free trade agreements, this time including with countries in Northern Africa (e.g. Morocco), providing for cooperation with a view to achieving a gradual liberalization of services and investment, banning restrictions on transfers of payments related to investments, protecting intellectual property rights and restricting anticompetitive practices. More recently, EFTA has signed a more elaborate type of free trade agreement with a few developing countries with relatively advanced economies, such as Chile, Mexico and Singapore. Although the contents of the agreements vary, they contain a wider range of obligations than their predecessors, especially with respect to trade in services.

Interregional initiatives have also been undertaken by individual countries. Canada has engaged, starting in the mid-1990s, in the conclusion of a series of bilateral arrangements on trade and economic cooperation (TECA) with countries in different regions (e.g. Australia, Iceland, Norway, Switzerland and South Africa). Under these arrangements, the parties typically agree to “endeavor to create the most favourable conditions for liberalization of trade in goods and services as well as of investment” (article II (1) of the TECA with Norway) in accordance with a joint work programme set forth in an annex. The joint work programme includes matters such as the removal of barriers to trade and investment and information exchange, with a view to encouraging the expansion of trade and investment. These TECA contemplate the creation of a consultative group to ensure implementation of the work programme, including the identification and removal of impediments to trade and investment. Another important element of the joint programme is to strengthen the parties' cooperation on negotiations in the WTO.

Furthermore, the United States entered into, throughout the 1990s and in early 2000, a series of bilateral agreements concerning the development of trade and investment relations with countries outside the American region, notably African and Middle East countries. Typically, these agreements commit the parties to seek to encourage trade and investment flows between themselves and establish a “council on trade and investment” to hold consultations aimed at enhancing trade and investment and removing impediments to trade and investment flows. With Jordan and Viet Nam the United States signed free trade agreements that are far more detailed. They contain an investment chapter that is quite similar to the United States BIT model.

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Since 2002, a number of countries (including Chile, Japan, Morocco, Singapore and the United States) have embarked on the conclusion of very elaborate bilateral EIAs with countries outside their region. These agreements are in fact an expanded version of the NAFTA model, although there are significant individual variations.

\* \* \* \* \*

The preceding overview confirms that a complex network of EIAs is rapidly expanding across regions and is involving most countries in the world. This network consists of an intricate web of heterogeneous instruments with overlapping membership and diverse structures, approaches, coverage of issues and depth of commitments, reflecting different policy priorities as well as regional preferences. Although, at first sight, the complexity of the network defies classification and synthesis, an attempt is made in the next chapter to quantify the incidence and geographical distribution of the EIAs, and identify global patterns with respect to their approach to investment issues.

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### III. THE PRESENT UNIVERSE OF EIAs

#### A. Geographical Distribution

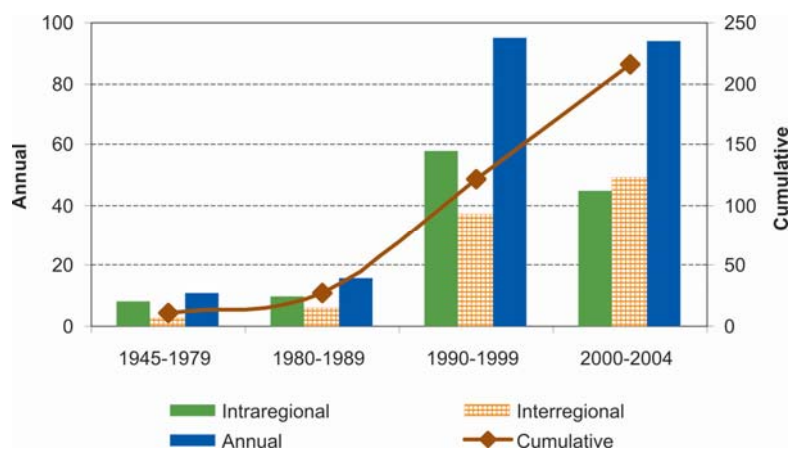
##### 1. Global trends

EIAs identified in this study exceed 218,<sup>46</sup> about 67% of the total 300 EIAs reviewed<sup>47</sup> (see annex table I). Approximately 87% of all these EIAs have been concluded since 1990 (41% since 2000), and the other 13% between 1945 and 1989 (figure III.1).

Initially, EIAs between countries in the same geographical region dominated the scene and, until the late 1980s, economic integration through EIAs remained confined mainly to intraregional processes, albeit with important exceptions.<sup>48</sup> Since the early 1990s, however, countries and groups located in

different regions began to sign EIAs with one another, with the result that interregional EIAs now account for 44% of the total 218 EIAs (87 of which have been concluded since 1990) (figure III.1). This trend is a manifestation of the globalization strategies being pursued by more and more countries in response to the increasing global competition for resources and markets facing national economies. Of course, the choice of partners within and between regions responds to a variety of economic and political motivations depending also on the characteristics of the countries involved.

Figure III.1. Growth of EIAs, 1945 - June 2005  
(Number)



Source: UNCTAD.

The dramatic growth in the number of EIAs since the early 1990s parallels the increase in the number of countries that are party to such agreements. Today, more than 99% of all

<sup>46</sup> The test used for the selection of the agreements included in the study is based on the definition of EIAs and EIAs provided in the introduction to the study. This definition allows for the exclusion of EIAs that are only insignificantly or indirectly related to investment, although where there is a doubt, the balance is tilted towards inclusion. Excluded from the 218 EIAs identified in this study are also EIAs that have been superseded by new EIAs, including those that have been terminated as a result of the relevant countries' accession to the European Union, or EIAs that are no longer in force. In certain cases, major revisions and additional protocols adopted by a pre-established EIA group are counted as separate agreements.

<sup>47</sup> An exact account of all existing EIAs and EIAs is difficult, if not impossible, in part because there are no consistent data source covering all EIAs, but also in part because of the difficulty of defining precisely what agreements fall within the scope of EIAs. For example, some agreements may deal only very peripherally with investment. It is also difficult to ascertain whether certain old agreements are still in force.

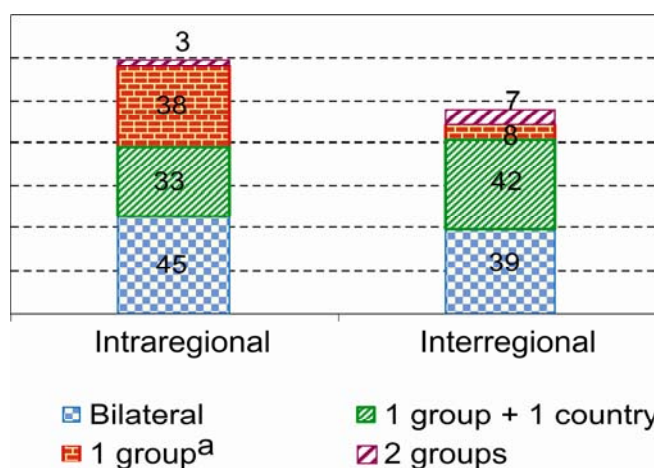
<sup>48</sup> For example, the agreements signed among Arab and Islamic countries, and earlier EIAs signed by the European Community with third countries, including notably the Lomé Conventions between EC and ACP countries (see chapter II).



countries and economies are members of at least one EIIA,<sup>49</sup> and the majority of countries are members of several such treaties. At the same time, the increase in membership of certain regional integration schemes has reduced the number of existing EIAs. For example, the recent accession of 15 European countries to the EC has rendered obsolete a number of previous agreements between the EC and these countries.

The geographical expansion of EIAs is proceeding along various paths. Thus, while existing EIIA groups have kept adding new members (e.g. EC, ASEAN), approximately 39% of the total number of agreements concluded since 1945 have been signed between two individual countries (bilateral EIAs) (83 since 1990), of which 53.5% involve countries in the same geographical region and 46.5% are between countries located in geographically dispersed regions. Regarding the other 60% of EIAs, 22 involve the formation of a new group (six since 1990), 24 are major revisions or additional protocols adopted by a pre-established EIIA group (14 since 1990) and only 7.5% involve the adoption of an EIIA between several pre-existing groups of countries (eight since 1990). Finally, over half of this 60% of EIAs are between a group of countries and a third country (40% of which are within the same region, and 60% are interregional). EIAs between an economically integrated group and a third country are sometimes concluded as an intermediate step towards full membership of the third country at a future time (e.g. the association agreements signed by the European Community) (figure III.2).

**Figure III.2. Intraregional and interregional EIAs, by type, June 2005**



Source: UNCTAD.

<sup>a</sup> Including major revisions of and protocols on pre-existing EIAs.

In terms of the distribution of EIAs among geographical regions, the American countries have concluded the largest number of EIAs with 95 agreements, experiencing a sharp increase in the mid-1990s after the conclusion of NAFTA. European countries<sup>50</sup> were the first to conclude an EIIA after the adoption of the GATT. They have since concluded the second largest number of EIAs, reaching a total of 83 (excluding EIAs that were terminated after the EC accession of additional European countries). They are followed closely by Asian countries with 81 agreements, although these countries had a late start. On the other hand, African countries were the first among developing countries to conclude EIAs but have since concluded fewer agreements than the other developing regions. The African countries are parties to 34 agreements (figure III.3).

<sup>49</sup> The other 1% of countries/economies that have not concluded an EIIA includes Andorra, the Democratic People's Republic of Korea, Monaco, San Marino, Sao Tome and Principe, and Timor-Leste.

<sup>50</sup> Including the Commonwealth of Independent States (CIS).

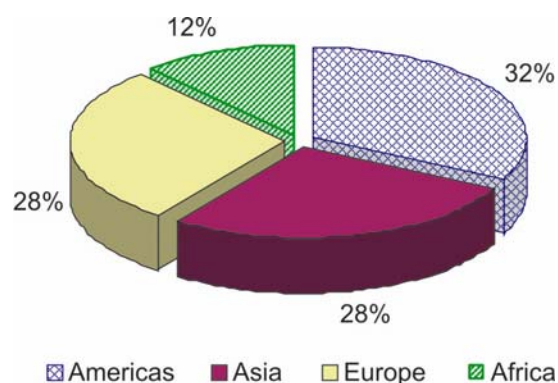


## 2. Intra-regional trends

When one looks more closely at the agreements signed between countries located in the same geographical region (*intra-regional EIAs*), the following picture emerges (figure III.4):

- Countries in the Americas have signed the largest number of intra-regional EIAs, with 49 treaties (six before 1990). The investment-related economic integration process in America had an early start, notably with the creation of the Andean Pact and CARICOM. However, it was mainly after the conclusion of NAFTA that American EIAs began to proliferate. Apart from the formation, expansion and consolidation of several main sub-regional groups,<sup>51</sup> together with their major amendments and additional protocols, and one EIA signed between two sub-regional groups,<sup>52</sup> 40% of all American EIAs have been signed between two individual countries, and another 30% between a group and a third country (e.g. the CARICOM-Costa Rica Free Trade Agreement).

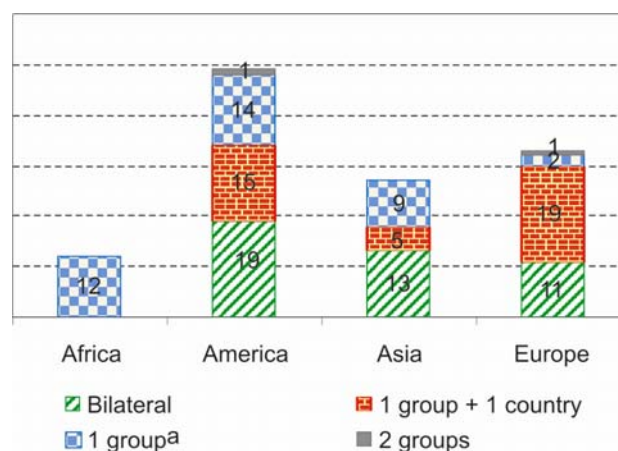
**Figure III.3 Total EIAs concluded by region, June 2005**



Source: UNCTAD.

- European countries now account for the second largest number of intra-regional EIAs, with 33 such agreements. In addition to the three main European regional economic integration agreements (EC, EFTA and the EEA), 33% of these EIAs have been signed between two European countries, typically between two South-Eastern European countries. The remaining 57% involve the European Community (16) or the EFTA countries (three) with another European country. As noted before, a number of the earlier agreements signed by the European Community with other European countries, as well as between two European countries, have been replaced over the years by new generation of agreements as part of a process of wider and closer European integration.<sup>53</sup>

**Figure III.4. Intra-regional EIAs concluded, by region, June 2005**



Source: UNCTAD.

<sup>a</sup> Including major revisions of and protocols on pre-existing EIAs.

<sup>51</sup> Notable examples of American subregional groups are MERCOSUR, NAFTA, the Andean Community, CARICOM and the Central American Common Market.

<sup>52</sup> The Framework Agreement for the Creation of a Free Trade Area between the Central American Common Market and MERCOSUR.

<sup>53</sup> Thus, after full accession to the European Community by ten European countries in 2004, the EC association agreements with Slovenia (1996), Estonia (1995), Latvia (1995), Lithuania (1995), the Czech Republic (1993), Slovakia (1993), Hungary (1991), Poland (1991), Cyprus (1972) and Malta (1970) became obsolete.

- Asia ranks third in terms of the number of EIAs signed between countries within the region, with 27 treaties (23 since 1990). These figures confirm the perception that traditionally EIAs between Asian countries were not very popular. Until recently, ASEAN was the main engine for intra-Asian investment-related economic integration. Today, new groups are emerging, especially in Southern Asia and the Pacific, although the process of investment integration within them is moving rather cautiously. Of the total 27 Asian EIAs, five involve the creation of a subregional integration group,<sup>54</sup> and four are major revisions or protocols amending or expanding pre-existing EIAs, while about 50 % of all EIAs involve two countries, Australia and Singapore being the countries with the highest number of bilateral agreements within the region. The remaining 18.5% of the agreements have been concluded between a group and a third country.<sup>55</sup> There are no agreements between two Asian groups. As noted, the expansion of EIAs among Asian countries is a recent phenomenon, the region being traditionally more inclined to conclude investment agreements with countries in other regions.
- In contrast, in Africa, intraregional EIAs were most popular among sub-Saharan African countries before 1990.<sup>56</sup> Of the 12 intraregional EIAs signed (including their major revisions and protocols), 50% were concluded before 1990. Through these EIAs the investment-related economic integration in sub-Saharan Africa has proceeded along subregional groups that expanded, regrouped, re-emerged or merged over the years. Interestingly, there are no bilateral EIAs between individual African countries, nor are there EIAs between North African countries. Some EIAs concluded between Northern and sub-Saharan African countries before the 1990s were in the broader context of Arab and Islamic interregional groups (see below). Since the early 1990s, a new wave of regional and subregional African EIAs has emerged, including the African Economic Community, covering most African countries.

### 3. Interregional trends

With respect to EIAs concluded by countries located in different geographical regions (*interregional EIAs*), the largest number of agreements have been concluded between European and Asian countries, with approximately 30% of the total, most of which have been concluded between the European Union or EFTA and individual Asian countries and groups (figures III.5 and III.6). These figures are not surprising given the size of the entire Asian region. In second place rank the agreements signed between American and Asian countries, with 25% of all interregional EIAs, the majority of which are between two countries (figures III.5 and III.7). These include 18 bilateral agreements recently signed by the United States. In third place are the agreements between European and American countries and groups, with 14.5% of the total (figures III.5 and III.8). Countries in America have signed 11 agreements with African countries, while European countries have signed eight, including the Cotonou Agreement, which in fact

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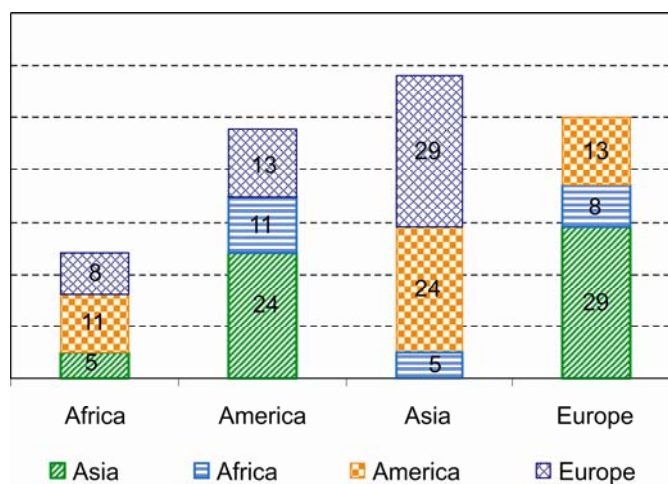
<sup>54</sup> The Association of Southeast Asian Nations (ASEAN), the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC), the Gulf Cooperation Council (GCC), the South Asian Association for Regional Cooperation (SAARC) and the South Pacific Regional Trade and Economic Cooperation Agreement (SPARTECA).

<sup>55</sup> For example, the ASEAN-China Framework Agreement and the Gulf Cooperation Council-Lebanon Agreement Establishing a Free Trade Area

<sup>56</sup> The Treaty Establishing the Economic Community of West African States (ECOWAS) and the Common Convention on Investments in the States of the Customs and Economic Union of Central Africa (UDEAC or CEMAC) are examples.

involves also the Pacific and Caribbean subregions (figures III.5, III.9 and III.10). Furthermore, the EC has recently embarked on the negotiation of reciprocal economic partnership agreements with the Central African Economic and Monetary Community (CEMAC), the Economic Community of West African States (ECOWAS), the East and South African States (ESA) and the Southern Africa Development Commission (SADC), which are intended to replace the non-reciprocal Cotonou system. EFTA is also negotiating an interregional EIIA with SACU. EIAs between Asia and Africa consist of agreements among Arab and Islamic countries. The Arab and Islamic countries, two groups of countries spread over Asia and Africa but with a clearly defined cultural affinity, signed five agreements among themselves, all of them before 1990.

**Figure III.5. Distribution of interregional EIAs, June 2005<sup>a</sup>**



Source: UNCTAD.

<sup>a</sup> The EC-ACP agreement, which covers more than two regions, was counted as an Africa-Europe EIIA.

Some interregional EIAs span over more than two regions. One is the Cotonou Agreement signed by the EC with a group of African, Pacific and Caribbean countries. Other examples include the Mediterranean Initiative launched in 1995 aimed at creating a free trade area by 2010 between the EC and its Southern Mediterranean neighboring countries (covering most North African and Middle Eastern countries) and the Energy Charter Treaty with members from Asia, America and Europe.

#### 4. New trends of selected countries

With regard to recent EIIA activity by individual countries, several new trends are also noteworthy. One is the recent conversion of the United States to bilateral reciprocal preferential EIAs, which, with the exception of earlier FTAs with Canada, Israel and NAFTA, that country had avoided in the past, preferring instead to focus on the MFN-based multilateral approach. Since 2002, the United States has signed bilateral EIAs with countries in various regions, including 14 framework agreements on trade and investment relations<sup>57</sup> and seven free trade agreements.<sup>58</sup> Also, negotiations are under way with five additional countries and groups.<sup>59</sup> The difficulties encountered in the negotiations of the FTAA and the Cancún Ministerial Conference

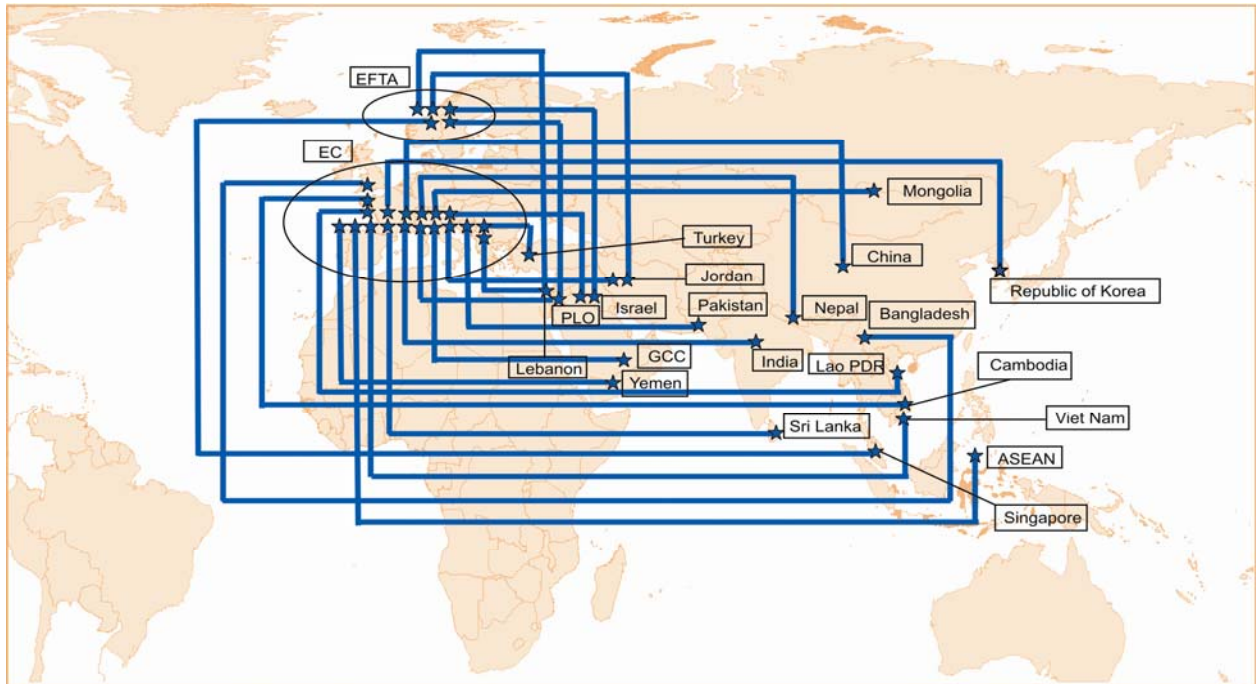
<sup>57</sup> The latest framework agreements concluded by the United States were with Mozambique and Iraq on 21 June and 11 July 2005, respectively, just a few days after the cut-off date for inclusion in the list of EIAs reviewed in this study.

<sup>58</sup> Since 2002 the United States has concluded free trade agreements with Australia, Bahrain, Central America and the Dominican Republic, Chile, the Lao People's Democratic Republic, Morocco and Singapore.

<sup>59</sup> Colombia, Ecuador, Panama, Peru, the Southern African Customs Union (SACU) and Thailand, while other EIAs are under consideration (Bolivia, Egypt, New Zealand, Pakistan, Philippines, Republic of Korea, Sri Lanka, and Taiwan Province of China) (World Bank, 2005, pp. 32-33).

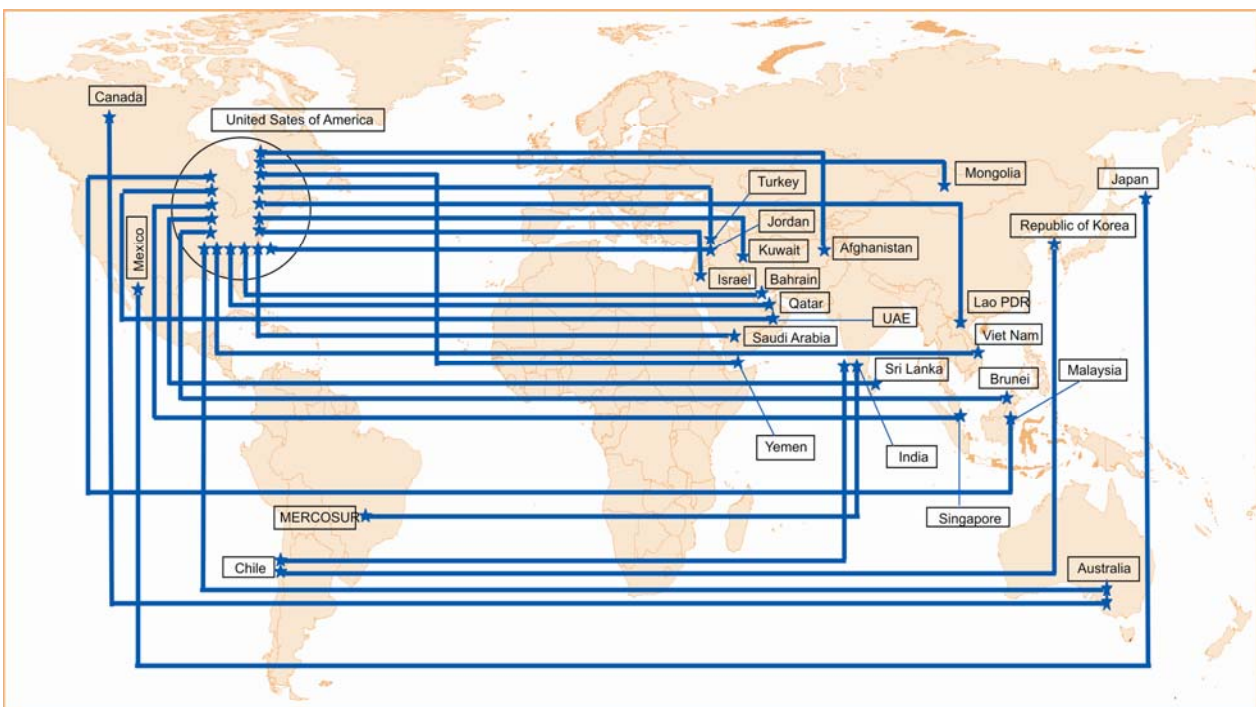
of the WTO may have played a role in this new move by the United States. Efforts are also under way to establish a Middle East Free Trade Area by 2013.<sup>60</sup>

**Figure III.6. Interregional EIAs between Asia and Europe, June 2005**



Source: UNCTAD.

**Figure III.7. Interregional EIAs between America and Asia, June 2005**

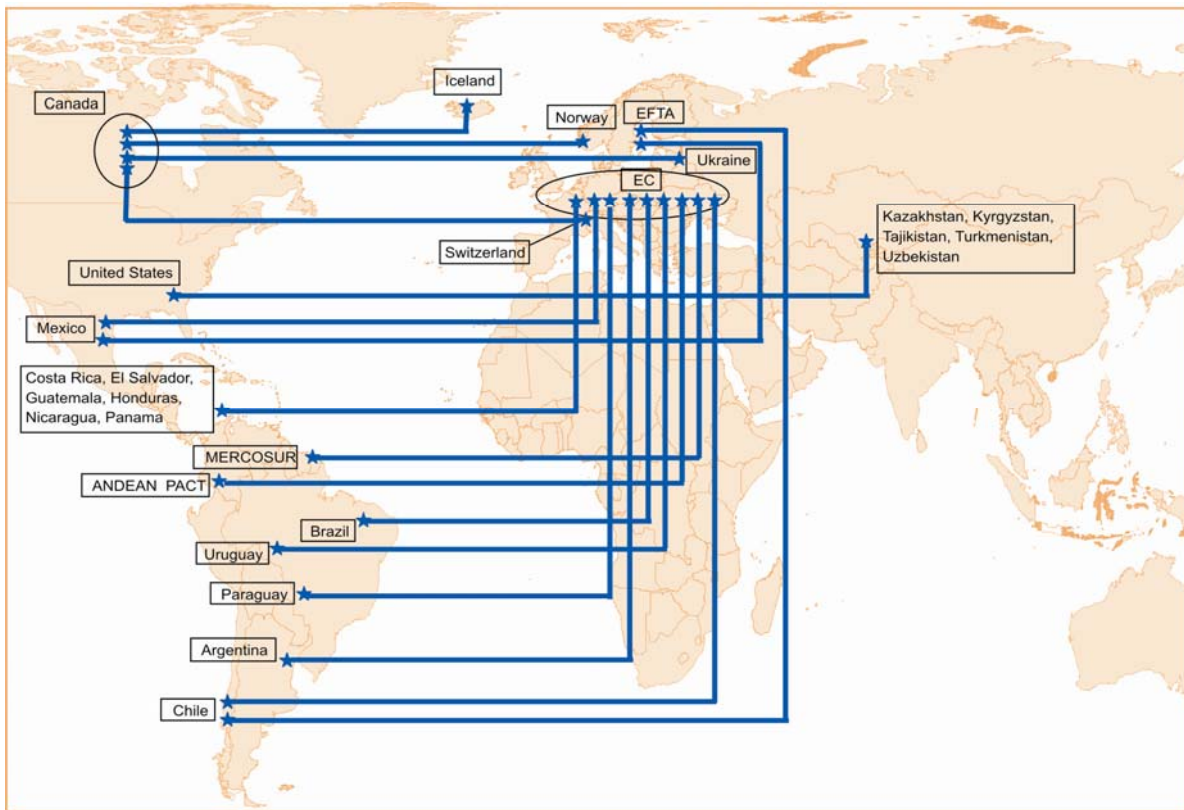


Source: UNCTAD.

<sup>60</sup> In addition to the EIAs already concluded with countries in that area, negotiations with the United Arab Emirates and Oman have already started.

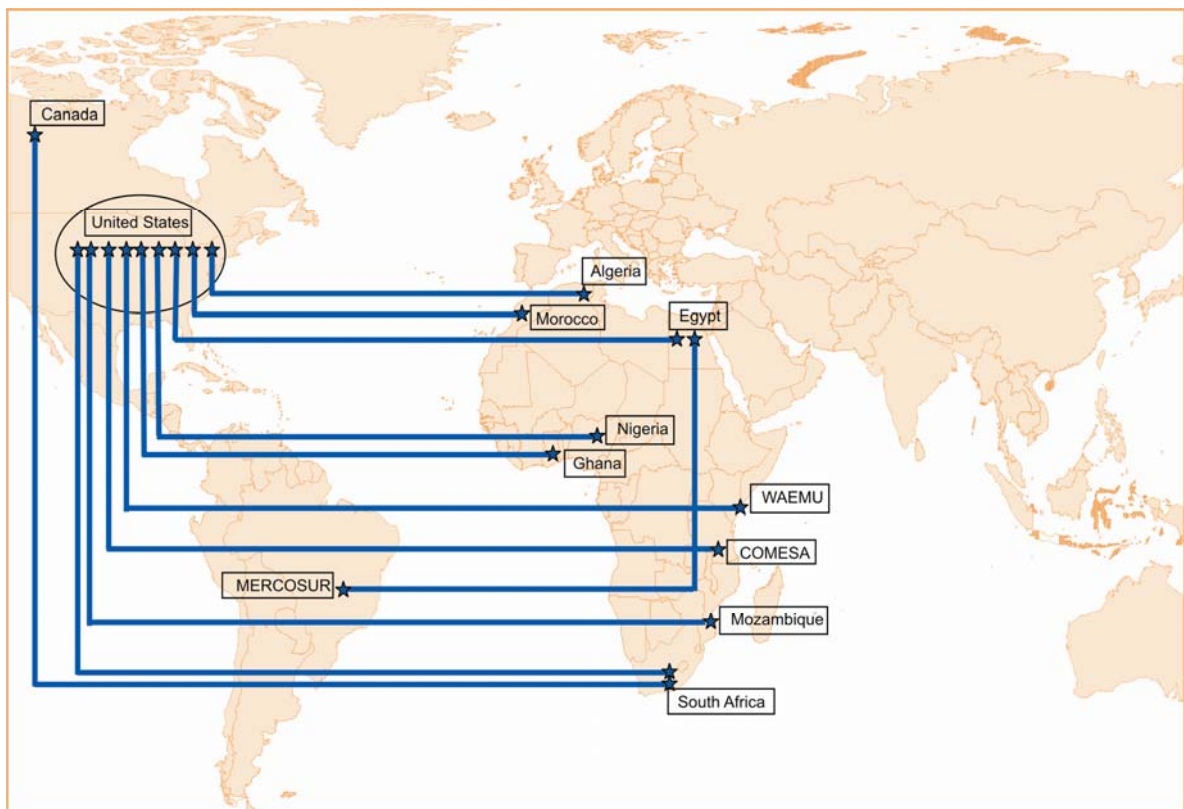


Figure III.8. Interregional EIAs between America and Europe, June 2005



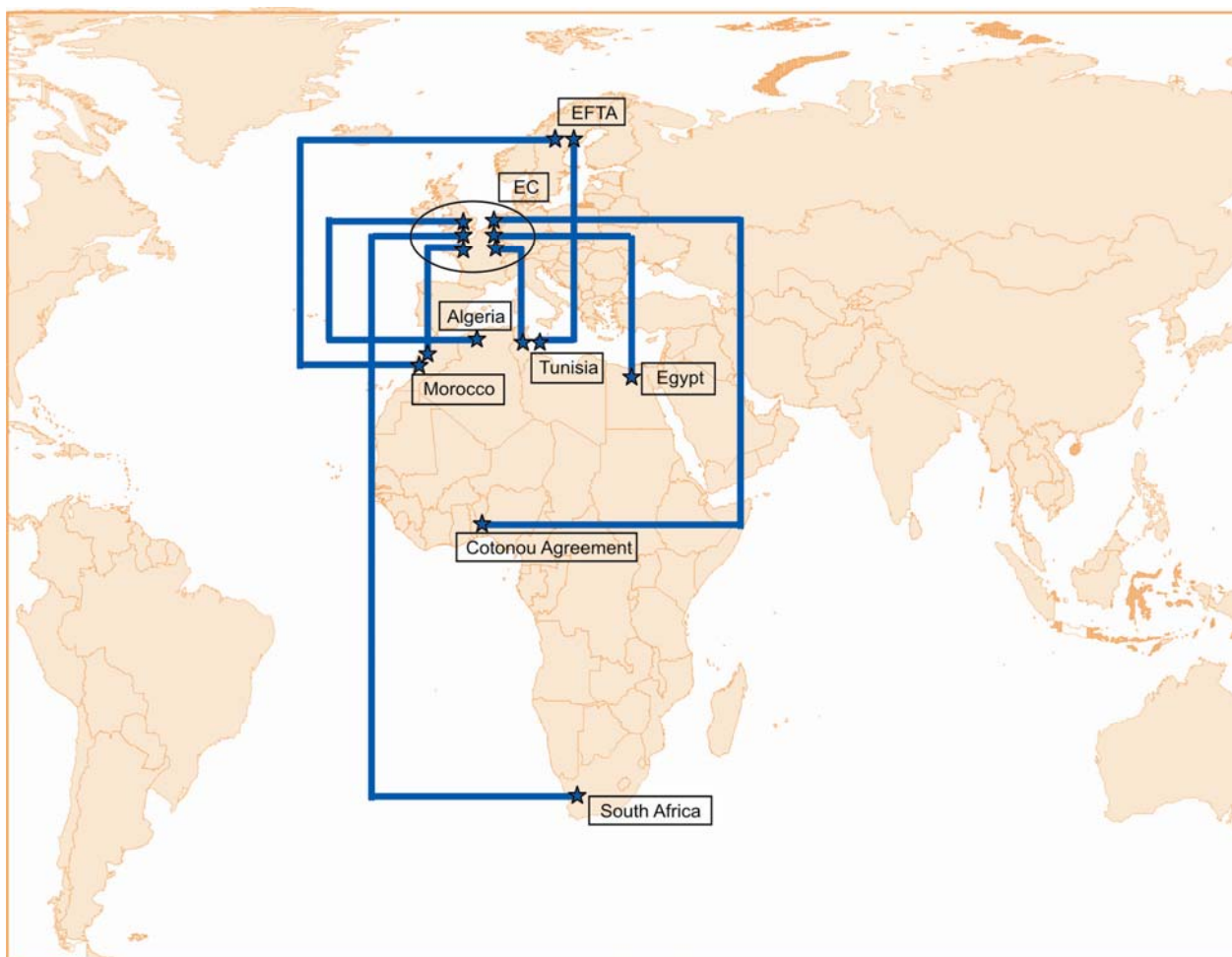
Source: UNCTAD.

Figure III.9. Interregional EIAs between Africa and America, June 2005



Source: UNCTAD.

Figure III.10. Interregional EIAs between Africa and Europe, June 2005



Source: UNCTAD.

Japan is another major developed country that has recently embraced this strategy and started to negotiate bilateral EIAs both within the Asian region and interregionally. After years of pursuing an open-door trade and investment liberalization under APEC's best-practice approach (based on MFN treatment), Japan signed its first EIA with Singapore in 2002. This agreement was followed a year later by the Trade and Economic Framework Agreement with Australia and the Framework for Comprehensive Economic Partnership with ASEAN, and, in 2004 by the Economic Partnership Agreement with Mexico. Negotiations have also begun with Canada, Chile and the Republic of Korea, while talks are under way with three individual members of ASEAN (Malaysia, the Philippines and Thailand) as well as with the ASEAN group. Some preliminary moves are also taking place on a possible EIA *à trois* between China, Japan and the Republic of Korea. Australia, as well as some advanced developing countries, such as Chile, China, the Republic of Korea, India, Mexico and Singapore, has also become very active in the pursuit of bilateral EIAs with partners in several regions.<sup>61</sup>

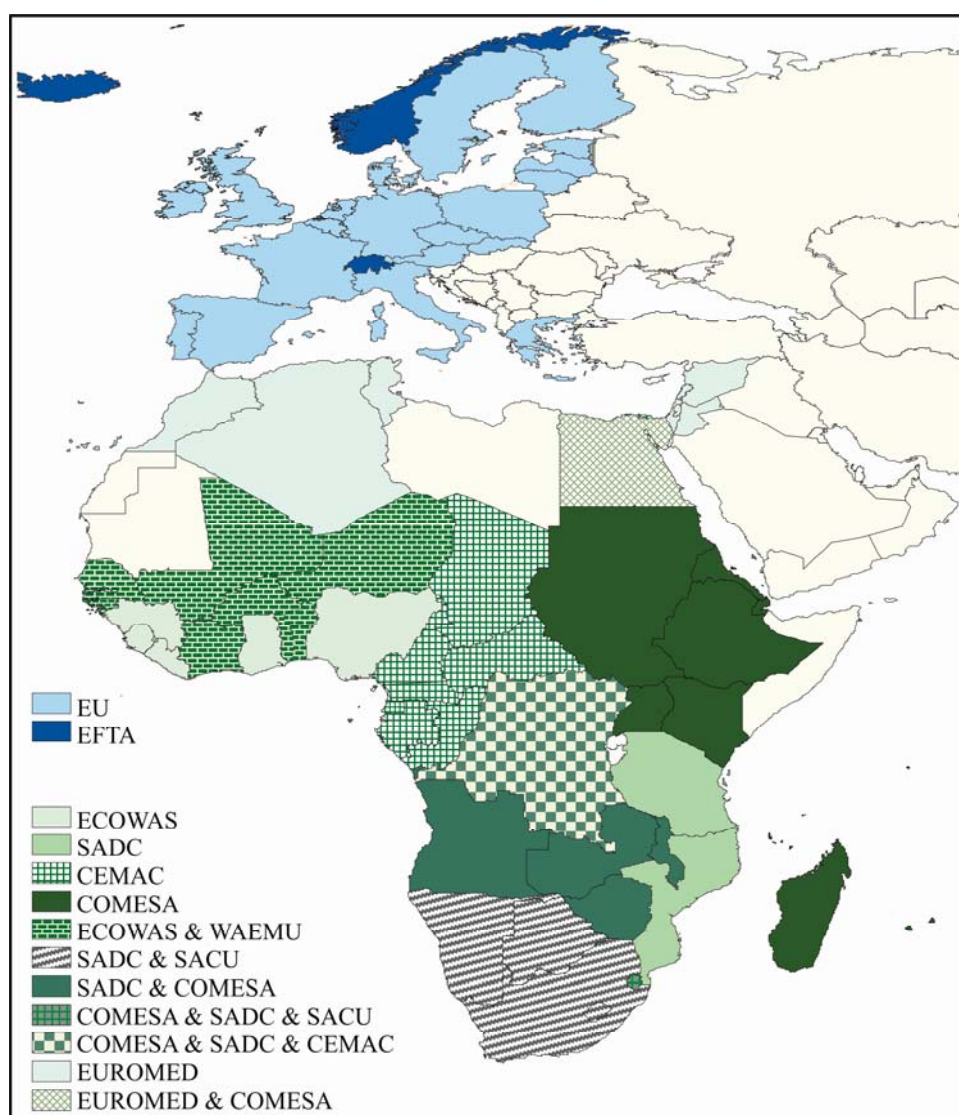
\* \* \* \* \*

<sup>61</sup> In addition to its six EIAs already signed, Singapore is currently negotiating EIAs with 10 other developing countries.



The foregoing description of the present EIIA network suggests a universe in constant expansion and change, formed by variable constellations that are linked by overlapping membership and complex interactions. It is still too early, however, to identify a dominant pattern in this constant reconfiguration of the EIIA network, as many forces are in play. Thus, while it appears that there is a tendency towards consolidation and expansion of investment-related economic integration around several geographically close groups through the attraction of new members from neighbouring areas (*circular integration*) (figures III.11, III.12 and III.13), other forces are propelling countries to diversify their EIIA partners through the proliferation of bilateral EIAs that link geographically disperse countries (*linear integration*). Of course, the basic motivations behind these variable tendencies are similar. Not the least among them is the “domino effect” caused by the increase in EIAs, as countries from all parts of the world struggle to both participate and compete in an increasingly global world economy.

**Figure III.11. Areas of EIIA integration through subregional groups within and between Africa and Europe<sup>a b</sup>**

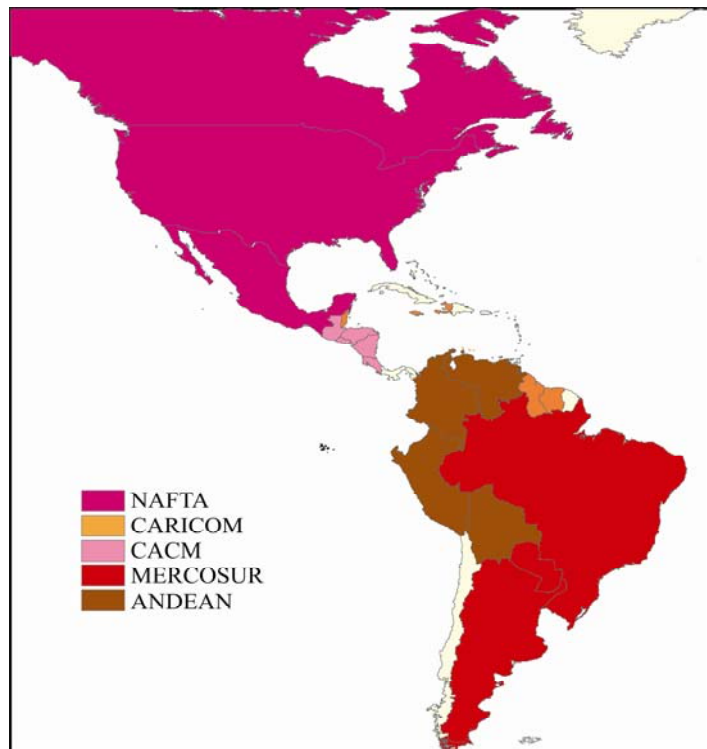


Source: UNCTAD.

<sup>a</sup> This figure does not show EIAs between two countries or between one group and a third country.

<sup>b</sup> The European Economic Area, the African Economic Union and the ACP-EC agreement are not reflected in this figure.

**Figure III.12. Areas of EIIA integration through subregional groups within America<sup>a b</sup>**

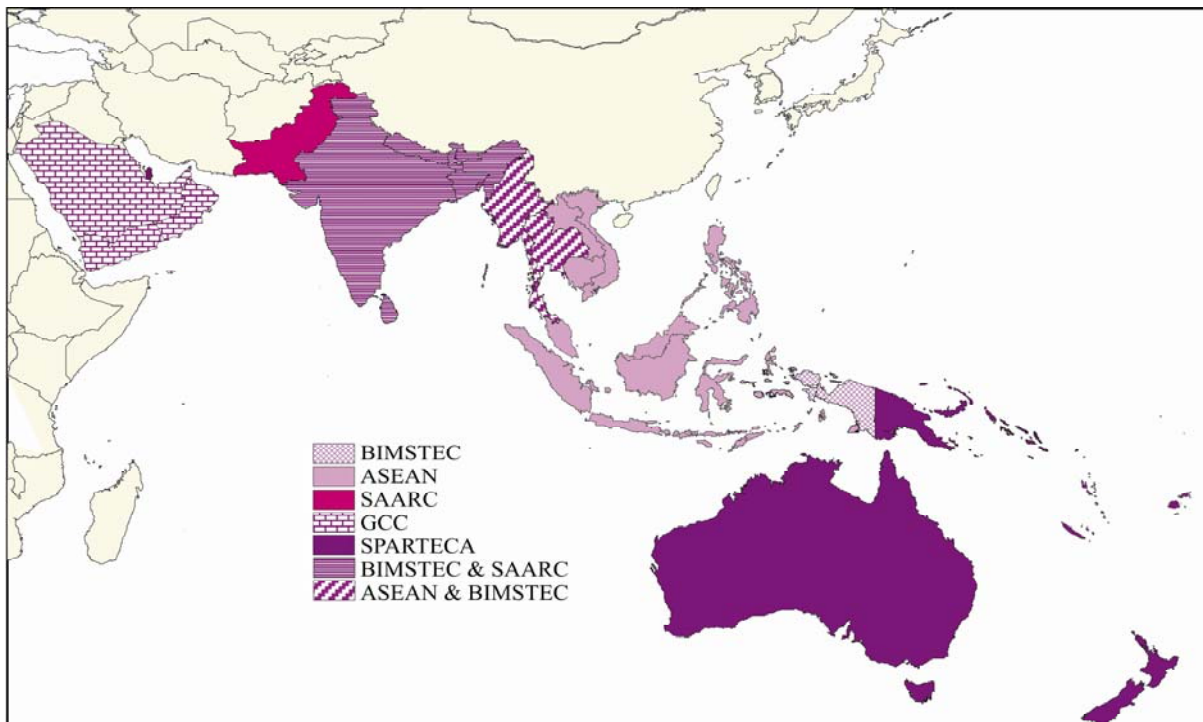


Source: UNCTAD.

<sup>a</sup> This figure does not show EIAs between two countries or between one group and a third country.

<sup>b</sup> The Latin American Integration Association is not reflected in this figure.

**Figure III.13. Areas of EIIA integration through subregional groups within Asia<sup>a/</sup>**



Source: UNCTAD.

<sup>a</sup> This figure does not show EIAs between two countries or between one group and a third country.

## B. Global Patterns in EIIA Approaches to Investment

As noted in the Introduction, one of the principal objectives behind the adoption of EIAs is to facilitate investment flows as a means of enhancing the process of economic integration between their parties. To achieve this goal, EIAs undertake commitments to liberalize investment, to provide legal protection and guarantees, to promote investment or to regulate investment; or they combine several or all of these elements. Unlike BITs — the other major type of investment agreement — EIAs do not have a uniform structure or a consistent approach to investment.<sup>62</sup> Rather, their approach to investment varies significantly in terms of the coverage of issues, the depth of the commitments they make on these issues, and the way in which they deal with investment from third parties. As in the case of BITs, however, the structure and the approach to investment in many EIAs have been influenced by previous EIAs and by other investment agreements, notably the BITs themselves, and WTO agreements. Thus, the existing universe of EIAs may be classified according to a number of “models” or patterns that have been followed more or less closely by these agreements through an interactive process that reflects the economic and political conditions of the day, the purposes and priorities of the parties involved, and the preferences of each region.

### 1. Coverage of Investment Issues

A first approximation to the classification of EIAs in relation to their coverage of investment issues may relate to the purpose of the investment provisions. On this basis, EIAs can be grouped according to four main categories of purposes: cooperation, liberalization, liberalization and protection, and protection and promotion. In practice, however, EIAs are often a combination of several approaches. The range of investment issues addressed under each category may also vary considerably (table III.1). Moreover, as noted earlier, the approach of EIAs in relation to investment does not necessarily parallel their approach to trade or other transactions. Accordingly, the following typology of EIAs relates exclusively to their investment provisions.

#### a. Investment cooperation EIAs

This group encompasses agreements containing general mandates to engage in various forms of present or future cooperation aimed at promoting, protecting and/or liberalizing investment. It is also common for these agreements to set up a consultative committee or similar institutional arrangement between the parties to give specificity and effect to the cooperation mandates. On the basis of their specific aims, two main types of EIAs may be discerned.

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<sup>62</sup> The two basic approaches to BITs, represented by the traditional European model and the United States model, have remained in use for more than two decades, although these models have become significantly more elaborate in recent years.

Table III.1. Key investment-related issues in EIAs

Agreement	Scope Definition of investment/ investor	Liberalization			Legal protection					Cooperation			
		Admission Rights of establishment	Transfer of funds	Performance requirements	Treatment after entry		FET*	Expropriation	IPR**	Dispute settlement		Promotion	Framework / future negotiation
					NT*	MFN*				State-State	Investor-State		
<b>North-North</b>													
EFTA (2001)	•	•	•		•				•	•			
Australia-United States (2003)	•	•	•	•	•	•	•	•	•	•			
Australia-Japan (2003)											•	•	
<b>North-South</b>													
NAFTA (1994)	•	•	•	•	•	•	•	•	•	•	•		
EC- Sri Lanka (1994)									•		•	•	
Canada-Chile (1996)	•	•	•	•	•	•	•	•	•	•	•		
EFTA-Morocco (1997)			•						•	•	•	•	
Canada-South Africa (1998)											•	•	
EC-Egypt (1999)			•						•	•	•	•	
EC- South Africa (1999)			•						•		•	•	
United States-Ghana (1999)												•	
EC-ACP (2000)									•	•	•	•	
United States-Viet Nam (2000)	•	•	•		•	•	•	•	•	•	•	•	
Canada-Costa Rica (2001) <sup>1</sup>											•	•	
Japan-Singapore (2002)	•	•	•	•	•		•	•	•	•	•		
EFTA-Singapore (2002)	•	•	•		•	•	•	•	•	•	•		
Australia-China (2003)											•	•	
EFTA-Chile (2003)	•	•	•						•		•		
United States-Chile (2003)	•	•	•	•	•	•	•	•	•	•	•		
CAFTA (2004)	•	•	•	•	•	•	•	•	•	•	•		
Australia-Thailand (2004)	•	•	•		•	•	•	•	•	•	•		
EFTA-Lebanon (2004)			•						•	•	•	•	
United States-Qatar (2004)												•	
United States-Morocco (2004)	•	•	•	•	•	•	•	•	•	•	•		
<b>South-South</b>													
Investment and Free Movement of Arab Capital Among Arab Countries (1970)			•		•	•		•				•	
COMESA (1993)	•	•	•				•	•		•			
MERCOSUR Colonia Protocol (1994)	•	•	•	•	•	•	•	•	•	•	•		
Group of 3 (1994) <sup>2</sup>	•		•	•	•	•	•	•	•	•	•		
ASEAN Investment Area (1998)	•	•			•	•				•		•	
CARICOM (1973/2001)	•	•	•		•	•			•	•	•	•	
India-Thailand (2003)										•	•	•	
Chile-Republic of Korea (2003)	•	•	•	•	•	•	•	•	•	•	•		
ASEAN-China (2003)											•	•	
BIMSTEC Free Trade Area (2004)										•	•	•	
Uruguay-Mexico (2004)	•	•	•	•	•	•	•	•	•	•	•		
Taiwan Province of China -Panama (2004)	•	•	•	•	•	•	•	•	•	•	•		
CARICOM-Costa Rica (2004)	•	•	•	•	•	•	•	•	•	•	•		
<b>North- Economies in Transition</b>													
EC-Bulgaria (1993)	•	•	•		•	•			•	•	•	•	
EC-Russia (1994)	•	•	•		•	•			•	•	•	•	
EFTA-Croatia (2001)			•						•	•		•	
United States-Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan (2004)											•	•	

Source: UNCTAD.

\* NT = National treatment, MFN = Most favoured nation treatment, FET = Fair and equitable treatment, IPR = Intellectual property rights.

<sup>1</sup> The Parties note the existence of a BIT between Canada and Costa Rica.

<sup>2</sup> Group of 3: Colombia-Venezuela-Mexico.

The first type of cooperation EIIA consists of agreements that address *investment promotion through cooperation*. The framework cooperation and partnership agreements signed by the EC with a number of Asian and Latin American countries and groups of countries,<sup>63</sup> as well as the Partnership Agreement between the EC and APC countries, are examples of this approach, as are also the framework agreements concerning trade and investment relations signed by the United States with a number of African and Middle East countries, and, lately, with the former Soviet Republics of Central Asia, the arrangements on trade and economic cooperation signed by Canada with countries in various regions, and, among the most recent EIAs, the Trade and Economic Framework Agreement between Australia and China. These agreements often spell out specific promotional measures that should be taken by the parties (or by some of them), including in particular exchange of information. In some cases, the cooperation mandate includes identification, analysis and gradual elimination of obstacles to investment flows. In other cases, the parties (through the consultative committee) agree to hold consultations on specific investment (and trade) matters and to identify agreements appropriate for negotiation. In still other cases, the parties are specifically encouraged to conclude bilateral protection and promotion agreements. The investment promotion provisions in some cooperation EIAs are part of a broader framework for economic cooperation addressing a variety of sectors and areas of economic activity. Countries tend to negotiate these types of investment cooperation provisions when the field is not yet ready to start negotiations for a full economic integration agreement. Consequently, they tend to involve countries which are geographically dispersed and foresee a relatively low level of economic integration between them in the short term. Often these agreements involve countries whose level of economic and social development differ substantially. In these cases, they tend to be tailored to the characteristics of the developing country partner and involve technical assistance.

The second type of cooperation EIIA consists of agreements that set up a *framework for future negotiations aimed at liberalizing and/or protecting investment flows*. This approach is found in, for example, the Euro-Mediterranean agreements signed by the EC with countries in North Africa and the Middle East. These agreements contain a mandate to widen the scope of the agreement to cover right of establishment for firms and the liberalization of services at a future date (article 31(1)). A follow-up clause provides for assessment of the achievement of these objectives after five years (article 31 (2 and 3)). Another example of this approach is the Partnership Agreement between the EC and the ACP countries, which provides for the negotiation of reciprocal economic partnership agreements between the EC and regional ACP groups in the near future. The Cotonou Agreement mandate goes on to specify what the main characteristics and purposes of these economic partnership agreements should be: they should aim at gradually liberalizing trade in services and should spell out investment protection standards. The recently adopted Framework Agreement between ASEAN and China is another example of this approach. It commits the parties to enter into negotiations in order to progressively liberalize their investment regimes and improve the transparency of investment rules. A similar approach is found in the South Asian Free Trade Agreement, and in the BIMSTEC FTA. In the latter arrangement the parties agree to negotiate expeditiously in order to establish a BIMST-EC FTA through *inter alia* progressive liberalization of trade in services with

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<sup>63</sup> Examples include the Cooperation Agreement between the Economic Community and its Member States and the Member Countries of ASEAN, the Political Dialogue and Cooperation Agreement between the European Community and the Republics of Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama, and the Cooperation Agreement between the European Community and its Member States and the States of the Gulf Cooperation Council.



substantial sectoral coverage, and the establishment of an open and competitive investment regime that facilitates and promotes investments within the BIMST-EC FTA. The mandates in most FTAs concluded by the EFTA countries, as well as the bilateral FTAs signed by Southern European and CIS countries between themselves, are less concrete: the parties recognize the importance of investment and services and agree “to cooperate” with the aim of achieving progressive liberalization and mutual opening of their markets for investment.

### **b. Investment liberalization EIAs**

Although the majority of EIAs contain specific obligations regarding the liberalization of investment between the parties as a means to complement trade liberalization and achieve deeper levels of market integration, certain types of EIAs focus mainly, or almost entirely, on liberalization. The scope and range of the liberalization issues covered may vary significantly among EIAs. Several patterns can be discerned in this respect.

At one end of the spectrum, some EIAs contain specific liberalization obligations covering a wide range of investment issues, including typically issues of investment entry, establishment and operation (e.g. post-establishment national treatment), transfer of funds and, in some cases, entry of managerial personnel, as well as trade in services and competition policy. Some liberalization EIAs deal with intellectual property protection as a complement to their liberalization provisions. Liberalization commitments are typically subject to exceptions and are often given effect through a more or less protracted process of gradual elimination of existing restrictive measures (see chapter IV.B.2). EIAs signed between developed countries often fall into this category of EIA.<sup>64</sup> With respect to EIAs between developing countries, the CARICOM Revised Treaty and the Framework Agreement on the ASEAN Investment Area are also close to this model. The latter provides for a list of temporary exclusions from entry, establishment and national treatment to be phased out by a particular date. Also falling under this model are the Europe agreements of association signed by the EC with Central and South- East European countries. They provide for progressive liberalization of investment and trade in services to be completed in several stages on the basis of detailed provisions, including on rights of establishment, non-discrimination, post-establishment national and MFN treatment, admission of personnel, transfer of funds and competition. (As noted earlier, EC association agreements are often signed as steps towards full EC integration.) The partnership and cooperation agreements between the EC and Eastern European countries cover similar liberalization issues, but the rights granted on these issues are more limited (see chapter IV.B).

The range of specific liberalization issues covered in other types of investment liberalization EIAs is narrower. For example, the Euro-Mediterranean agreements signed by the EC with countries in North Africa and the Middle East contain a prohibition on future restrictions on movements of capital and current payments, with some exceptions. (As noted earlier, these agreements do not grant rights of entry and establishment but commit the parties to provide such rights at a future date.) In addition, these two types of EC liberalization agreements, like their association counterparts, provide for intellectual property protection and protection against anticompetitive practices.

Another yet more limited EIA investment liberalization model, but with potentially far-reaching effects, consists of agreements that contain only general liberalization commitments in

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<sup>64</sup> For example, the EC, EFTA and the European Free Trade Area, and the OECD Codes of Liberalization.



principle but provide for the development of these commitments in the future. This model is followed in some recent African EIAs, for example the Agreement Establishing the African Economic Community. It includes among its objectives the removal of obstacles to the free movement of persons, goods, services and capital and to the right of residence and establishment, to be provided in stages. The agreement envisages the full establishment of these freedoms in the sixth stage of its implementation. In the meanwhile, free movement of capital is to be implemented in accordance with a timetable, and measures to achieve the right of establishment are to be developed in a protocol. The Revised ECOWAS Treaty follows a similar approach. Even less concrete in terms of the specification of its liberalization commitments is the Unified Agreement between the Countries of the Gulf Cooperation Council.

Yet another type of liberalization EIA focuses solely or mainly on the liberalization of services. Examples are the ASEAN Framework Agreement on Services, the Protocol of Montevideo on Trade in Services in MERCOSUR and the Andean Community General Framework of Principles and Rules for Liberalizing Trade in Services (Commission Decision 439).

Stand-alone services liberalization agreements are usually a part of a broader integration framework encompassing trade in goods and, often, investment. A different model is that followed by the recent EIAs signed by the EC with Mexico and Chile and by EFTA with Chile, Mexico and Singapore. These agreements combine specific liberalization commitments in a number of services sectors with general commitments to liberalize investment at a future date (see chapter IV for further details).

### **c. Investment liberalization and protection EIAs**

Another set of EIAs addresses both liberalization and protection of investment. A leading example of this model is the Investment Chapter (Chapter XI) of the North American Free Trade Agreement (NAFTA). Many EIAs signed between American countries follow the NAFTA quite closely in substance. With respect to liberalizing measures, these agreements typically guarantee national and MFN treatment on entry, subject to a list of exceptions, grant free transfer of payments related to an investment, prohibit certain performance requirements and place limits on restrictions on the investors' choice of managerial personnel of their choice. With respect to protection measures, they guarantee national and MFN treatment after establishment, subject to specified exceptions, guarantee minimum standards of treatment, including fair and equitable treatment, full protection and security, and also protection against unlawful expropriation. These commitments are complemented with provisions for investor-to-State arbitration of investment disputes. Other chapters address liberalization of trade in services and competition policy and protect intellectual property rights. The Latin American agreements sometimes depart from the NAFTA model in several respects, notably in the inclusion of a prohibition on the extraterritorial application of laws and, in some cases, in the absence of a right of establishment or an asset-based definition of investment (see chapter IV).

Recent EIAs following the NAFTA model sometimes go further than NAFTA in terms of the coverage of investment and investment-related issues. Included in this group are a number of bilateral (both regional and interregional) EIAs concluded by countries in the Americas and Asia that are, for the most part, more comprehensive and detailed than prior NAFTA-type EIAs. They seek to deal in very extensive ways with trade in services as well as investment. Separate

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chapters may appear on topics such as competition policy, government procurement, intellectual property rights, labour, the environment, trade in special service sectors such as telecommunications and financial services, temporary entry for business persons, and transparency. Among the countries concluding these agreements are Australia, Chile, Japan, the Republic of Korea, Mexico, Morocco, Singapore and the United States (box III.1).

Yet other EIAs that deal with liberalization and protection of investment do not go as far as NAFTA in their coverage of issues. An example is the MERCOSUR Protocol of Colonia on Reciprocal Promotion and Protection of Investments within MERCOSUR. The Colonia Protocol is closer to the United States BIT model than to NAFTA.

Belonging to this group are also earlier agreements signed between African countries and by Arab and Islamic countries that provide for a combination of limited protection and liberalization standards. They authorize the host State to grant preferences to investors of member countries meeting certain conditions. These preferences sometimes include a limited right of establishment and freedom of movement of persons. They also typically contain a few provisions on investment protection, most commonly a guarantee of compensation for expropriation, but in some cases a right of free transfers or even a right to investor-State dispute resolution.

**Box III. 1. The investment-related provisions in the Agreement  
Between Japan and Singapore for a New-Age Economic Partnership**

The Economic Partnership Agreement between Japan and Singapore contains an investment chapter that follows the NAFTA model but is more comprehensive and detailed than earlier NAFTA-type EIAs. The investment chapter includes,

- A broad, asset-based definition of investment;
- A general guarantee of national treatment, both pre-establishment and post-establishment, subject to exceptions set forth in an annex;
- A guarantee of national treatment with respect to access to courts and administrative tribunals both in pursuit and defense of investors rights;
- A prohibition on certain performance requirements subject to exceptions set forth in an annex;
- A guarantee of fair and equitable treatment and full protection and security;
- A guarantee of compensation for expropriation;
- A guarantee with respect to repurchase of leases by the host government;
- A guarantee of national treatment with respect to the payment of compensation for war or civil disturbance;
- A guarantee of free transfer of payments relating to investments;
- A temporary safeguard with respect to cross border capital transactions;
- Investor-to-state dispute resolution;
- A general exceptions clause;
- A prudential measures clause;
- A limitation on national treatment with respect to intellectual property rights in accordance with the WTO TRIPS Agreement;
- A limitation on taxation measures as a form of expropriation;
- Establishment of a “Joint Committee on Investment” to monitor the implementation of the agreement;
- An extension of the observance of agreement to local governments and non-governmental bodies;
- A guarantee of MFN treatment.

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**Box III. 1. The investment-related provisions in the Agreement  
Between Japan and Singapore for a New-Age Economic Partnership (concluded)**

The agreement includes as well a chapter on trade in services with GATS-like provisions on,

- Market access commitments and national treatment in sectors where commitments have been made;
- A requirement that domestic regulation of trade in services be reasonable, objective and impartial;
- Judicial review of decisions affecting trade in services; and
- Restrictions on anticompetitive practices.

Further the agreement includes a chapter on movement of natural persons which

- Allows parties to make specific commitments for entry of investors; and
- Establishes a committee on mutual recognition of professional qualifications.

Also included in the agreement are separate chapters that deal respectively with

- Intellectual property rights;
- Restrictive business practices;
- Financial services;
- Science and technology;
- Promotion of trade and investment;
- State-to-state dispute resolution.

*Source:* UNCTAD.

#### **d. Investment protection and promotion EIAs**

Some EIAs follow the traditional European BIT pattern which provides for standards of treatment and protection of investment only after entry. An example is the ASEAN Agreement on the Reciprocal Promotion and Protection of Investments. These agreements typically provide for national treatment, MFN and fair and equitable treatment after entry (the ASEAN Agreement provides only MFN treatment), a guarantee of compensation upon expropriation and the right to free transfer of funds, and include provisions on the settlement of investment disputes between investors and host countries. However, the parties reserve the right to admit investments from the other members in accordance with their national laws. It needs to be noted in this example that the ASEAN promotion and protection agreement is part of a broader integration framework among the members of the ASEAN, encompassing other agreements that cover issues of liberalization of investment and services. The Energy Charter Treaty as it stands at present, and the Agreement on Promotion, Protection and Guarantee of Investments among Member States of the Organization of the Islamic Conference, are other examples of this model.

Another type of agreement belonging to this category are a number of EIAs that follow the NAFTA model in other respects, and provide for both national treatment and MFN but only after establishment. Accordingly, these agreements do not pursue the liberalization of investment flows but provide for investment protection, including guarantees of non-discrimination after entry. Examples are the free trade agreements between Mexico and Costa Rica, between Mexico and Nicaragua, between Colombia, Venezuela and Mexico and between Central America and the Dominican Republic.

The provisions on promotion in this type of investment protection EIIA, like its BIT counterparts, tend to be rather general and vague, as promotion is expected to come about through the protection standards granted in the agreement intended to minimize political risk. However, some agreements falling into this group contain detailed provisions on promotion. An example is the Mexico-Costa Rica FTA, which *inter alia* specifies various information items to be exchanged with the intention of promoting investments between the parties. Still other agreements combine framework provisions on promotion and some general investment protection standards (e.g. COMESA).

In yet another approach, certain recent agreements call for the conclusion of BITs between the parties as part of their mandate to promote investment (see III.B.1.a).<sup>65</sup> On the other hand, other recent EIAs do not cover investment protection issues for the stated reason that a BIT already exists between the signatories. This is the case with, for example, the Free Trade Agreement between Jordan and the United States and the Free Trade Agreement between Canada and Costa Rica.

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EIAs sometimes pursue more than one purpose and thus combine several of the approaches identified above, in particular by providing for both specific liberalization obligations and cooperation commitments to promote investment flows. This is often the case of agreements between countries at different stages of development, where economic integration cannot be expected to proceed on the basis of liberalization alone, but necessitates additional specific promotional efforts by the Governments involved, including notably exchange of information and technical assistance (typically to be provided by the more developed country or countries). The partnership and cooperation agreements signed by the EC with Central and Eastern European countries, the Cotonou Agreement between the EC and APC countries and the Euro-Mediterranean agreements signed by the EC are examples of EIAs with this hybrid purpose and approach (see above in this section).

Finally, sometimes agreements concluded under a group's integration mandate do not follow a clear pattern or model. This is the case of, for example, the series of economic complementation agreements signed between Latin American countries under the aegis of ALADI. Each individual complementation agreement establishes its own purpose and coverage of investment issues, based on specific needs, which are not necessarily similar to those in other ECAs. As a result, the range and the type of investment issues addressed vary greatly from one agreement to another.

## 2. *Depth of Commitments on Investment*

A second criterion that may be used for distinguishing between different models or patterns of EIAs in relation to investment relates to the *depth* of the investment commitments made in these agreements. The depth of an EIA in relation to investment is determined by the substantive scope of the agreement (e.g. types of investments and investors covered), and by the extent and nature of the commitments made by the parties under specific investment provisions.

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<sup>65</sup> References to the future conclusion of BITs appear in, for example, association agreements and partnership and cooperation agreements signed by the EC with third countries, in the EC-MERCOSUR and EC-Chile agreements, and in Decision No. 2/2001 of the European Union and the Mexico Joint Council of 27 February 2001.

The “depth dimension” of an EIIA, together with the extent of coverage of investment issues (discussed in the preceding section), provides the substantive parameters that best help determine the degree of investment integration afforded by an EIIA. Some indications of different degrees of depth in EIAs were already given in the preceding section in relation to the coverage of investment issues. Thus, as noted before, while many of the so-called liberalization agreements do little more than promise liberalization in the future, other EIAs go much further in the number of topics covered and the level of detail. Other disciplines on investment also tend to be more rigorous in some EIAs than in others. The actual picture, however, is more complex than these rough classifications may suggest, as it impinges upon the formulation of specific investment provisions as well as the interrelations between provisions. These aspects are examined in detail in the next two chapters.

In addition, the depth dimension of an EIIA with respect to investment is further determined by the manner and extent to which the commitments contained in its investment provisions are implemented. Agreements that contain similar types of liberalization, protection or promotion commitments under their investment provisions may differ greatly when it comes to the level of liberalization or protection or promotion they actually achieve. This study does not discuss implementation issues, nor does it assess the implementation status of EIAs. Nevertheless, it is important to bear this aspect in mind.

### 3. *Treatment of Third Parties*

A third way of differentiating between EIAs in relation to their approach to investment relates to the manner in which different EIAs treat investment from non-parties. This criterion allows one to discern the degree of EIIA integration *vis-à-vis* third countries. As noted earlier, a key characteristic of non-multilateral EIAs is that they provide preferential treatment to investments within the EIIA group, thus introducing a level of asymmetry (i.e. usually less favourable treatment) with respect to investment from countries outside the group. Such preferential treatment granted to EIIA members is typically reinforced by the use of REIO clauses or exceptions to MFN treatment in other agreements signed by any of the members of an EIIA with third countries. Under a REIO clause, a country is not obliged to extend MFN treatment to the other signatories of an investment agreement on the benefits or preferences resulting from its participation in an EIIA. The REIO exception has been broadly used in all types of investment agreements.<sup>66</sup>

At the same time, while EIAs deal principally with investment relations between the parties, a number of these agreements contain provisions explicitly addressing the treatment of third parties. Third-party provisions of EIAs reflect various models or levels of investment integration between members and non-members of EIAs. An example of EIIA provisions reflecting a fairly liberal approach towards third parties in an investment-related area is article 56 (1) and (2) of the European Community Treaty (consolidated text). This article prohibits all restrictions on the movement of capital and payments between member States and third countries. Articles 57 through 60 allow for certain exceptions and safeguards. The combined effect of these provisions and the provisions granting national treatment within the European Community would seem to suggest that not only would most investments from third countries, once established in one European country in accordance with the relevant entry and establishment rules, be allowed

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<sup>66</sup> For an in-depth discussion of the REIO clause and its economic and legal implications, see Karl (1996) and UNCTAD (2005a).

to freely transfer capital and related payments in and out of the Community, but that also third-party firms would be treated in the same manner as EC companies with respect to European Community rules. It should be noted, however, that while the EC has specific provisions establishing an open-door policy towards investment from third countries, it does not go as far as creating a complete Community-wide foreign investment regime. Instead, investment relations with third countries are, for the most part, within the purview of the individual EC members' national law. Hence, asymmetries between third-party investment regimes within the EC may, and often do, exist.

Another type of EIIA that has explicitly adopted a liberal approach towards investment from third parties is the Framework Agreement on the ASEAN Investment Area. This agreement commits the parties to extend full right of establishment and national treatment to investments from third countries by a particular date (2020), that is 10 years after the same rights must be granted to the members of ASEAN.

In yet another approach, the MERCOSUR Protocol on the Promotion and Protection of Investments from Countries not Members of MERCOSUR is entirely dedicated to third-party investment. The Protocol is reminiscent of the traditional European BIT model. It grants ample protection standards for investments from countries outside MERCOSUR after these investments have been in accordance with the national laws of the MERCOSUR member countries, including investor-State settlement of disputes. The Protocol represents a fairly comprehensive common regime of MERCOSUR for third-party investment, thus leaving little room for asymmetrical treatment of non-party investments by individual MERCOSUR countries. However, the Protocol does not go so far as to grant entry and establishment rights to investments from third countries, which are enjoyed by investments from MERCOSUR countries.

Some earlier African EIAs, such as the Community Investment Code of the Economic Community of the Great Lakes countries, grant specific rights to investors of third parties. In particular, they grant the same legal protection as that granted to enterprises with intra-Community capital, including with respect to intellectual property rights, and are not to be subject to discrimination under the law. A right of free transfer of funds is also granted, subject to existing legislation. However, third party investors have to meet certain requirements in order to benefit from the Agreement's preferential regime.

Other earlier agreements, such as the Andean Pact Commission Decision 24 (superseded by Decision 291), make explicit reference to investments from outside the region, with the purpose of restricting and controlling them, and conditioning their participation in the benefits and preferences of the Agreement.

EIIAs that follow the NAFTA model do not address explicitly the treatment of investment originating from non-parties, except for certain disciplines (e.g. on performance requirements) that apply also to third countries. However, investment from third countries might be affected in certain respects by the rules of origin established by these agreements, as these determine the level of local content a product must have in order to qualify for the preferences granted by the agreement.

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#### *4. Distinction between Developed and Developing Country EIAs*

Relatively few of the EIAs considered in this study are solely among developed countries. The principal exceptions are the agreements among the European countries. As has been noted, these agreements strongly emphasize investment liberalization, rather than investment protection or promotion.

The majority of the EIAs considered in this study are between developed countries on the one hand and developing countries or transition economies on the other. For the most part, regional differences predominate among these agreements, with the most important factor usually being the region in which the developed country is located. For example, as described above, European Community agreements with transition economies and developing countries focus on liberalization, limiting anticompetitive behaviour, creating a right of free transfers, protecting intellectual property and/or promoting investment through economic cooperation. The nature of the obligations varies, depending upon the region of the non-European country. A number of agreements between the United States and developing countries, by contrast, include liberalization commitments, but also have strong investment protection provisions.

Nevertheless, a significant and growing number of EIAs among only developing countries also exist. Again regional patterns predominate. For example, many of the agreements among developing countries in the Americas have been very much influenced by NAFTA. Agreements among developing countries in Africa or among the Arab States are also unique. Within Asia, the ASEAN agreements are among the most important EIAs among developing countries, which also are distinct from the agreements among developing countries in the other regions.

Some generalizations can be offered concerning the nature of EIAs among developing countries. First, agreements solely among developing countries are less likely to include specific liberalization commitments than agreements involving developed countries. For example, as noted earlier, some of the EIAs among developing countries in the Americas strongly resemble NAFTA, but omit the right of establishment contained in NAFTA (e.g. FTAs between Colombia, Mexico and Venezuela, between Costa Rica and Mexico, and between Mexico and Nicaragua), although many others have it. Similarly, earlier agreements among African or Arab States often limit their liberalization commitments. This tendency should not be overstated, however. Among the earlier developing country EIAs within the Americas, the CARICOM agreement also has liberalization provisions, as does the MERCOSUR Protocol of Colonia. In Asia the ASEAN Framework Agreement on the Investment Area includes liberalization commitments as well. A number of new developing country regional EIAs in Africa and Asia contain the promise of future liberalization, but it is still too early to assess the extent to which these groups will deliver on that promise. Examples are the African Economic Community and the Revised ECOWAS treaty in Africa and the BIMST-EC treaty in Asia. On the other hand, several recent interregional EIAs between developing countries have specific and far-reaching liberalization commitments, such as the free trade agreement between Chile and the Republic of Korea.

Second, agreements solely among developing countries are more likely to have provisions establishing regional preferences. Regional preferences are typically found in older agreements among African and Arab States as well as Asian and Latin American States. Recent developing country EIAs, however, do not seem to dwell much on preferences (except of course for the fact that the establishment of a non-multilateral EIA is, by its very nature, a preferential regime for

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the parties involved) but on market-oriented approaches to promotion, protection and liberalization of investment.

Third, agreements solely among developing countries tend to have less extensive provisions on the protection of intellectual property rights. Although intellectual property would be protected against host country action in the same way as other forms of investment, agreements solely among developing countries generally do not provide for special protection of intellectual property against private infringement.

Fourth, agreements solely among developing countries are more likely to have provisions for special and differential treatment, based on the level of development of the parties involved. Such provisions appear, for example, in the CARICOM agreement, the Framework Agreement on the ASEAN Investment Area, and Decision 439 of the Commission of the Andean Community Establishing a General Framework of Principles and Rules for Liberalizing Trade in Services in the Andean Community.

Such provisions are not exclusive to agreements solely among developing countries. The Cotonou Agreement also includes such provisions. Their absence from most agreements involving developed countries may be explained by the fact that most of the EIAs involving developed countries have only one developing country as a party, in which case special provisions to take account of different levels of development are unnecessary since the special circumstances of the one developing party can be taken into account directly in fashioning the various substantive provisions.

The distinction between developed and developing countries is a crude one that may mask some noteworthy trends. For example, as noted earlier, a few relatively developed, but still developing, countries are starting to participate in the negotiation of highly elaborate and complex EIAs with lengthy provisions on both investment and trade in services, including among themselves. Pre-eminent on this list of countries are Chile and Singapore. Half a dozen agreements to which these countries are parties (including also with the European countries, the United States, Australia or Japan) have set detailed and comprehensive standards for both investment liberalization and investment protection. They represent a more market-oriented development policy that is sometimes seen in earlier EIAs among developing countries.

Furthermore, while one might expect that EIAs among developed countries would provide the highest standards of investment protection, this is not always the case. For example, the FTA between the United States and Australia does not include an investor-State dispute resolution mechanism, while a number of EIAs among developing countries do.

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In conclusion, while regional differences remain, and the traditional broad distinction between types of EIAs — that is, agreements that emphasize investment liberalization, agreements that focus on both investment protection and liberalization, agreements that deal with protection only, and agreements that address investment promotion through cooperation — is still valid, a new generation of regional and interregional EIAs is emerging that is moving gradually towards greater coverage and depth of investment issues. In some cases, this is the result of the process of integration set out in the agreements advancing and maturing over time. Also, earlier North-South agreements that granted non-reciprocal preferential treatment to the developing

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countries parties are moving towards full reciprocity. Such is the case of the post-Cotonou agreements currently being negotiated between the ACP and European Community countries. South-South EIAs meanwhile are also moving gradually closer to their North-South counterpart models, although significant individual differences are often observed. At the same time, cooperation agreements containing only very few and general commitments on investment have proliferated in recent years, especially within Europe and Asia, as well as between countries in different regions, reflecting a certain reluctance to embark upon full-fledged investment commitments at the earlier stages in certain cases. Hence, as new EIAs appear on the radar screen on an almost daily basis, it might still be too early to reach more definite conclusions in terms of EIA approaches to investment.

A more definitive observation that can be made at this stage is that, as the cross-membership of EIAs continues to expand, and EIAs from all regions increasingly overlap, it becomes more and more difficult to determine in practice what specific investment rules apply to foreign investors in a particular country at a particular time. This suggests that efforts towards rationalization and simplification of the current universe of rules on investment might be in the interest of both countries and investors.

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## IV. DIFFERENCES AND SIMILARITIES BETWEEN EIIAS AND WITH OTHER AGREEMENTS

### A. Overview

It has been observed earlier (chapter III.B) that EIIAs have been influenced by other investment agreements, notably by BITs and the WTO Agreements.<sup>68</sup> However, BITs and EIIAs typically differ in a number of important respects.

First, except for the BITs concluded by the United States and Canada, BITs generally provide for the treatment and protection of investment once established, but do not provide for a right to establish foreign investment. That is, BITs are usually intended to protect and thereby promote investment. EIIAs, by contrast, seek to integrate economies and thus are more likely to focus on liberalizing investment flows, as well as protecting and promoting investment. They are also more likely to regulate the behaviour of investment, at least insofar as anticompetitive behaviour is concerned.

Second, unlike BITs, certain types of EIIAs do not deal with investment protection issues. As noted earlier, this may be partially explained by the fact that EIIAs were traditionally concluded between countries that shared similar political, economic and social systems. Developed country EIIAs in particular did not spell out protection provisions, as protection could be guaranteed by the parties' national legal systems or under the established general legal review processes (e.g. the European Court of Justice in the EC). On the other hand, other types of EIIAs do include investment protection provisions, including notably North-South and some South-South agreements. In the latter cases, the protection provisions of EIIAs often replicate those of BITs.

Third, with respect to the settlement of investment disputes, EIIAs and BITs differ in one important respect. That is, while recent BITs almost invariably allow for direct settlement of investor-State disputes through international arbitration, certain types of EIIAs — typically those that do not address investment protection issues — do not allow for international arbitration of investor-State disputes, nor do they always address specifically the issue of investment disputes. Instead, investment disputes are often dealt with implicitly in these EIIAs under general provisions for the settlement of disputes arising between the States parties (State-State) that apply to all (or most) aspects of the agreement.

The discussion thus far might be read to suggest that BITs provide a higher level of investment protection, while EIIAs permit more variation, which in turn leads to a weakening of the protections afforded. In fact, however, the existing EIIAs demonstrate that it is possible to obtain a high standard of investment protection and liberalization in agreements that bind multiple States. The distinction between a BIT and an EIIA is not necessarily the distinction between a strong and a weak agreement.

Fourth, EIIAs tend to include mechanisms for consultation, follow-up and implementation that are more elaborate and complex than those found in BITs (if any). EIIAs also often contain

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<sup>68</sup> For example, NAFTA's Chapter Eleven on Investment is based on the United States BIT model of the time, and so is the MERCOSUR Protocol of Colonia (Intra Zone). BIT provisions on investment protection have been replicated in EIIAs that address protection issues. Similarly, the provisions of the WTO TRIMs Agreement have influenced EIIA provisions dealing with performance requirements, while GATS has inspired most trade-in-services provisions or chapters in EIIAs.

specific mandates regarding the further expansion of the agreement, or specific aspects thereof, which are largely absent in BITs. It is also common, especially for regional integration EIAs, to establish elaborate institutional arrangements, including a permanent secretariat, to deal with the day-to-day administration of the agreement. In the case of highly integrated EIA groups such as the EC, the institutional machinery may include a parliament and a permanent court of justice. BITs, on the other hand, have tended to rely on informal exchanges and regular diplomatic channels to address questions related to their implementation.

Fifth, while BITs address a more limited number of issues and tend to be quite uniform in their approach to those issues, EIAs reflect far more variation in their scope and content. Although an EIA may address relatively few investment issues, as do some of the agreements discussed in this study, they potentially address a much larger range of investment-related issues than the BITs. Thus, an increasing number of recent EIAs deal very extensively with trade in services, while there are provisions or chapters in them on topics such as competition policy, intellectual property, government procurement, labour, environment, trade in special sectors, temporary entry for business persons, and transparency. The more issues that are addressed, the more complex the agreement becomes, and the greater the likelihood that variations in the text reflecting the special cultural characteristics of countries in different regions must be taken into account. As this suggests, the negotiation of an EIA may require a higher level of expertise and more preparation than the negotiation of a BIT.

Sixth, the greater variation among EIAs perhaps presents a better opportunity than do BITs for experimentation with different approaches to addressing development issues. EIAs, for example, tend to have a larger number of provisions that take into account the special circumstances of developing countries than do BITs. Thus, EIAs typically contain a broader range of exceptions, safeguards and transitional periods than BITs, which are both general and issue specific. Another set of development-related provisions which tend to be more prominent and detailed in EIAs than in BITs relates to investment promotion. Many EIAs, including notably South-South and North-South EIAs, contain elaborate clauses providing for *inter alia* exchange of information and technical assistance, so as to help improve the investment climate of the less developed countries of the group. Probably the most extensive investment promotion provisions of this type are those in the Cotonou Agreement. Again, it requires more expertise to negotiate a complex agreement with special provisions for developing countries than to conclude a BIT that departs very little from the model negotiating text, but the reward for the effort may be an agreement more carefully tailored to the circumstances of the parties.

The elaboration of EIAs has also been influenced by earlier EIAs signed by EIA partners. In particular, EIAs signed by the same regional group with different third countries share many common features (as is the case with agreements signed by the EC and EFTA with other European countries, and by ASEAN with other Asian countries). Also, influential individual countries tend to establish a similar pattern for their bilateral EIAs with different countries (e.g. the bilateral EIAs signed by the United States and Canada). This applies also to interregional EIAs, which as a result tend to share many of the features of the regional models established by their more influential partners (e.g. recent interregional agreements signed by the United States are based on the NAFTA model). In addition, recent developing country EIAs are moving closer towards the North-South approaches. As a result of this cross-fertilization among EIAs over the years, a certain convergence of patterns regarding EIA provisions has emerged — amidst many EIA-specific variations — which often transcend regional lines.

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A basic common characteristic of EIAs — and one that is not found in BITs — is that these agreements typically set in motion a *dynamic process* whereby they will achieve their aims. As the impossibility of implementing an ambitious agenda at the time of conclusion of the agreement is realized, procedures are established with the help of institutional mechanisms that are intended to ensure the implementation of the agreement's objectives over time.

This feature is particularly relevant with respect to the implementation of the investment liberalization commitments adopted by EIAs. EIAs typically follow two main patterns in this respect. One is to provide for actual liberalization subject to a list of country exceptions (negative list approach). This pattern is characteristic of, for example, the agreements signed between American countries that follow the model of NAFTA. The second pattern is to provide for the progressive abolition of restrictions on the entry, establishment and operation of investment.<sup>69</sup> With respect to the second pattern, the level of liberalization sought varies considerably amongst different types of EIAs. Thus, while some agreements commit to achieving full liberalization of investment almost immediately (the EC) or by a particular date (the ASEAN Investment Area), others provide for the process of investment liberalization to be carried out in several stages (the Europe Agreements signed by the EC with Central and South-East European countries). Yet another pattern is to start with an initial agreement that contains a few general obligations and definitions, and provide a framework for future negotiations to liberalize investment (e.g. the Euro-Mediterranean Agreements, the African Economic Community, the ASEAN Agreement with China). In certain cases, the latter approach may resemble the liberalization model established by GATS.

Even when the investment regime on admission and establishment laid out by an EIA is fairly open, foreign firms may be confronted by a range of internal policy measures that restrict their operations and seek to influence their various effects. Certain categories of issues, including transfer of funds, have been traditionally a part of most EIAs' investment liberalization schemes as they can be considered "border measures". Others issues started to receive special attention mainly during the Uruguay Round of Trade Negotiations and, since then, have been increasingly included in EIAs as they are considered important aspects of market access. These include trade in services, performance requirements, employment of managerial and technical personnel, and intellectual property protection.

As the process of investment integration progresses, investment treatment and protection standards after entry increasingly become also an important part of the EIA. Indeed, as economic integration deepens, national treatment at the point of entry might not suffice to guarantee market access when internal national legislation creates obstacles to the flow of investment. The critical relevance of the national treatment standard for an investment integration process is emphasized as it refers to an entire body of law, not to specific measures. With respect to investment protection issues, one of the most important potential obstacles to foreign investment after entry relates to the non-commercial risks facing foreign firms in host countries, in particular the risks of arbitrary treatment, lack of due process and certain takings of property. Provisions addressing these concerns (notably fair and equitable treatment, conditions for expropriation and settlement of disputes) have become increasingly common in EIAs moving to advanced stages of investment integration. The main model for investment protection

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<sup>69</sup> This pattern has been followed by, among others, the agreements between the European Community and third countries, and the Framework Agreement on the ASEAN Investment Area.

continues to be NAFTA's Chapter Eleven, which in turn is based on the United States and Canadian BIT models of the time, but with the addition of intellectual property protection. While the key protection issues addressed in these types of EIAs have varied little, a new generation of agreements that follow the NAFTA model — concluded mainly by American and Asian countries — are more comprehensive, detailed and, in the main, rigorous than prior NAFTA-style EIAs. They reflect the accumulated experience derived from previously concluded EIAs and BITs, which has identified issues requiring resolution that were not addressed in earlier agreements.

In some cases, the decision to start a process of investment liberalization and integration is preceded by a preliminary stage in which the EIA partners limit their commitments to establishing a cooperation framework in order to create a policy climate in which investment could flow within the EIA area. This pattern is followed in cases where the parties' political and economic systems are too far apart for integrating their investment policies. Exchange of information, regular contact, commitments to improve the investment climate and technical assistance measures aimed at institution building are typical ingredients of promotion programmes that seek to prepare the way for more mature mutually-beneficial stages of investment relations. Of course, promotional measures often stand side by side with liberalization commitments in EIAs as the parties realize in certain cases that liberalization measures alone may not suffice to ensure the flow of investment in both directions.

The actual patterns are of course much more complex than these stylized rough descriptions suggest. Some EIAs start with few and general investment commitments and move through various stages of increased specificity and depth. Other EIAs remain fairly static in their original commitments, which may be set at any of the described levels. One important variation is the possibility of allowing certain countries, whether developing countries or economies in transition, to benefit from transitional arrangements. Another variant involves the selective use of "best efforts" clauses to cover some issues of special difficulty. In short, the elaboration of investment rules through EIAs is advancing at various *tempos* through dynamic and flexible processes that build on previous experience while experimenting with innovative approaches to address new challenges.

Yet another important common characteristic of EIAs, and one that sets these agreements apart from the other IAs, relates to their inclusion of trade, investment and other transactions as part of a common normative framework. Here again, as noted in the Introduction (table I.1), the overall approach to investment, as well as the breadth and depth of the investment provisions in an EIA, does not necessarily parallel (and indeed in many cases it does not) the approaches to, and provisions on, trade or other economic transactions covered under the common framework. Many variations of EIAs coexist also in this respect. Thus, in many EIA-driven economic integration processes, investment provisions only enter the picture when a certain level of trade integration has already been achieved. Other EIAs take a "big bang" approach whereby trade, investment and other liberalization and integration processes start and advance apace. In some cases, trade in services is part of the package, as are labour, knowledge and other production factors, while in other cases, they are not. The accumulation of various normative processes with different conceptual and operational characteristics advancing together but not necessarily at the same speed, or even in the same direction, adds layers of complexity to the already multifaceted nature of EIAs, as compared with other IAs. This in turn further complicates the task of gauging the full legal and policy implications of EIAs.

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## B. Main Substantive Provisions on Investment in EIAs: A Comparative Analysis

As has been noted (chapter III.B.2), EIAs exhibit different degrees of investment integration. The depth of integration of an EIA in relation to investment is determined by the extent and content of the commitments the parties undertake on specific investment issues. This in turn is directly related to the formulation of its substantive provisions. This section analyses the content of investment provisions in EIAs. It identifies the most important investment provisions that appear in EIAs and examines the most common or notable variations in the formulation of these provisions. Section 1 discusses provisions that establish the subject-matter scope of the agreement. Sections 2 through 5 analyse, respectively, substantive provisions that liberalize, protect, promote or regulate investment. As noted above, some provisions may serve more than one purpose, and thus the placement of a provision in one category rather than another is intended principally to facilitate organization of the material.

### 1. *Scope of the Agreement*

The subject-matter covered by the investment provisions in an EIA is established through definitions, through its operational provisions, and through general exceptions and special exceptions.

#### a. **Definitions**

Investment provisions in an EIA typically apply to investment by investors of one party in the territory of another party. Accordingly, the most important definitions in establishing the subject-matter scope of these provisions are of the terms “investment” and “investor.” Many EIAs, however, do not define those terms. These include EIAs that focus on investment liberalization, such as the EC Agreement and the association agreements signed by the EC with Central European countries as well as the Euro-Mediterranean agreements. Similarly, agreements providing a general framework for further cooperation on investment (including sometimes investment promotion) signed by the EC, EFTA, Canada and the United States with various countries do not include definitions of investment or investor. Whether an instrument explicitly defines key terms or not, its application requires that the parties use some working definition of these terms.

#### i. *Investment*

EIAs that define investment have used three types of definitions:

- **Asset-based definition.** EIAs that are directed at the protection of investment tend to define “investment” broadly, covering the various types of assets that might need to be protected during the life of the investment. They use an asset-based definition similar to that which appears in BITs. Such agreements tend not to include a right to establish investment and thus the host country can still narrow the scope of the agreement by preventing the establishment of undesirable investment.

- **Transaction-based definition.** This type of definition is found in EIAs that concern the liberalization of cross-border financial flows through which an investment is made. An example of this approach is the definition used in Annex A of the OECD Code of Liberalization of Capital Movements. The Code does not define investment but lists a number of capital transactions between residents and non-residents that are the subject of liberalization commitments.
- **Enterprise-based definition.** EIAs that concern the liberalization of investment have tended to define investment in narrow terms, insisting on the element of control over the enterprise as a key element of the concept. An example is the Free Trade Agreement between Canada and the United States (UNCTAD, 2003a, ch. IV; 1999a, pp. 31-32).

Recent practice in EIAs that seek both to liberalize and to protect investment has moved in the direction of broad asset-based definitions. However, several approaches have emerged that aim at limiting the broad asset-based type of definition, some of which are close to the enterprise-based definition.

The broad, asset-based definition typically defines investment as “every kind of asset” and then adds an illustrative list of assets that are included in the definition. Typical is the definition in article I of the Agreement Establishing the Free Trade Area between the Caribbean Community and the Dominican Republic, which provides that:

- (i) *Investments: means every kind of asset and in particular though not exclusively, includes:*
  - a) *movable and immovable property and any other property rights such as mortgages, liens and pledges;*
  - b) *shares, stocks and debentures of companies or interests in the property of such companies;*
  - c) *a claim to money or to any performance having a financial value;*
  - d) *intellectual and industrial property rights, including rights with respect to copyrights, patents, trademarks, trade names, industrial designs, trade secrets, technical processes and know-how and goodwill;*
  - e) *business concessions conferred by law or under contract, including any concessions to search for, cultivate, extract or exploit natural resources.*

Occasionally, the list of assets is not illustrative, but exhaustive. For example, article 159 of COMESA provides that:

*[f]or the purposes of investment protection, the following activities shall be considered as investment:*

- (a) *movable and immovable property and other property rights such as mortgages, loans and pledges;*
  - (b) *shares and any other rights of participation in the management or economic results of a company or a firm, whether incorporated or not, including minority shares, corporate rights and any other kind of shareholding;*
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- (c) *stocks, bonds, debentures, guarantees or other financial instruments of a company or a firm, government or other public authority or international organization;*
- (d) *claims to money, goods, services or other performance having economic value;*
- (e) *intellectual and industrial property rights, technical processes, know-how, goodwill and other benefits of advantages associated with a business; and*
- (f) *such other activities that may be declared by the Council as investments.*

As this language indicates, the broad definition includes portfolio as well as direct investment.

Some earlier EIAs dealing only with investment protection have defined investment as an investment that is made in accordance with the laws of the host country, or used other language to the same effect. Local laws may require approval of the investment and the approval may be granted subject to certain conditions. The implication of this type of clause is that an investment which is not made in accordance with the approval requirements and conditions established under the host country's local laws is outside the scope of the agreement and cannot benefit from its provisions. This is explicitly stated in article II of the ASEAN Agreement for the Protection and Promotion of Investments, which provides that:

*1) This Agreement shall apply only to investments brought into, derived from or directly connected with investments brought into the territory of any Contracting Party by nationals or companies of any other Contracting party and which are specifically approved in writing and registered by the host country and upon such conditions as it deems fit for the purposes of this Agreement.*

Article II was later qualified by the 1996 protocol amending the 1987 Agreement with the insertion of a new Article III-A, which read "*Each Contracting Party shall endeavour to simplify and streamline its investment procedures and approval process to facilitate investment flows*".

A similar approach has been followed by some agreements signed in recent years. For example, the FTA between Australia and Thailand (article 901(a)) provides that:

*"covered investment" means an investment... which has been admitted by the latter Party ... in accordance with its laws, regulations and policies*

Article 908(1)(a)) stipulates that the provisions on protection and promotion of the agreement apply to:

*covered investments which, if so required, have been specifically approved in writing by the competent authorities concerned of the other Party as being entitled to the benefits of an agreement relating to investments*

Significantly also, the Australia-Thailand FTA applies different definitions of investment to the promotion and protection provisions and to the liberalization provisions, thus avoiding some of the potential definitional difficulties that arise when an EIA both protects and liberalizes investment flows, since in these cases the host country surrenders a significant part of its ability to exclude undesirable investment. As a result, in such cases, the likelihood increases that the definition of investment will be somewhat narrower.

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For example, some host countries are reluctant to extend treaty protection to portfolio investment because they are concerned that it may not contribute to development, insofar as it may not result in the introduction of technology, and its potential volatility may exacerbate economic instability and, in that way, undermine economic development. Thus, some EIAs limit the definition of investment to direct investment. For example, article 45 of the FTA between the EFTA States 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.*

A footnote added to the definition states that:

*Direct Investment embraces operations carried out in the country concerned by non-residents and operations abroad by residents by means of: 1) creation or extension of a wholly-owned enterprise, subsidiary or branch, [or] acquisition of full ownership of an existing enterprise; 2) participation in a new or existing enterprise; 3) a loan of five years or longer.*

To similar effect is article 2 of the Framework Agreement on the ASEAN Investment Area, which provides that:

*[t]his Agreement shall cover all direct investment other than ... portfolio investment; and ... matters relating to investments covered by other ASEAN Agreements, such as the ASEAN Framework Agreement on Services.*

Such definitions, however, are atypical in more recent EIAs. The distinction between direct and portfolio investment is often merely a matter of degree rather than of kind, frequently determined by a somewhat arbitrary percentage of equity shares owned. Thus, in some cases, it is difficult to distinguish between the two in principle. Furthermore, portfolio investment can in fact contribute to development, including the introduction of new technology, because it may provide necessary financing for an enterprise that will create employment, provide training, generate export earnings and transfer technology. A host country may choose, therefore, to allow the definition of investment to include portfolio investment and to address concerns about volatility in other ways, such as through limitations on the right of free transfer of investments.

The broad, asset-based definition also goes beyond the kinds of assets that an economist might traditionally consider to be “investment”. For example, it could include short-term contracts and merchandise, the kinds of assets that are usually associated with trade rather than investment. A couple of different approaches have emerged to address this concern. One approach is to utilize an enterprise-based definition, such as that which appears in article 1139 of NAFTA. This definition differs from the broader, asset-based definition in that it limits investment principally to those assets that are associated in certain ways with an enterprise, as opposed to those, for example, that might be present in the territory for purposes of trade, such as merchandise to be sold. It provides that:

*investment means:*  
*(a) an enterprise;*  
*(b) an equity security of an enterprise;*  
*(c) a debt security of an enterprise*



- (i) where the enterprise is an affiliate of the investor, or
- (ii) where the original maturity of the debt security is at least three year, but does not include a debt security, regardless of original maturity, of a state enterprise;
- (d) a loan to an enterprise
  - (i) where the enterprise is an affiliate of the investor, or
  - (ii) where the original maturity of the loan is at least three years, but does not include a loan, regardless of original maturity, to a state enterprise;
- (e) an interest in an enterprise that entitles the owner to share in income or profits of the enterprise;
- (f) an interest in an enterprise that entitles the owner to share in the assets of the enterprise on dissolution, other than a debt security or a loan excluded from subparagraph (c) or (d);
- (g) real estate or other property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes; and
- (h) interests arising from the commitment of capital or other resources in the territory of a Party to economic activity in such territory, such as under
  - (i) contracts involving the presence of an investor's property in the territory of the Party, including turnkey or construction contracts, concessions, or
  - (ii) contracts where remuneration depends substantially on the production, revenues or profits of an enterprise;

but investment does not mean,

- (i) claims to money that arise solely from
  - (i) commercial contracts for the sale of goods or services by a national or enterprise in the territory of a Party to an enterprise in the territory of another Party; or
  - (ii) the extension of credit in connection with a commercial transaction, such as trade financing, other than a loan covered by subparagraph (d); or
- (j) any other claims to money, that do not involve the kinds of interests set out in subparagraphs (a) through (h).

Thus, while the definition is broad enough to include both direct and portfolio investment, the enterprise-based definition tends to exclude assets that are not related to a long-term investment. This definition also underscores the idea that portfolio investment should be included in the definition of investment if it assists in capitalizing an enterprise that will presumably make a long-term contribution to the economy of the host country.

A second approach is to try to define “investment” in economic terms. This approach is utilized in several recent free trade agreements. For example, Article 10.27 of the Free Trade Agreement between Chile and the United States 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.*
- Forms that an investment may take include:*
- (a) an enterprise;
  - (b) shares, stock, and other forms of equity participation in an enterprise;
  - (c) bonds, debentures, loans, and other debt instruments;
  - (d) futures, options, and other derivatives;

- (e) *rights under contract, including turnkey, construction, management, production, concession, or revenue-sharing contracts;*
- (f) *intellectual property rights;*
- (g) *rights conferred pursuant to domestic law, such as concessions, licenses, authorizations, and permits; and*
- (h) *other tangible or intangible, movable or immovable property, and related property rights, such as leases, mortgages, liens and pledges; but investment does not mean an order or judgment entered in a judicial or administrative action.*

This definition includes the usual categories of assets that appear in the asset-based definition, but limits the assets to those that have the characteristics of an investment, such as the placement of capital at risk for purposes of gain.

## *ii. Investor*

EIIAs that contain a broad asset-based definition of the term “investment” tend also to define the term “investor”, following in this respect the approach of BITs. In addition, EIIAs that deal with investment liberalization tend to include a definition of companies or firms for the purpose of determining the scope of the rights of establishment they confer.

Two issues typically arise with respect to the definition of an investor. The first is to determine the types of entities that can be investors. The second is to determine the nationality of the investor, since typically an investor must have the nationality of a treaty party to have rights under the treaty.

Investors generally include natural persons and juridical entities, sometimes referred to generically in the EIIAs as “companies.” A common approach is to include virtually every type of juridical entity within the definition. For example, Article 1 of Chapter IV of the Agreement between the United States and Vietnam on Trade Relations defines “company” as:

*any entity constituted or organized under applicable law, whether or not for profit, and whether privately or governmentally owned or controlled, and includes a corporation, trust, partnership, sole proprietorship, branch, joint venture, association, or other organization.*

Given that often the EIIA also includes a broad definition of “investment”, the broad scope of juridical entities that may be considered “investors” is perhaps not surprising. Certain types of investments are likely to be associated with certain types of juridical entities. For example, small businesses may take a different corporate form than large, publicly-traded multinational enterprises. Investments in the service sector often make use of partnerships, which are less common in the manufacturing sector. A strategic alliance between a foreign and a domestic investor may take the form of a joint venture. A host country that excludes certain juridical entities from treaty protection may unintentionally exclude certain desired investments. That said, the issue of the legal form of a juridical entity is not a matter of indifference to a host country. Different types of juridical entities, for example, shield the beneficial owners from liability for the acts of the entity to differing degrees. Nevertheless, EIIAs that define “investor” tend to do so quite broadly.

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Some agreements, however, limit the definition of "companies" only to those that are organized for profit. An example is article 48 of the European Community treaty, according to which:

*'Companies or firms' means companies of firms constituted under civil or commercial law, including cooperative societies and other legal persons governed by public or private law, save for those which are non-profit-making.*

The nationality of natural persons generally is determined by domestic law. In other words, a natural person is a national of the home country if the laws of the home country so state. An issue that occasionally arises is how to ascribe the nationality of a person who has the nationality of more than one country. Some EIAs address that issue explicitly. For example, article 10.20 of the Free Trade Agreement between Singapore and the United States provides that:

*investor of a Party means a Party or state enterprise thereof, or a person of that Party, that attempts to make, is making, or has made an investment in the territory of the other Party; provided, however, that a natural person who is a dual national shall be deemed to be exclusively a national of the State of his/her dominant and effective nationality.*

Most EIAs, however, do not address the issue explicitly. If this issue is one that concerns a treaty party, it would be advisable to include language resolving it.

The nationality of juridical entities in most investment agreements is usually determined by one of three tests. These tests base nationality on the State under the laws of which the entity is organized (the place of organization); the State where the entity has its headquarters or main facility (the place of the seat); or the State whose nationals own or control the entity (the place of ownership or control).

The place of organization is the easiest test to administer, because it can usually be determined with certainty and is unlikely to change. This test, however, allows the ultimate, beneficial owners of the investment to acquire treaty protection even without having any genuine economic link to the home country. The home country may be concerned about this result because the application or interpretation of its treaty may be driven, particularly if the investor-to-State dispute resolution provision is invoked, by persons who have no allegiance to the home State. The host country may also be concerned about this result because it means that it is extending treaty protection to beneficial owners whose own state of nationality does not extend reciprocal protection to investors from the host country. Furthermore, the place of organization test exposes the host country to the risk that unforeseen investors with no link to the home country at the time the treaty was concluded may later acquire the nationality of the home country through incorporation there, thus expanding the group of investors protected by the agreement beyond those contemplated during the negotiations.

The place of ownership or control presents the opposite situation. Ownership or control can be difficult to ascertain if the company is publicly traded and it may change over time, with the result that investment can lose or gain treaty protection as ownership or control changes. However, the place of ownership or control has a strong and genuine economic link to the company.

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The place of the seat is a compromise between the two: it is easier to ascertain than ownership and control, and represents more of an economic link than the place of organization.

The place of organization test might be thought to be the most liberal of the tests, because it seeks an efficient mechanism for establishing corporate nationality, rather than concerning itself with whether the State of nationality will truly benefit from the extension of its protection to the investor and the investment. Perhaps not surprisingly, many EIAs use the place of incorporation as the test for corporate nationality. Typical is the Free Trade Agreement between CARICOM and the Dominican Republic. Article I(ii) defines an investor as:

*any corporation, company, association, partnership, or other organization, legally constituted under the laws of a Party, whether or not organized for pecuniary gain, or privately, or governmentally owned or controlled.*

Other EIAs, however, seek to ensure that the home country has a genuine economic link to the investor. For example, article I(b) of the ASEAN Agreement for the Protection and Promotion of Investments defines “company” as:

*a corporation, partnership or other business association, incorporated or constituted under the laws in force in the territory of any Contracting Party wherein the place of effective management is situated.*

This definition ascribes corporate nationality on the basis of both the place of incorporation and the place of the seat, and brings an entity within the definition of “investor” only if both places are the same. Similarly, article 37 of the Free Trade Agreement between EFTA and Singapore defines “investor of a Party” as “*a company constituted or organized under the applicable law of that Party and carrying out substantial business activities there*”. Thus, incorporation must be accompanied by “substantial business activities”, a link that is weaker than the requirement that the investor have its seat in the home State, but that nevertheless requires a substantial economic link with the state of nationality. A similar approach is followed in the European Community Treaty. Article 48 states:

*Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community shall, for the purposes of this Chapter, be treated in the same way as natural persons who are national of Member States.*

The Treaty Establishing the Caribbean Community uses a definition of nationality for juridical persons which encompass all the three tests. Thus, article 35 dealing with establishment provides:

*For the purpose of this Article and Articles 36 and 38 of this Annex:*

(a) *a person shall be regarded as a national of a Member State if such a person*

(i)...

(ii)...

(iii) *is a company or other legal person constituted in the Member State in conformity with the law thereof and which that States regards as belonging to it, provided that such company or other legal person has been formed for gainful purposes and has its registered office and*

*central administration, and carries on substantial activity within the Common Market and which is substantially owned and effectively controlled by persons falling under (i) and (ii) above.*

Some regional integration groups have created "regional corporations" to which a special status is granted.<sup>70</sup> In the case of developing countries, the creation of regional corporations is typically linked to the establishment of regional industrialization programmes.<sup>71</sup> The definition of a regional corporation usually involves a number of criteria. For example, article I of Decision 292 of the Commission of the Cartagena Agreement defines the Andean Multinational Enterprise as follows:

*For the purposes of this Code, an Andean Multinational Enterprise shall be a company fulfilling the following requirements:*

- a) Its principal domicile shall be in the territory of one of the Member Countries of in that where the enterprises is transformed or merged.*
- b) It must be constituted as a corporation in accordance with the procedures contemplated in the corresponding national legislation and it shall add to its name the words "Andean Multinational Enterprise" ... .*
- c) Its capital must be represented by nominal shares of equal value that confer on the shareholders equal rights and impose equal obligations.*
- d) It must have contributions of property from national investors from two or more Member Countries that together are greater than sixty percent of the capital of the company.*
- e) ....*
- f) The sub-regional majority of the capital must be reflected in the technical, administrative, financial and commercial management of the company in the judgment of the corresponding national competent entity.*
- g) ... .*

Some EIAs, presumably influenced by the GATS, have also used a "commercial presence" test for determining corporate nationality. For example, the Free Trade Agreement between Colombia, Venezuela and Mexico allows a private entity to establish nationality in either of two ways. First, under article 17-01, an investor may be "*an enterprise constituted, organized, or protected in accordance with the laws of that Party*". Thus, it uses the place of incorporation test. Under that same article, however, an investor may also be "*a branch located in the territory of that Party that engages in commercial activities therein*". This last test does not fall within any of the three categories. Rather, an entity becomes a national of a State by having a commercial presence in the territory of that State. The test has the virtue of being relatively easy to apply, but also represents a genuine economic link between the investor and the State of nationality.

The variety of tests increases the likelihood that an investor will have multiple nationalities. For example, an investor may be incorporated under the laws of one State, but

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<sup>70</sup> An example is the European company or SE created by the European Company Statute, adopted by the EC in 2001.

<sup>71</sup> Examples include Decision 292 of the Commission of the Cartagena Agreement (Andean Pact) adopting the Uniform Code on Andean Multinational Enterprises, the Revised Treaty of the Economic Community of West African States (ECOWAS), the Revised Basic Agreement on ASEAN Industrial Joint Ventures and the Charter on a Regime of Multinational Industrial Enterprises in the Preferential Trade Area of Eastern and Southern African States.

have a commercial presence in another State, thus being able to claim the nationality of both and being able to assert the protection offered by the EIAs of any State of which it is a national. Among other things, this has significant implications for the settlement of investment disputes as it allows an investor potentially to submit the same dispute to the dispute resolution mechanism provided by each of the agreements.

Finally, EIAs that deal with trade in services often include a number of definitions, such as “commercial presence”, that are relevant for investment in the services sector. For example, article 20 of the Free Trade Agreement between the EFTA States and the United Mexican States defines “commercial presence” as follows:

- (i) as regards nationals, the right to set up and manage undertakings, which they effectively control. This shall not extend to seeking or taking employment in the labour market or confer right to access to the labour market of another Party;*
- (ii) as regards juridical persons, the right to take up and pursue the economic activities covered by this Section by means of the setting up and management of subsidiaries, branches or any other form of secondary establishment.*

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Policymakers have a number of choices when deciding on the scope of the investment rules of an EIA. In particular, this raises questions about which types of investment should be covered by the agreement. All forms of investment can, in principle, contribute to the economic development of participating host countries and so there is no form of investment that from a developmental perspective should always be excluded. However, certain forms of investment raise concerns that others do not. Portfolio investment, for example, raises concerns about its potential volatility. These concerns can be addressed by excluding certain types of investment/investor from the scope of the agreement, but that can send a less favourable signal to investors. Also, efforts to exclude certain types of investment/investor can lead to uncertainty concerning the scope of the agreement.

Alternatively, concerns about certain types of investment/investor may be addressed not by excluding those investments from treaty coverage, but by drafting the substantive provisions in a way that alleviates the concerns. For example, concerns about the volatility of portfolio investment may be addressed by placing limitations on the right to transfer investments out of the territory of the host State under certain circumstances. The ability, however, to take account of potential problems through the substantive provisions requires a somewhat higher level of expertise on the part of the negotiating States, since they must be able to anticipate some of the most important problems and craft language to avoid them.

As a third possibility, concerns about the potentially adverse effects of certain investments can be addressed by limiting the liberalization achieved by the agreement and reserving the right to exclude those investments entirely, although the maintenance of an elaborate screening mechanism can undermine to some extent the rationale for entering into an EIA.

A fourth possibility would be to adopt a hybrid of both broad and narrow definitions for different purposes in an agreement. Thus a broad asset-based definition can be used for protecting investment and a narrow transaction-based for dealing with cross-border investment

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liberalization. In short, concerns about the scope of the agreement can be addressed through the definitions provisions, through the liberalization provisions or through the investment protection provisions, but each approach presents its own difficulties.

With respect to the definition of investors, an important task for negotiators is to avoid using definitions that would permit legal persons from non-EIIA parties to benefit from the provisions of the agreement on a “free rider” basis. Thus, they need to ensure that the companies covered under the treaty have a real link with the home country, and to avoid giving legal protection to companies that have no substantial business activities in that country. In the present era of globalization, no single test for attributing corporate nationality can guarantee appropriate coverage of foreign investors. In these circumstances, using several tests together may provide a more reliable method of defining foreign companies for the purposes of treaty protection. (UNCTAD, 1999a, p. 66; 1998a, pp. 38-41).

### **b. General exceptions**

EIIAs often include provisions that permanently exclude certain actions by the parties from the application of the agreement. These provisions limit the substantive scope of the agreement and typically are intended to maintain regulatory flexibility for the host country. Thus, general exceptions are usually structured in such a way as to insulate from the application of the treaty those regulatory activities of the host country that are of special importance to that host country and that seem potentially to be affected by the application of treaty rules.

Two common exceptions are for measures taken by a host country to preserve public order or to protect national security. Some EIIAs exclude measures to enforce the criminal laws of the parties. The Free Trade Agreement between Colombia, Venezuela and Mexico includes all three of these exceptions. Article 17-02 provides that:

*[n]othing in this Chapter shall be construed to prevent a Party from adopting or maintaining measures for preserving its national security or public order, or implementing the provisions of its criminal laws.*

Most EIIAs do not provide any definition of public order. An exception is the Free Trade Agreement between Australia and Singapore, which provides in a footnote to article 18 that “[t]he public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society.”

In some cases, the national security exception is quite detailed. For example, article 34 of the Free Trade Agreement between the EFTA States and Singapore provides that:

*Nothing in this Agreement shall be construed:*

- (a) to require a Party to furnish or allow access to information the disclosure of which it considers contrary to its essential security interests;*
- (b) to prevent a Party from taking any action which it considers necessary for the protection of its essential security interests:*
  - (i) relating to the supply of services as carried out directly or indirectly for the purpose of provisioning a military establishment;*
  - (ii) relating to fissionable and fusionable materials or the materials from which they are derived;*

- (iii) *taken in time of war or other emergency in international relations; or*  
 (c) *to prevent a Party from taking any action in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.*

Some EIAs have exceptions for measures to protect the environment or the cultural patrimony. Article 9.02(b) of the Free Trade Agreement between Central America and the Dominican Republic provides that:

*[t]his chapter shall not apply to measures that a Party adopts to restrict the participation of the investments of investors of the other Party in its territory, for reasons of national security or public order, the protection of the cultural and environmental patrimony, and the conservation of the environment.*

The environmental exception is sometimes more detailed. Article 10.15 of the Free Trade Agreement between Panama and Taiwan Province of China provides that:

1. *Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken under its ecological or environmental laws.*
2. *The Parties recognize that it is inappropriate to encourage investment by relaxing domestic health, safety or environmental measures. Accordingly, a Party shall not waive or otherwise derogate from, or offer to waive or otherwise derogate from, such measures as an encouragement for the establishment, acquisition, expansion or retention in its territory of an investment of an investor. If a Party considers that the other Party has offered such an encouragement, it may request consultations with the other Party.*

These regulatory exceptions typically permit the host country to protect certain non-economic interests that might otherwise have been incidentally affected by the economic provisions of the EIA. However, their language in some cases could be interpreted to allow Governments broad discretion as regards regulatory actions. If one compares, for example, the environmental exception in the agreement between Central America and the Dominican Republic with that in the agreement between Panama and Taiwan Province of China, it can be seen that the latter permits a party to adopt measures that “*it considers appropriate*” to preserve the environment, language that is absent from the former provision. An issue arises as to whether this additional language renders a party’s determination that a measure is necessary to preserve the environment conclusive, or whether a measure undertaken purportedly to protect the environment, but perhaps in reality to protect a local investment against foreign competition, could be challenged through the dispute resolution mechanisms of the agreement.

Not all general exceptions are intended to maintain regulatory discretion on certain special activities. Some are intended to preserve the ability of the host country to provide social services to its people. For example, article 3.02 of the Treaty on Investment and Trade in Services between Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua provides that:

*[n]o provision of this chapter shall be interpreted in the sense of preventing a Party from providing services or performing functions related to law enforcement, correctional*

*services, pension or employment security or social security services, social welfare, public education, health and child care.*

EIIAs that contain provisions to liberalize trade in services may include additional general exceptions that are inspired by general exceptions found in the GATS. Illustrative of these EIIAs is the Free Trade Agreement between the European Community and Chile, article 135 of which provides that:

*Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between the Parties where like conditions prevail, or a disguised restriction on trade in services, financial services or establishment, nothing in this Title shall be construed to prevent the adoption or enforcement by either Party of measures:*

- (a) necessary to protect public morals or to maintain public order and public security;*
- (b) necessary to protect human, animal or plant life or health;*
- (c) relating to the conservation of exhaustible natural resources if such measures are applied in conjunction with restrictions on the domestic supply or consumption of services or on domestic investments;*
- (d) necessary for the protection of national treasures of artistic, historic or archaeological value;*
- (e) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Title including those relating to:*
  - (i) the prevention of deceptive and fraudulent practices or to deal with the effects of a default on services contracts;*
  - (ii) the protection of the privacy of individuals in relation to the processing and dissemination of personal data and the protection of confidentiality of individual records and accounts; or*
  - (iii) safety.*

Another version of this provision, reflecting somewhat different concerns, appears in the Free Trade Agreement between Singapore and the United States, article 13.4 of which states that:

- 1. Nothing in this Chapter shall be construed to prevent either Party from imposing or enforcing measures:*
  - (a) necessary to protect public morals, order, or safety;*
  - (b) necessary to protect human, animal, or plant life or health;*
  - (c) necessary to protect intellectual property; or*
  - (d) relating to products or services of handicapped persons, of philanthropic institutions, or of prison labor, provided that such measures are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on international trade.*
- 2. The Parties understand that paragraph 1(b) includes environmental measures necessary to protect human, animal, or plant life or health.*

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The scope of an EIIA in relation to investment may be determined — in addition to by defining key terms — through exclusion by the general exceptions that take certain actions on the part of the parties outside the application of the agreement. Parties have excluded a wide variety of matters from the coverage of EIAs, including matters relating to national security, the preservation of public order, preservation of the environment and protection of the cultural patrimony. Certain social welfare programmes have also been excluded. Broad exceptions can undermine the efficacy of the agreement. However, certain interests can be important enough to justify exceptions to the treaty's general provisions.

### c. Special exceptions

The scope of the investment commitments in an EIIA is also determined by a variety of special exceptions, often included to address specific developmental concerns. The underlying theoretical assumption of an EIIA, of course, is that implementation of the general rules of the agreement on investment will promote economic development. EIAs, however, sometimes adopt the position that *not* implementing the general rules of the agreement in certain cases will promote economic development. Thus, EIAs often contain provisions allowing all or certain parties to deviate from the treaty's general rules on investment, or from specific provisions thereof, in certain circumstances. These provisions are intended to preserve for host country parties, in particular for the less developed parties, sufficient discretion to pursue developmental objectives in ways that otherwise may be difficult to reconcile with treaty obligations. Some approaches used in existing EIAs are described below.<sup>72</sup>

One approach is to allow special transitional periods during which less developed parties to an EIIA assume obligations gradually. Thus transitional periods may be different for different countries, depending upon the relative state of their development vis-à-vis other parties. For example, article 7(3) 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 Vietnam which shall do so not later than 2010.*

Another example is Decision 439 of the Commission of the Andean Community establishing a General Framework of Principles and Rules for Liberalizing Trade in Services in the Andean Community. This Decision includes a provision for preferential treatment for Bolivia and Ecuador regarding temporal exceptions. Article 22 provides that:

*[p]referential treatment for Bolivia and Ecuador shall be given consideration during such negotiations as are carried out in the context of this General Framework, with regard to deadlines and temporary exceptions for compliance with their obligations, in keeping with the provisions of the Cartagena Agreement.*

A second approach is to allow existing exceptions to the principles of the EIIA to remain in place. An example of this approach is article 52 of the Partnership and Cooperation

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<sup>72</sup> For a detailed discussion of special exceptions used for development purposes see UNCTAD (2000a).

Agreement between the European Community and the Russian Federation. This article introduces free movement of capital between residents of the Community and residents of the Russian Federation in the form of direct investment. Article 52(3) authorizes the Russian Federation to apply pre-existing restrictions on outward direct investment by Russian residents. This approach is also 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. Thus, in the previous example of the EC-Russian Federation Partnership and Cooperation EIIA, article 52(5) provides that *"Five years after the entry into force of this Agreement the Parties agree to consult over the maintenance of these restrictions ..."* The implication of article 52(5) is that, after the transitional period, the Russian Federation might or might not be allowed to continue to maintain the restrictions on outward direct investment by Russian residents.

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 from others throughout the process of implementing the agreement. Such an approach is found in the Caribbean Community (CARICOM). For example, article 37 of the Treaty Establishing the Caribbean Community provides that:

*[t]he Council shall examine ways and means for the introduction of a scheme for the regulated movement of capital within the Common Market giving particular attention to the development needs of the Less Developed Countries and shall recommend to Member States proposals for the establishment of such a scheme.*

Article 85(1) of the partnership agreement between the African, Caribbean and Pacific States and the European Community similarly provides that:

*[t]he 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 all parties to deviate 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. For example, article 34 of the Agreement on Trade, Development and Cooperation between the European Community and South Africa provides that:

*[w]here one or more Member States of the Community, or South Africa, is in serious balance of payments difficulties, or under threat thereof, the Community or South Africa, as the case may be, may, in accordance with the conditions established under the General Agreement on Tariffs and Trade and Articles VIII and XIV of the Articles of Agreement of the International Monetary Fund, adopt restrictions on current transactions which shall be of limited duration and may not go beyond what is necessary to remedy the balance of payments situation. The Community or South Africa, as the case may be, shall inform the other Party forthwith and shall submit to it as soon as possible a timetable for the elimination of the measures concerned.*

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Similar provisions are included, for instance, in the context of the Economic Partnership Agreement between the EC and Mexico,<sup>73</sup> and in some of the Euro-Mediterranean agreements. The Free Trade Agreement between Colombia, Mexico and Venezuela also provides for the possibility of temporarily limiting transfer on a non-discriminatory basis in case of balance-of-payments difficulties. Similarly, the FTA between the EFTA States and Mexico provides, in article 50(1), for the possibility of adopting restrictive measures that "*shall be equitable, non-discriminatory, in good faith, of limited duration and may not go beyond what is necessary to remedy the balance of payments situation*". The free trade agreements between Mexico and El Salvador, Guatemala and Honduras and between Central America and the Dominican Republic provide that the measures have to be compatible with internationally acceptable criteria.

As the foregoing examples show, the balance-of-payments exception often includes conditions to limit the impact and duration of measures taken thereunder. Some EIAs contain detailed provisions in this respect. For example, article 15(1) of the Framework Agreement on the ASEAN Investment Area provides that:

*[i]n the event of serious balance of payments and external financial difficulties or threat thereof, a Member State may adopt or maintain restrictions on investments on which it has undertaken specific commitments, including on payments or transfers for transactions related to such commitments. It is recognized that particular pressures on the balance of payments of a Member State in the process of economic development or economic transition may necessitate the use of restrictions to ensure, inter alia, the maintenance of a level of financial reserves adequate for the implementation of its programme of economic development or economic transition.*

Article 15(3) imposed some restrictions on the measures, however. The measures:

- a. shall not discriminate among Member States;*
- b. shall be consistent with the Articles of Agreement of the International Monetary Fund;*
- c. shall avoid unnecessary damage to the commercial, economic and financial interests of any of Member State;*
- d. shall not exceed those necessary to deal with the circumstances described in paragraph 1; and*
- e. shall be temporary and be phased out progressively as the situation specified in paragraph 1 improves.*

A treaty may contain a more general safeguard provision. For example, article 14 of the Framework Agreement on the ASEAN Investment Area authorizes emergency safeguard measures. It provides that:

- 1. 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 States may take emergency safeguard measures to the extent and for such period as may be necessary to prevent or to remedy such injury. The measures taken shall be provisional and without discrimination.*

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<sup>73</sup> Article 31 of Decision No. 2/2001 of the European Union and Mexico Joint Council of 27 February 2001, Implementing Articles 6, 9 12(2)(b) and 50 of the Economic Partnership, Political Coordination and Cooperation Agreement.



2. *Where emergency safeguard measures are taken pursuant to this Article, notice of such measures shall be given to the AIA Council within 14 days from the date such measures are taken.*
3. *The AIA Council shall determine the definition of serious injury and threat of serious injury and the procedures of instituting emergency safeguard measures pursuant to this Article.*

CARICOM has a similar provision. Article 47(1) of the Revised Treaty of Chaguaramas Establishing the Caribbean Community provides that:

*[w]here the exercise of rights granted under this Chapter creates serious difficulties in any sector of the economy of a Member State or occasions economic hardships in a region of the Community, a Member State adversely affected thereby may, subject to the provisions of this Article, apply such restrictions on the exercise of the rights as it considers appropriate in order to resolve the difficulties or alleviate the hardships.*

The treaty requires that the appropriate organ of CARICOM be notified of the measures and provides for a review of those measures. Article 47(4) states that:

- [t]he competent Organ shall give its earliest considerations to the programme, and:*
- (a) make a determination in respect of the appropriateness of the restrictions and whether they shall be continued; and*
  - (b) where it decides that the restrictions shall be continued, determine:*
    - (i) the adequacy of the programme; and*
    - (ii) the period for which the restrictions should continue.*

The competent Organ, in making a determination under subparagraph (b) of this paragraph, may impose such conditions as it considers necessary.

Article 47 imposes additional restrictions on the measures that may be adopted. For example, they must be confined to those necessary to resolve the difficulties in the affected sectors or to alleviate economic hardships in a particular region. The State imposing them must minimize damage to the commercial or economic interests of the other members, progressively relax them as conditions improve, and maintain them only as long as the conditions justify their application. Article 46 of the EFTA-Singapore free trade agreement permits future reservations as long as they do not “affect the overall level of commitments of that Party under this Chapter” and calls for biennial reviews of the reservations with a view to reducing their number.

In addition to special exceptions based on the specific development needs of EIIA member countries, subject-specific exceptions may be included allowing the parties to exclude certain matters from the application of individual provisions. A typical subject-specific exception relates to taxation. The difference between subject-specific exceptions and those discussed earlier in this section is that the former typically are permanent and apply to all parties, regardless of their development level. These are discussed in the relevant sections below.

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The scope of the investment provisions in an EIIA can also be affected by special exceptions that may apply only to certain parties or to certain provisions of the agreement, or for limited periods of time. Such provisions do not seek to take certain subjects outside the scope of the agreement entirely, but rather to define certain circumstances in which the normal application of the treaty will not occur. In many cases, these special exceptions are intended to enhance the development dimension of the agreement by permitting a party to deviate from the normal operation of the latter in order to promote a developmental objective. Such exceptions may be easier to obtain agreement on than general exceptions because they are temporary or applicable in only limited circumstances and thus do not undermine the general structure of the agreement.

## **2. *Investment Liberalization***

Investment liberalization provisions are those that reduce or eliminate barriers to the entry, establishment and operation of cross-border investment. EIAs contain either of two different provisions intended to remove legal and policy barriers to cross-border investment flows. The first is a provision that typically provides for rights of entry and establishment for investment in at least certain sectors of the economy. The second is a market access provision that generally provides for a right to provide services in at least certain sectors through a commercial presence in the host country. Recent EIAs frequently have both, and this gives rise to the possibility that certain investments will be covered by both provisions.

Some EIAs also have provisions intended to remove informational barriers to entry. These are transparency provisions that require the host country to make available certain information about the investment climate in its territory.

In addition, EIAs that seek to liberalize investment flows usually contain provisions intended to grant free transfer of funds related to such investment. Provisions allowing for entry of foreign personnel in relation to the investment, and those proscribing the imposition of performance requirements, are also associated with investment liberalization EIAs.

### **a. Admission and establishment of investment**

Unlike most BITs, EIAs often include commitments regarding the entry and establishment of investment with significant liberalization effects for the investment regimes of the parties. Under customary international law, States have the right to decide on the admission of foreign investors in their territory. It is therefore unlikely for a State to grant foreign investors an unrestricted right to invest. Usually a State will regard foreign investment in certain sectors of its economy as contrary to vital national interests, whether they are military, cultural or economic. Thus, when a right of establishment appears in an EIA, it is generally limited in some way. Three basic approaches are evident.

The strongest approach from the perspective of the foreign investor is to provide that investors originating in other member countries have a right to establish investment in the host member country, though usually subject to exceptions. The European Community and EFTA are typical examples of this approach. In the case of EFTA, article 23 of the EFTA Agreement provides that:

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*[w]ithin the framework of, and subject to, the provisions of this Convention, there shall be no restrictions on the right of establishment of companies, or firms, formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business in the territory of the Member States. This shall also apply to the setting up of agencies, branches or subsidiaries by companies or firms of any Member State established in the territory of any other Member State.*

*The rights of establishment shall include the right to set up, acquire and manage undertakings, in particular companies or firms... under the conditions laid down for its own undertakings by the law of the Member State where such establishment is effected....*

Article 23(3) authorizes the parties to set forth exceptions to the right of establishment in an annex and provides that the parties “*shall endeavor to eliminate gradually remaining discriminations...*” The parties also agree to review the annexes within two years “*with a view to reducing, and ultimately eliminating, the remaining restrictions*”. Article 23(4) prohibits the introduction of new restrictions on the right of establishment.

The European Community's exceptions to the right of establishment are set out in articles 45 and 46 of the Treaty of Rome, as amended. Article 45 states that:

*The provisions of this Chapter shall not apply, so far as any given Member State is concerned, to activities which in that State are connected, even occasionally with the exercise of official authority.*

*The Council may, acting by a qualified majority on a proposal from the Commission, rule that the provisions of this Chapter shall not apply to certain activities.*

Article 46 adds that.

*The provisions of this Chapter and measures taken in pursuance thereof shall not prejudice the applicability of provisions laid down by law, regulation or administrative action providing for special treatment for foreign nationals or on grounds of public policy, public security or public health.*

Language similar in effect to that in the EC and ETA agreements appears in the Framework Agreement on the ASEAN Investment Area, article 7(1) of which provides that “[s]ubject to the provisions of this Article, each Member State shall ... open immediately all its industries for investments by ASEAN investors.” The remainder of the article, however, provides the 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 safeguard measure in article 14, which provides that:

*[i]f, 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.*

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This approach to granting rights of establishment — which is also used in the OECD Code of Liberalisation of Capital Movements — has been followed by other EIAs signed by developing countries. The CARICOM Agreement specifically mentions right of establishment in article 35. This provision was later amended by a protocol prohibiting new restrictions on the establishment of nationals of other member countries, and obliging member countries to remove existing restrictions in accordance with a programme to be determined. A similar approach is followed in a number of African EIAs<sup>74</sup> that proclaim the granting of rights of establishment as a general principle, although they have yet to formulate the operational provisions that will give effect to such rights. The Community Investment Code of the Economic Community of the Great Lakes Countries (CEPGL) also contains provisions on rights of entry and establishment (article 6). However, these are preceded by a detailed regime for what are termed "joint enterprises" and "Community enterprises" (articles 2-5). In order to benefit from various advantages such classes of enterprises are subject to an authorization process. (UNCTAD, 1999b, pp. 24-25).

A second common approach is to provide for national and MFN treatment with respect to the right of establishment, again with a negative list of sectoral exceptions. For example, article 1102 of NAFTA provides that:

1. *Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.*
2. *Each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords, in like circumstances, to investments of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.*

Most-favoured-nation treatment with respect to the right of establishment is provided for in article 1103, which states that:

1. *Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to investors of any other Party or of a non-Party with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.*
2. *Each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords, in like circumstances, to investments of its investors of any other Party or of a non-Party with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.*

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<sup>74</sup> These include, for example, the Treaty Establishing the African Economic Community (AEC), the Treaty Establishing the Common Market for Eastern and Southern Africa (COMESA), the Treaty Establishing the East African Community, the Revised Treaty of the Economic Community of West African States (ECOWAS), the Treaty for the Establishment of the Economic Community of Central African States (ECCAS), and the Joint Convention on the Freedom of Movement of Persons and the Right of Establishment in the Central Africa Customs and Economic Union.

Article 1108, however, provides that these grants of national and MFN treatment are subject to exceptions listed in an annex. The NAFTA model has been followed by more recent agreements, especially those involving NAFTA signatories, but also increasingly between developing non-NAFTA countries.<sup>75</sup>

A number of EIAs concluded by the EC with third countries also follow this approach. The Agreement Establishing an Association between the European Economic Community and the United Republic of Tanzania, the Republic of Uganda, and the Republic of Kenya of 1969 (the first EC association agreement, which has since been superseded) provided already for a right of establishment based on MFN treatment. Since the 1990s, association agreements and partnership and cooperation agreements concluded by the EC with European economies in transition have also addressed establishment issues and provided for national treatment with regard to the establishment and operation of companies and nationals. These commitments are generally subject to transitional periods. Some agreements include a list of reservations to the establishment obligations. Some partnership and cooperation agreements, such as the one with the Russian Federation, provide only for MFN treatment in the pre-establishment phase (article 28), although the importance of moving towards the granting of national treatment is recognized.

The scope of the right of establishment depends on how "investor" is defined. This is because the right to national or MFN treatment with respect to establishment of investors from member countries is linked to the treatment provided to investors of the host country party, or any other party, or a non-party country/s. For example, if the definition of "investor" is broad enough to include State entities, covered investors with a right of national treatment with respect to establishment would have the right to establish investment in sectors of the economy in which the host country/s has itself made investments. This, again, illustrates the critical role that the definitions provisions play in determining the content of substantive provisions.

Note that neither of the approaches described typically provides for an unlimited right of establishment. They typically provide for a general right, subject, in some cases, to limited exceptions and, in most cases, to a negative list of exceptions included in an annex, which in theory can be as extensive as the parties wish. Indeed, the negative list could be so extensive as to effectively eliminate any right of establishment, and, as a practical matter, the compilation of a lengthy negative list could prompt objections from another party to the EIA, which could delay or even prevent the eventual conclusion of the agreement. Either of these approaches also could be utilized with a "positive list," so that the right would apply only in those sectors listed in an annex. Admission and establishment provisions in existing EIAs, however, have most commonly used the negative list approach. As will be shown below, the positive list, by contrast, is more often utilized in market access provisions for trade in services, which in fact overlap with admission and establishment investment provisions. It appears, however, that some recent EIAs are moving closer to the positive list approach also with respect to their investment liberalization commitments (see below).

A third approach is simply to provide for future liberalization. For example, the Euro-Mediterranean agreements concluded by the European Community call for future creation of a

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<sup>75</sup> This is the case, for example, of the Canada-Chile Free Trade Agreement, the Mexico Singapore FTA, the FTA between Mexico and El Salvador, Guatemala and Honduras, the Agreement between the United States and Viet Nam on Trade Relations. A similar approach was also followed by the Agreement between New Zealand and Singapore on Closer Economic Relationship.



right of establishment and opening of the services market to foreign competition. Article 31 of the agreement with Morocco provides that:

1. *The Parties agree to widen the scope of this Agreement to cover the right of establishment of one Party's firms on the territory of the other and liberalisation of the provision of services by one Party's firms to consumers of services in the other.*
2. *The Association Council will make recommendations for achieving the objective described in paragraph 1....*
3. *The Association Council will make a first assessment of the achievement of this objective no later than five years after this Agreement enters into force.*

This third 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. A number of EIAs created by developing countries follow a combination of this approach and the first approach. Thus, as noted earlier, the COMESA Agreement (article 164) and the Treaty Establishing the African Economic Community provide, as a general principle, for the right of establishment for investors from signatory countries, and then make commitments to give effect to these rights at a future date through the conclusion of protocols. Similarly, the ECOWAS Revised Treaty, in articles 3(2) and 55, commits members to the removal of obstacles to the right of establishment within five years of the creation of a customs union between member States.

The admission and establishment of investment provisions, like those prescribing the scope of the EIA, determine the reach of the agreement as a practical matter. If an EIA grants no right of establishment, investment can be established in a host country party, and thereby become subject to the protection of the treaty, only if the host country permits the investment under its local law, which it may change at any time. As investments are permitted or forbidden, the reach of the agreement as a practical matter changes. Thus, an EIA may address some of the concerns of its members about the advisability of protecting investment from other parties by allowing individual members to retain the right to exclude investment and thereby prevent investment from being established. This approach is typical of EIAs that provide for investment protection but not liberalization. For example, the ASEAN Agreement on the Reciprocal Promotion and Protection of Investments provides for MFN and fair and equitable treatment after entry. This provision is modelled on the traditional European BITs, in which the admission of investments is to be decided by the parties in accordance with the national laws.

An alternative approach is to permit investment, but subject to certain restrictions the existence of which serves to allay the host country concerns about the investment. For example, under Decision 24 of the Commission of the Andean Pact (superseded by Decision 291), article 38, member countries were explicitly allowed to reserve sectors of economic activity for its private or public national undertakings and decide whether joint undertakings could participate in them. The article further allowed the Commission of the Cartagena Agreement, on a proposal of the Board, to determine the sectors that all member countries should reserve for national public or private undertakings, and decide whether joint undertakings might participate in them. To qualify as a joint undertaking, Article 1 of Decision 24 required that the undertaking:

*is established in the recipient country and between 51 and 80 percent of which capital belongs to national investors; provided that in the opinion of the competent authority this*

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*proportion is reflected in the technical, financial, administrative and business management of the undertaking.*

These restrictions, however, had to be consistent with the provisions of the treaty. A ban on performance requirements or a guarantee of national treatment could prevent the host country from imposing certain restrictions on the investment, leaving it with the choice of allowing the investment without the desired restrictions or excluding it. Decision 292 of the Commission of the Cartagena Agreement, revising the preferential regime for Andean Multinational Enterprises, provides, in article 14, that Andean enterprises may participate in economic sectors reserved for national companies in accordance with the respective legislation of the member States. Thus Andean countries were given broad discretion with respect to granting rights of establishment within the Andean Community on a national treatment basis. To qualify for Andean multinational company status, the property contributions from national investors from two or more Andean countries had to exceed 60 per cent of the company's capital.

Yet another alternative to limiting the right of establishment is to agree only to a narrow definition of investment, which would have the effect of excluding from treaty protection certain investments permitted by the host country (see section IV.A.1.a). This approach, however, could discourage the establishment of some desirable investments.

As noted earlier, another approach to the right of establishment is for it to be granted only when a party makes commitments on liberalization of specific industries and measures. This approach is similar to the positive list approach of the GATS in relation to services. The FTA between Australia and Thailand provides in article 904:

*In all sectors inscribed in Annex 8, and subject to any conditions and qualifications set out therein, each Party shall accord to investments of the other Party treatment no less favourable than it accords, in like circumstances, to its own investors, with respect to the establishment and acquisition of investments in its territory.*

The recently adopted agreement between ASEAN and China commits the parties to enter into negotiations in order to, *inter alia*, progressively liberalize their investment regimes. While there are no firm commitments as yet on specific liberalization negotiations, the wording of this clause suggests that future liberalization of investment under this agreement would take an approach similar to the *positive list liberalization model* represented by GATS. A similar approach is also found in the South Asian Free Trade Agreement, and in the BIMSTEC framework agreement.

Thus far the discussion has focused on approaches to the liberalization of investment between the members of an EIIA. However, as noted before (chapter III.B.3), some EIAs explicitly address the admission of foreign investment by non-members. The admission provisions in these cases are typically more restrictive than their intra-EIIA counterparts. Thus, as was noted earlier, while the MERCOSUR Protocol on Protection and Promotion of Investments within MERCOSUR allows rights of establishment to firms within the subregion, on the basis of national and MFN treatment, the MERCOSUR Protocol on Protection and Promotion of Investments from Third Parties provides that investments from non-MERCOSUR members must be admitted in accordance with the members' local laws.

Some early EIAs, such as the Andean Pact Commission Decision 24 (superseded by Decision 291), subjected the entry of investment from third countries to strict controls. Thus

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article 2 of Decision 24 required that all investment from third countries be subject to previous authorization by the competent national authorities, which should assess whether the application met the development priorities of the receiving country.

Yet other agreements explicitly adopt an open door policy with respect to cross-border movements of capital from third countries. The European Community Treaty, for example, provides in article 56(1) that “all restrictions on the movement of capital...between Member States and third countries shall be prohibited”. Article 56(2) provides that “all restrictions on payments...between Member States and third countries shall be prohibited”. Article 57 *et seq.* allow certain narrow exceptions.

Finally, yet other agreements commit to grant rights of establishment for investments from third countries at a future date. In the Framework Agreement on the ASEAN Investment Area, the date for liberalizing the establishment of investments from non-member countries of ASEAN is set for the year 2020, subject to exceptions provided for in the Agreement (article 4(6)).

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A country entering an EIIA has a number of options concerning the extent, if any, of investment liberalization to be provided by the treaty. The treaty can provide for future liberalization or it can incorporate liberalization commitments that take effect at the time of entry into force of the agreement. Assuming that liberalization will be an element of the treaty, the parties will need to decide whether they wish to grant broad rights of establishment subject to a limited set of exceptions, or to employ a positive or a negative list approach to determine the sectors or measures to which liberalization commitments apply or do not apply under the agreement. In the event that the negative list approach is selected, the country must be prepared to specify the sectors to be excluded from the liberalization obligation. If the positive list approach is selected, typically commitments will be added sector by sector over time. The negative list approach requires greater effort during treaty negotiations since the list must be compiled before the treaty can be concluded, and would seem to require a higher level of expertise and preparation than a positive list approach, under which liberalization commitments are made incrementally over a long period of time. Furthermore, a party may raise objections if it perceives that another party is preparing a negative list that is too lengthy and undermining the purpose of the liberalization commitments. A positive list approach, on the other hand, is likely to result in less liberalization initially and the host country may find that, once the agreement is concluded, opposition from affected industries may make it difficult to add sectors to the positive list in the future, with the result that inefficient industries are protected and an important purpose of the EIIA, namely to promote the competitiveness of the local economy, is thereby undermined.

Liberalization provisions, by opening the borders to certain investments, along with the definition provisions, determine the scope of investments that ultimately will be covered by the treaty. Countries that are concerned about the effect of certain protection provisions may curtail the extent of their liberalization obligations so as to preserve the right to exclude investments that they are not prepared to protect fully. Exclusion of an investment, however, denies the host country all benefits attributable to that investment. An alternative is to accept broad liberalization commitments while limiting the effect of the protection provisions, by drafting them narrowly, by creating exceptions to them, or by including reservations in a positive list of sectors in which liberalization is to be achieved.

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## b. Market access for services

During the Uruguay Round of trade negotiations, many EIAs began to include provisions on trade in services. Because one of the modalities by which services are delivered is through a commercial presence, and because a commercial presence usually falls within even a narrow definition of investment, agreements regarding trade in services very often affect investments. In other words, many agreements that liberalize trade in services provide what, in effect, is a right of establishment in the services sector that potentially overlaps any right of establishment of investment set forth elsewhere in the agreement.

Five general approaches are evident with respect to providing market access for services.

The first approach is to include a general commitment to future liberalization of trade in services. Typical of these agreements are many of the free trade agreements concluded by EFTA with transition economies and other States. For example, article 27 of the agreement with the former Yugoslav Republic of Macedonia provides that:

*[t]he Parties recognize the growing importance of services and investments. In their efforts to gradually develop and broaden their co-operation, in particular in the context of European integration, they will co-operate with the aim of further promoting investments and achieving a progressive liberalization and mutual opening of markets for trade in services, taking into account on-going work under the auspices of the WTO.*

That article also provides that the parties will review developments in the services sector with a view to considering liberalization measures.

The association agreements between the European Community and various transition economies go several steps further in their commitment to liberalize investment in services. For example, article 56 of the agreement with Romania provides that:

*[t]he Parties undertake in accordance with the provisions of this Chapter to take the necessary steps to allow progressively the supply of services by Community or Romanian companies or nationals who are established in a Party other than that of the person for whom the services are intended taking into account the development of the services sector in the Parties.*

A stronger and more elaborate provision for future liberalization appears in the ASEAN Framework Agreement on Services. Article III provides that:

*[m]ember 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(1) 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*

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*on an MFN basis*". These commitments are to be set out in a schedule. Under Article X, they may be modified or withdrawn after three years, provided that compensatory adjustments are made. This first approach does not by itself result in any liberalization, but does start the parties on a course towards liberalization in the future.

A second approach, which appears in the Euro-Mediterranean Agreements concluded by the European Community, is to affirm or incorporate the parties' commitments under the GATS. For example, article 29 of the agreement with Egypt "reaffirms" the parties' GATS commitments, particularly those relating to MFN treatment, and also incorporates the exceptions to MFN treatment provided for by the GATS. This second approach also does not result in any liberalization, since it affirms only liberalization that has already occurred 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, it could be argued that GATS commitments become commitments under the EIIA as well and that any violation of those GATS commitments would also violate the EIIA and be subject to any applicable dispute resolution mechanism under the EIIA as well as under the GATS. This in turn could result in multiple proceedings to remedy an alleged violation of the obligation.

A third approach is to include in the EIIA a chapter on services that is structured similarly to the GATS. A number of countries, including the United States, Australia, Chile and Singapore, have recently begun to conclude agreements adopting this approach. Illustrative is the Agreement between Japan and the Republic of Singapore for a New-Age Economic Partnership. 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. 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. For example, it provides that domestic regulation of trade in services shall be administered in a reasonable, objective and impartial manner and requires that parties provide judicial or administrative review for decisions affecting trade in services. 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 fourth approach is to include market access commitments structured differently from those that appear in the GATS. Illustrative of these EIAs is the NAFTA, in which articles 1202 and 1203 guarantee national and MFN treatment with respect to the supply of services, subject to exceptions contained in an annex. Article 1208 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 has separate chapters dealing with telecommunications and financial services. The NAFTA approach is to create a general rule of market access in all service sectors, subject to exceptions contained in an annex, often referred to as the "negative list" approach. This differs from the third approach described above, as well as the approach used in the GATS, under which liberalization occurs only in those sectors listed in the annex, the so-called positive list approach.

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As noted earlier (in relation to admission and establishment of investment), the fourth (negative list) approach tends to provide greater liberalization than the third (positive list) approach, since it presumes liberalization in all sectors not listed. This is likely to be an approach selected by countries considering an immediate, large-scale liberalization of trade in services, as opposed to the more incremental approach of the positive list. The negative list approach also requires a much greater level of preparation to negotiate, inasmuch as the parties must be able to list all sectors in which liberalization is not desired at the time they prepare the negative list. The positive list approach allows the parties to identify over time those sectors in which liberalization is or is not desired and then to add them to the list only as appropriate.

A fifth approach is to provide freedom of movement of services subject to some exceptions, which are applied in a restrained manner. The European Community Treaty (consolidated text) represents this approach. It establishes an internal common market characterized by *inter alia* the free movement of services between the member States. This principle is given effect by article 49, which provides that:

*Within the framework of the provisions set out below, restrictions on freedom to provide services within the Community shall be progressively abolished during the transnational period in respect to nationals of Member States who are established in a State of the Community other than that of the person for whom the services are intended.*

One important complement to the provision of market access for supply of services is the recognition of the professional qualifications of service providers. Article 47(1) of the European Community Treaty (consolidated text) provides for the issuance of directives for the mutual recognition of diplomas, certificates and other evidence of formal qualifications, although the stated purpose is to facilitate self-employment rather than employment in connection with an investment. The agreements of association between the European Community and some of the transitional economies contain a similar provision, though without an explicit link to the goal of self-employment. For example, article 47 of the treaty with Romania, which falls within Title IV on Movement of Workers, Establishment and Supply of Services, provides that:

*[i]n order to make it easier for Community nationals and Romanian nationals to take up and pursue regulated professional activities in Romania and the Community respectively, the Association Council shall examine which steps are necessary to be taken to provide for the mutual recognition of qualifications. It may take all necessary measures to that end.*

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In the light of the GATS, the issue whether to include a commitment to provide market access for services may well arise in the context of an EIIA negotiation. If so, the parties must consider how market access commitments in the EIIA interact with commitments made in the GATS and how they interact with other commitments in the EIIA, particularly those relating to establishment and treatment of investment as well as dispute resolution.

### **c. Transparency**

EIIAs tend to include general transparency provisions imposing obligations on EIIA members to disclose certain types of governmental information relevant to investment relations.

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Sometimes these provisions are included in a separate chapter on transparency that applies to the entire agreement.<sup>76</sup> Generally, provisions in a transparency chapter tend to be broader and more detailed than transparency provisions included in an investment chapter. In relation to investment, transparency provisions found in EIAs are of two types.

The first type of transparency provision essentially requires the host State to make certain kinds of existing information available. This type of provision 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. For example, article III-B of the ASEAN Agreement on the Promotion and Protection of Investment provides that:

*Each Contracting Party shall ensure the provision of up-to-date information on all laws and regulations pertaining to foreign investment in its territory and shall take appropriate measures to ensure that such information be made as transparent, timely and publicly accessible as possible.*

Another obligation is to provide information to the other parties. For example, article 11(2) of the Framework Agreement on the ASEAN Investment Area provides that:

*[e]ach Member State shall promptly and at least annually inform the AIA Council of the introduction of any new or any changes to existing laws, regulations or administrative guidelines which significantly affect investments or its commitments under this Agreement.*

This first type of transparency provision often appears in EIAs as a form of cooperation to promote investment, with information sharing seen as one element of that cooperation. For example, the Euro-Mediterranean agreement between the European Community and Egypt includes a title on economic cooperation covering an entire range of matters, including education, science and technology, industrial cooperation, investment promotion and tourism. Article 46, on investment promotion, lists among the modalities of investment promotion

- appropriate means of identifying investment opportunities and information channels on investment regulation;*
- providing information on European investment regimes (such as technical assistance, direct financial support, fiscal incentives and investment insurance) related to outward investments and enhancing the possibility for Egypt to benefit from them;*

Transparency provisions of this type may also feature in EIAs in the context of the implementation of their liberalization or other commitments. For example, the Treaty Establishing the Caribbean Common Market, as regards establishment, provides in article 35(3) as follows:

*A Member State shall notify the Council within such period as the Council may decide of particulars of any restrictions which it applies in such a way that persons belonging to another Member State are accorded in the first-mentioned State less favourable treatment in respect of matters set out in paragraph 1 of this Article that is accorded to persons belonging thereto.*

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<sup>76</sup> An example of this approach is the Agreement between the United States and Viet Nam on Trade Relations.



Similarly, the OECD Code of Liberalization of Capital Movements provides in article 11(a):

*a. Members shall notify the Organization, within the periods which the latter may determine, of the measures of liberalization which they have taken and of any other measures which have a bearing on this Code, as well as of any modifications of such measures.*

The second type of transparency provision imposes on the parties a general obligation of transparency in their dealings with investors. 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 :

*[e]ach Party shall, in accordance with the provisions of this Chapter, create and maintain stable, equitable, favourable and transparent conditions for investors of other Parties to make investments in its territory.*

Also, Article 159 of the Treaty Establishing the Common Market for Eastern and Southern Africa provides that member States shall “*create and maintain a predictable, transparent and secure investment climate...*” Although this type of clause at first glance may seem weak because it imposes no very specific obligation, it is potentially the most sweeping of the transparency provisions because it could apply to a wide variety of circumstances. This second type of provision thus requires not simply making existing information available, but also a certain mode of behaviour by the host State in dealing with covered investments. For example, this provision 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 is defined in much more specific terms and explicitly includes a right to participate in decision-making. Thus, a few recent EIAs contain transparency obligations with respect to draft laws and regulations. These obligations usually require parties to make public or notify their proposed laws or regulations with a view to affording interested parties the possibility of commenting on such laws before they are formally adopted. For example, NAFTA article 1802 provides that:

*to the extent possible, each Party shall*  
*(a) publish in advance any such measure it proposes to adopt ; and*  
*(b) provide interested persons and Parties a reasonable opportunity to comment on such proposed measures.*

Similarly, article 3 of Chapter IV on "Transparency-related Provisions of the Free Trade Agreement between the United States and Viet Nam" also provides to nationals of the parties, and not only to the parties themselves,

*the opportunity to comment on the formulation of laws, regulations and administrative procedures of general application that may affect the conduct of business activities covered by this Agreement.*

Transparency requirements that tend to enhance the level of participation of foreign actors in national legislative processes have recently been extended to national administrative

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proceedings. Thus, article 19.5 of the 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 Singapore-United States agreement also provides for a right of review and appeal of administrative decisions regarding matters covered by the agreement. Article 19.6 provides that:

- [e]ach Party shall ensure that, in any such tribunals or procedures, the parties to the proceeding are provided with the right to:*
- (a) *a reasonable opportunity to support or defend their respective positions; and*
  - (b) *a decision based on the evidence and submissions of record or, where required by domestic law, the record compiled by the administrative authority.*

Although these provisions are included in the chapter entitled “Transparency,” they expand upon the traditional concept of transparency, which is essentially access to information. By providing not only for notice of certain proceedings, but also an opportunity to be heard and a right of appeal, the Singapore-United States free trade agreement stretches the concept of transparency to include elements of due process.

The expansion of the traditional concept of transparency to include due process rights is significant because of the presence in some agreements of general obligations of transparency. These general obligations of transparency may be interpreted in the future to include not only an obligation to allow access to information, but also a right to participate in decision-making and a right to a decision of a certain quality.

Often, investors are required to meet transparency obligations under EIAs. Some EIAs explicitly include an obligation to that effect. For example, Article 17-09 of the Free Trade Agreement between Colombia, Mexico and Venezuela provides that each party may require an investor of another party, notwithstanding national and MFN obligations, to provide information about the particular investment, consistent with applicable laws in the State party. Similarly, article 111 (2) of NAFTA grants each party the right:

*to require an investor of another party or its investment in its territory, to provide routine information concerning that investment solely for informational or statistical purposes.*

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Transparency provisions allow participants in the investment process to obtain information from each other in order to make informed decisions and meet obligations and commitments. Transparency provisions in EIAs are usually formulated in general terms, imposing obligations on all parties to the agreement. Similarly, transparency obligations can be

extended to investors. A second key issue relates to the degree of intrusiveness of transparency obligations in EIAs. Clearly, the deeper the integration between national economies, the greater the impact that such obligations will have on national policies.

From the perspective of developing countries, as a matter of practical importance, the question arises of the costs involved in determining the scope of transparency provisions. Where transparency obligations demand a broad range of items and tight procedures, some developing countries may encounter problems. In these situations, less developed countries may be allowed additional time to adapt to the requirements of compliance. At the same time, provisions on transparency are important for fostering institutional strengthening and the promotion of the rule of law, especially in developing countries.<sup>77</sup>

#### d. Transfer of funds

Provisions granting free transfer of funds are among the most common in EIAs seeking to liberalize and/or protect investment. A typical provision guarantees to investors the right to transfer their investment and any returns from their investment into a freely convertible currency. This provision typically specifies the payments the transfer of which is protected. Many EIAs protect the transfer out of the territory of any payments related to an investment, including both the original investment and any returns on that investment. Some EIAs, particularly when they include a right of admission of investment, also protect transfers into the territory of the host country. EIAs generally prescribe a minimum standard of treatment to be afforded to such payments, including specification of the currency into which transfer is to be permitted and the rate of exchange to be used.

A typical approach is that taken by NAFTA. Article 1109(1) of NAFTA specifies that all transfers relating to an investment must be freely permitted, but then includes an illustrative, non-exclusive listing of transfers that must be permitted. It provides that:

*[e]ach Party shall permit all transfers relating to an investment of an investor of another Party in the territory of the Party to be made freely and without delay. Such transfers include:*

- (a) profits, dividends, interest, capital gains, royalty payments, management fees, technical assistance and other fees, returns in kind and other amounts derived from the investment;*
- (b) proceeds from the sale of all or any part of the investment or from the partial or complete liquidation of the investment;*
- (c) payments made under a contract entered into by the investor, or its investment, including payments made pursuant to a loan agreement; (d) payments made pursuant to Article 1110 [relating to compensation for expropriation];*
- (e) payments arising under Section B [relating to investor-state dispute resolution].*

Section 1109(2) specifies the currency and the exchange rate. It states that:

*[e]ach Party shall permit transfers to be made in a freely usable currency at the market rate of exchange prevailing on the date of transfer with respect to spot transactions in the currency to be transferred.*

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<sup>77</sup> For an in-deep discussion of transparency issues in IIAs, see UNCTAD (2004a).

In some cases, the specified transfers are described in general terms. For example, article 46 of the Free Trade Agreement between the EFTA States and the United Mexican States provides that:

*[t]he 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.*

Some EIAs apply only to certain specified transfers. The specification in these cases tends to be rather detailed. For example, article VII of the ASEAN Agreement on the Promotion and Protection of Investment provides that:

- 1) *Each Contracting Party shall, subject to its laws, rules and regulations, allow without unreasonable delay the free transfer in any freely-usable currency of:*
  - a) *the capital, net profits, dividends, royalties, technical assistance and technical fees, interests and other income, accruing from any investments of the nationals of companies of the other Contracting Parties*
  - b) *the proceeds from the total or partial liquidation of any investments made by nationals or companies of the other Contracting Parties;*
  - c) *funds in repayment of loans given by nationals or companies of one Contracting Party to the nationals or companies of another Contracting Party which both Contracting Parties have recognized as investments;*
  - d) *the earnings of nationals of the other Contracting Parties who are employed and allowed to work in connection with an investment in its territory.*
- 2) *The exchange rate applicable to such transfers shall be the rate of exchange prevailing at the time of remittance.*

The use of general language similar to that appearing in NAFTA is clearly more inclusive than more specific language since it refers to *all* transfers. On the other hand, EIA transfer provisions that apply only to specific transfers are usually quite broad and include most types of payments that an investor would wish to repatriate. Indeed, given that the list of covered payments is usually rather broad, it might be questioned whether there is much additional risk for the host State in specifying that the provision applies to all transfers.

The phrase “all transfers relating to an investment” or similar language appears to be broad enough to apply to transfers into as well as out of the host State. That is, it creates a right not only to repatriate capital, but also to bring capital into the host State’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, which could permit the investor otherwise to circumvent host State regulations on admission of investment.

On the other hand, provisions that list the types of payments covered generally refer only to payments that would be transferred out of the territory. Of course, the general language in NAFTA, and similar provisions in other agreements, could be modified so that it applies only to transfers out of the territory of the host State, thus preserving its generality, but making clear that it applied to outward, not inward, transfers. This would appear to be relevant in particular in

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cases where an EIIA grants a right to free transfer of funds but does not provide for rights of establishment. Such is the case, for example, with the Euro-Mediterranean agreements, which include a prohibition on future restrictions on movements of capital and current payments, with some exceptions, but their commitments to grant rights of establishment for investments are postponed to a future date.

Transfer provisions in EIAs may raise 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 transfer might result in massive capital flight during times of economic difficulty, thus exacerbating the host country's problems. For these reasons, EIAs often limit the right of free transfers in some way.

One approach is to implement the right of free transfer gradually. This approach is typical of the association agreements and the partnership and cooperation agreements between the European Community and economies in transition. These agreements often explicitly recognize that the transition economies are still in a process of gradual liberalization and provide for implementation over time of the obligation to ensure free transfer of payments related to an investment. For example, article 60 of the EC agreement with Bulgaria, dealing with current payments, provides that:

*The Contracting Parties undertake to authorize, in freely convertible currency, any payments on the current account of balance of payments to the extent that the transaction underlying the payments concern movement of goods, services or persons between the Parties which have been liberalized pursuant to this Agreement.*

Article 61(1), dealing with capital movements, provides:

*[w]ith regard to transactions on the capital account of balance of payments, from the entry into force of this Agreement, the Member States and Bulgaria respectively shall ensure the free movement of capital relating to direct investments made in companies formed in accordance with the laws of the host country and investments made in accordance with the provisions of Chapter II of Title IV [dealing with competition policy] and the liquidation or repatriation of those investments and of any profit stemming therefrom.*

*Notwithstanding the above provision, such free movement, liquidation and repatriation shall be ensured by the end of the first stage referred to in Article 7 for all investments linked to establishment of branches and agencies of Community companies and of Community nationals establishing in Bulgaria as self-employed persons...*

Article 61(2) prevents the introduction of new restrictions on capital or current payments, although this obligation is phased in for Bulgaria. It provides that:

*Without prejudice to paragraph 1, the Member States, as from the entry into force of this Agreement, and Bulgaria as from the end of the fifth year following the entry into force of the Agreement, shall not introduce any new foreign exchange restrictions on the movement of capital and current payments connected therewith between residents of the Community and Bulgaria and shall not make the existing arrangements more restrictive.*

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This 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 flexibility for the host State once the transitional period has ended.

A second approach is to include an exception to the transfer provision during periods of balance-of-payments difficulties (see also under “Specific Exception”, chapter IV, A.3). Such a provision is fairly common in EIAs. They 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. One relatively elaborate such provision is article 12 of chapter 08 of the Free Trade Agreement between Australia and Singapore, which provides that:

1. *In the event of serious balance of payments and external financial difficulties or threat thereof, a Party may adopt or maintain restrictions on payments or transfers related to investments. It is recognized that particular pressures on the balance of payments of a Party in the process of economic development may necessitate the use of restrictions to ensure, inter alia, the maintenance of a level of financial reserves adequate for the implementation of its programme of economic development.*
2. *The restrictions referred to in Article 12.1 shall:*
  - (a) *be consistent with the Articles of Agreement of the International Monetary Fund;*
  - (b) *avoid unnecessary damage to the commercial, economic and financial interests of the other Party;*
  - (c) *not exceed those necessary to deal with the circumstances described in Article 12.1;*
  - (d) *be temporary and be phased out progressively as the situation specified in Article 12.1 improves;*
  - (e) *be applied on a national treatment basis and such that the other Party is treated no less favourably than any non-Party.*
3. *Any restrictions adopted or maintained under Article 12.1, or any changes therein, shall be promptly notified to the other Party.*
4. *The Party adopting any restrictions under Article 12.1 shall commence consultations with the other Party in order to review the restrictions adopted by it.*

A third approach is to explicitly subordinate the right of transfer to the parties’ exchange restrictions. Agreements in the African region sometimes adopt this approach. For example, article 2 of the Common Convention on Investments in the States of the Customs and Economic Union of Central Africa provides that:

- [w]ithin the framework of their exchange regulations, the member States of the Union shall guarantee the free transfer of:*
- (a) *Capital;*
  - (b) *Profits lawfully acquired;*
  - (c) *Funds arising from the transfer or winding-up of business activities.*
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The Community Investment Code of the Economic Community for the Great Lakes Countries subordinates the right to existing regulations. Article 8 provides that:

*[s]ubject to compliance with existing legislation governing exchange regulations, the CEPGL member States shall guarantee the freedom to transfer capital accumulated in regulated markets, duly earned profits and funds arising from share transfers or from the cessation of business by an enterprise.*

EIIAs may contain provisions on the transfer of funds applicable to both capital and current accounts. For example, the Euro-Mediterranean Agreement between the European Community and Egypt includes three separate articles on this issue. Article 31 addresses current payments. It provides that “*[s]ubject to the provisions of Article 33, the Parties undertake to authorize, in fully convertible currency, any payments to the current account*”. Article 32 addresses transfers concerning direct investment. It states that:

*[t]he Community and Egypt will ensure . . . the free circulation of capital for direct investments made in companies formed in accordance with the laws of the host country, and the liquidation or repatriation of the investments and of any profits stemming therefrom.*

The agreement also includes a balance-of-payments exception. Article 33 allows any party, when facing “*serious difficulties concerning balance of payments,*” to take restrictive measures with respect to current payments if such measures are “*strictly necessary*”.

Some earlier EIIAs specifically restricted the free movement of capital and transfer of funds, including through “fade out” provisions that mandated third-party investors to transfer their investments to investors within the region over a period of time. This is the case with regard to Decision 24 of the Commission of the Cartagena Agreement. Decision 291 removes the restrictions on transfer of funds, and obligates member countries to permit foreign investments and subregional investors to remit net profits from foreign direct investment and the proceeds from the sales or liquidation of such investment. However, Decision 291 does not tackle the issue of balance of payments.

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Transfer of funds provisions are among the investment liberalization/protection provisions that often give rise to the greatest concerns on the part of developing host countries. The adverse consequences of capital flight can be severe, at least in the short run. Sudden infusions of large amounts of capital can also have adverse economic consequences. Thus, an initial policy question is whether the transfer provision should apply only to outward flows or to inward flows as well. The question of whether to include inward flows is necessarily linked to the extent of investment liberalization provided by the agreement, although it is not exclusively an issue of investment liberalization. An existing investment may wish to transfer payments into the country to use in its operation. Thus, a right to transfer payments into the territory may also be seen as an investment protection issue.

Free transfer of payments out of a host country's territory raises concerns when foreign exchange reserves are low. Some EIIAs address this issue by including exceptions to the right of free transfer when exchange reserves are at low levels. As noted above, the concern may also be

addressed by excluding more volatile forms of investment, such as portfolio investment, from the coverage of the treaty, or by restricting the right to establish such investments in the first place. In other words, concerns about outward transfers also can be addressed through limitations on inward transfers.<sup>78</sup>

#### **f. Performance requirements**

Host countries sometimes impose requirements on foreign investment that are intended to shape the economic consequences of the investment. For example, in order to ensure that the investment contributes to employment or has a favourable 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 for permitting the investments to be established. Often also, these requirements are imposed as a condition to qualify for certain incentives.

Such requirements introduce barriers that may interfere with the investor’s ability to manage its investment and may impair the value of the investment. Apart from their impact on a particular investment, performance requirements may also distort trade by preventing the importation of goods or services that would otherwise occur or by requiring the exportation of goods or services that otherwise would not occur. For these reasons, the WTO Agreement on Trade Related Investment Measures (TRIMs) prohibits certain performance requirements that are inconsistent with the requirement of national treatment or the prohibition on quantitative restrictions under articles III(4) and XI(1) in the General Agreement on Tariffs and Trade (GATT).

Upon the adoption of the WTO TRIMs Agreement, negotiated during the Uruguay Round of Trade Negotiations, EIAs dealing with investment liberalization began to include prohibitions on certain performance requirements. In fact, some EIAs, such as the Free Trade Agreement between Canada and the United States, did so before the adoption of the TRIMs Agreement.

The concept of a performance requirement is potentially quite broad and not well defined. Thus, EIAs that address this issue do not prohibit performance requirements generally. Rather, they generally prohibit certain specific performance requirements. The list appearing in, for example, the Free Trade Agreement between Colombia, Mexico and Venezuela covers the same measures identified in TRIMs Agreement. The list that appears in NAFTA and in other recent FTAs concluded by the United States based on NAFTA goes beyond the measures listed by the TRIMs Agreement. NAFTA. Article 1106 provides that:

*No Party may impose or enforce any of the following requirements, or enforce any commitment or undertaking, in connection with the establishment, acquisition, expansion, management, conduct or operation of an investment of an investor of a Party or of a non-Party in its territory:*

- (a) to export a given level or percentage of goods or services;*
- (b) to achieve a given level or percentage of domestic content;*

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<sup>78</sup> For an in-depth discussion of the issues arising with respect of transfer of funds provisions, see UNCTAD (2000b).

- (c) to purchase, use or accord a preference to goods produced or services provided in its territory, or to purchase goods or services from persons in its territory;
- (d) to relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment;
- (e) to restrict sales of goods or services in its territory that such investment produces or provides by relating such sales in any way to the value or value of its exports or foreign exchange earnings;
- (f) to transfer technology, a production process or other proprietary knowledge to a person in its territory, except when the requirement is imposed or the commitment or undertaking is enforced by a court, administrative tribunal or competition authority to remedy an alleged violation of competition laws or to act in a manner not inconsistent with other provisions of this Agreement, or
- (g) to act as the exclusive supplier of the goods it produces or services it provides a specific region or world market.

Recognizing, however, that performance requirements may be regarded by some host countries as an important element of their economic development policy, NAFTA allows the parties to specify in an annex, and to maintain, exceptions to the prohibition on performance requirements. It should be noted that while performance requirements are often prohibited as a condition on the establishment of investment, the NAFTA provision prohibits them whether they are imposed as a condition of establishment or subsequent to establishment. In addition, the NAFTA provision, unlike the TRIMs Agreement, covers trade in goods as well as trade in services. Furthermore, NAFTA prohibits performance requirements imposed even on investments of non-parties, although it does not provide a mechanism by which an investment of a non-party or a non-party can enforce the prohibition.

EIIAs that follow NAFTA have included provisions that in some cases are more complex than the NAFTA provision, but that are quite similar conceptually. These may prohibit certain performance requirements that are imposed directly or, in some cases, required as a condition of receiving a benefit; they may apply the prohibition to performance requirements imposed on investments of investors of non-parties as well as of parties; and they may allow the parties to specify exceptions to the general prohibition. An example is article 15.8 of the Free Trade Agreement between Singapore and the United States.

As a result of the TRIMs Agreement prohibitions, some EIIAs, particularly those concluded by the European Community, require one or both parties to abide by the TRIMs agreement. For example, article 73 of the Association Agreement between the European Community and Estonia provides that “*Estonia shall honour the rules on Trade-Related Aspects of Investment Measures (TRIMs)*”. To similar effect is the Free Trade Agreement between CARICOM and the Dominican Republic, which provides at annex III, article VII, that:

*[n]o Party shall impose any performance requirements which are contrary to the World Trade Organisation Agreement on Trade Related Investment Measures as a condition for establishing, expanding or maintaining investments.*

A similar approach was followed in the United States-Viet Nam agreement (article 11(1)). This article is unusual because it establishes special time limits for its application. In article 11(2) the parties agree:

*To eliminate all TRIMs (including those contained in laws, regulations, contracts or licenses) which fall under sub-paragraphs 2(A) (trade balancing requirements) and 2 (B) (foreign exchange controls on imports) of the List by the time this Agreement enters into force. Viet Nam shall eliminate all other TRIMs no later than five years after the date of entry into force of the Agreement, or the date required under the terms and conditions of Viet Nam's accession to the WTO, whichever occurs first.*

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 EIIA and thus make those same obligations enforceable through any dispute resolution mechanism contained in the EIIA, and not only the WTO dispute resolution procedures.

Unlike the case of the TRIMs Agreement, some EIAs, following the United States BIT model in this regard, allow performance requirements which are otherwise prohibited, provided that they meet certain conditions. One is that they are granted as conditions for the receipt of an advantage. For instance, NAFTA article 1106(4) explicitly allows the parties to condition the receipt of an advantage to:

*Locate production, provide a service, train or employ workers construct or expand particular facilities, or carry out research and development.*

Moreover, article 1106(3), referring to the list of performance requirements covered under article 1106(1), singles out a number of them that cannot be linked to incentives, implying that the remaining measures on the list may be allowed when linked to advantages.

Another approach to the issue of performance requirements associated with incentives is exemplified in earlier EIAs that established industrial regional industrialization programmes, often creating a "regional enterprise" to carry out these programmes. Thus, under the Charter on a Regime of Multinational Industrial Enterprises in the Preferential Trade Area for Southern African States, the benefits accorded to an enterprise established according to the rules of the Charter were balanced by a number of obligations, including performance requirements, such as the increase in local value-added of products, export support, training, minimum volume or supply for the national market and supply of information.<sup>79</sup>

Some EIAs do not go as far as prohibiting performance requirements but discourage their imposition through a "best effort" clause. Thus, article 3 of the Framework Agreement on the ASEAN Investment Area calls for the progressive reduction or abolition of:

*investment regulations or conditions which may impede investment flows or the operation of investment projects in ASEAN.*

Finally, some EIAs make explicit reference to measures that could be considered performance requirements but that are excluded from the prohibition. An example is article 1006(2) of NAFTA, which explicitly excludes the mandating of the use of certain technologies as being considered a performance requirement under the Agreement. Another example is article

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<sup>79</sup> Similar examples can be found in the Protocol on Cooperation in the Field of Industrial Development of COMESA, Decision 292 of the Andean Pact creating the "Andean Multinational Enterprise", the Revised Treaty of ECOWAS and the Revised Basic Agreement on ASEAN Industrial Joint Ventures.

17-04 (2) and (3) of the Free Trade Agreement between Colombia, Mexico and Venezuela mentioned above. In particular, article 17-04 (3) specifies that:

*Nothing in the provisions of this article shall be construed as preventing a Party from imposing, with regard to any investment in its territory, requirements to locate production, generate jobs, train workers, or carry out research and development.*

Under other EIAs, the freedom to impose performance requirements linked to incentives has been encouraged. For example, the CARICOM members have issued guidelines encouraging the imposition of performance requirements linked to incentives in the negotiation of BITs.

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Prohibitions on performance requirements have begun to appear in EIAs in recent years, notably since the adoption of the WTO TRIMs Agreement prohibited the imposition of certain trade-related investment measures. In some cases, these commitments are coextensive with those already made in the TRIMs Agreement. In other cases, however, these prohibitions go beyond the TRIMs Agreement and specifically prohibit certain enumerated measures that a State may consider part of its development policy. A country that wishes to balance its desire to attract foreign investors, by making commitments to limit performance requirements, with its desire to retain the right to impose them in some cases, could do so through the inclusion of a provision for exceptions to the performance requirements commitment. Alternatively, that country may wish to exclude certain specific performance requirements from the enumeration in the agreement.<sup>80</sup>

#### **g. Employment of key personnel**

Recent EIAs that deal with investment and services liberalization often include provisions intended to ensure that investments will be able to employ the key managerial or professional personnel of their choice. These provisions are an important complement to investment liberalization and over the years have become increasingly elaborate, appearing some times in a separate chapter of the EIA. Several approaches can be identified in this respect.

For example, article 13-07 of the Costa Rica-Mexico free trade agreement provides that “[n]o Party may require that an enterprise of that Party that is an investment of an investor of another Party appoint to senior management positions individuals of any particular nationality”. Significantly, however, the provision does not require that the host country allow unlimited immigration of nationals of the home country and thus the investment’s choice of senior management personnel necessarily is limited to those persons who can lawfully gain entry into the home country. This provision includes an exception that allows the host country to require that a majority of the board of directors have a particular nationality, provided that the requirement “does not materially impair the ability of the investor to exercise control over its investment”. The article is also subject to any exceptions listed in an annex. Similar approaches can be found in other EIAs following the NAFTA model.

Some EIAs do make reference to the parties' immigration laws and directly establish eligibility under these laws. An example is the Free Trade Agreement between Jordan and the United States, which addresses the issue of entry of nationals of the other party in relation both to

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<sup>80</sup> For an in-depth discussion of performance requirements in IAs, see UNCTAD (2001a).



trade in services and to investment under the heading of "visa commitments" (article 8), as follows:

1. *Subject to its laws relating to the entry, sojourn and employment of aliens, each Party shall permit to enter and to remain in its territory national of the other Party solely to carry on substantial trade, including trade in services or trade in technology, principally between the Parties.*
2. *Subject to its laws relating to the entry, sojourn and employment of aliens, each Party shall permit to enter and to remain in its territory nationals of the other Party for the purpose of establishing, developing, administering or advising on the operation of an investment to which they, or a company of the other Party that employs them, have committed or are in the process of committing a substantial amount of capital and other resources.*

Then paragraph 12 of the explanatory notes to the agreement states that:

*Paragraphs 1 and 2 of this Article render nationals of Jordan eligible for treaty-trader (E-1) and treaty-investor (E-2) visas subject to the applicable provisions of the United States laws and corresponding regulations governing entry, sojourn and employment of aliens. They also guarantee similar treatment for United States nationals seeking to enter Jordan's territory.*

The Australia-Thailand free trade agreement includes a separate chapter on the movement of natural persons (chapter 10) applying to both the trade in services and investment chapters (chapters 8 and 9 respectively) of the agreement. Chapter 10 includes detailed definitions describing various types of functions the persons in question might perform in the host country. It also differentiates between short-term and long-term temporary entry. The granting of temporary entry is made subject to immigration measures (article 1007), provided that:

*...such measures are not applied in such manner as to nullify or impair the benefits accruing to the other Party under the terms of this Chapter.*

In some cases, the subordination of the right to employ key personnel to the immigration laws is made explicit. For example, article 45(2) of the EFTA-Singapore free trade agreement provides that:

*[t]he Parties shall, subject to their laws and regulations, permit investors of another Party which have investments in their territories, and investments of such investors, to employ any key personnel of the investor's or the investment's choice regardless of nationality and citizenship provided that such key personnel has been permitted to enter, stay and work in the territory of the other Party and that the employment concerned conforms to the terms, conditions and time limits of the permission granted to such key personnel.*

The Agreement between Japan and Mexico for Strengthening Economic Partnership goes even further and provides, under the general scope and coverage article (article 57), that:

4. *Nothing in this Chapter shall impose any obligation on either party regarding measures pursuant to immigration laws and regulations.*
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Under EIAs that provide for the free movement of persons, an investor's right to employ key personnel of its choice is guaranteed in principle for individuals having the nationality of one of the member countries. This is the case, for example, in the European Community. However, other EIAs that grant a right of establishment specifically withhold any obligation on member States to grant freedom of movement of persons from other member States. An example is the CARICOM agreement (article 38).

Other EIAs do not totally deny investors a right to employ foreign personnel but give preference for employment to experts having the nationality of the host country, followed by employees from within the EIA area. Article 13 of the Unified Agreement for the Investment of Arab Capital in the Arab States provides that:

*[t]he State shall assist the Arab investor to secure such Arab labour and Arab or foreign experts as he needs. Where the requisite professional skills are available, priority in filling the relevant vacancies shall go to nationals of the State in which the investment is made, followed by Arab employees and, finally, experts of other nationalities.*

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Host countries sometimes require foreign investments to employ their own nationals, both to increase employment and to raise the skill level of the workforce. They may also require that a number of the managers or directors of companies operating in strategic economic sectors be reserved to nationals of the host country, or even be appointed by the host Government itself. This requirement responds to the perception that keeping the management of certain strategic companies under national control facilitates the implementation of their economic policies. However, part of the competitive advantage that allows a foreign investment to succeed in the host country is the managerial expertise or technical knowledge of its employees, which may not be as readily available in the host country. Moreover, restrictions regarding whom the investment employs may undermine the investor's ability to control its investment. Policymakers need to balance these concerns when considering a provision related to the entry and employment of foreign personnel.

### **3. Investment Protection**

A preliminary question facing policymakers is whether an EIA should address investment protection issues, or whether these issues should be dealt with in separate agreements (e.g. BITs) or should be left for the national laws of the host country. The introduction of protection standards in an EIA is likely to further the agreement's goal of establishing a favourable investment climate, but restricts the parties' future discretion in regulating foreign investment or promoting local investment. As noted before, certain types of EIAs that contain investment liberalization commitments also include provisions granting legal protection to investments. These include, notably, NAFTA and EIAs following the NAFTA model. Under other EIAs, for example the agreements concluded by the European Community with third countries, the question of investment protection remains largely a matter of national policy.<sup>81</sup>

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<sup>81</sup> As noted, one possible reason for not including investment protection in EIAs signed by the EC may be that while the European Commission has authority to negotiate EIAs, it does not have competence over investment protection issues.

Provisions that protect investment may use either relative or absolute standards. The relative standards generally require non-discrimination as between covered investment and certain other investments.

The absolute standards may be intended to protect investment generally or they may be intended to protect investment against only certain specified actions, such as expropriation or restrictions on intellectual property rights. Typically, these latter standards are intended to protect the ownership or beneficial use of the investment against political risk. Each investment protection provision raises its own policy implications.

### **a. Non-discrimination**

Non-discrimination provisions guarantee investments either treatment no less favourable than that granted to nationals of the host country (national treatment) or treatment no less favourable than that granted to nationals of any third country (most-favoured-nation or MFN treatment). Very often the two non-discrimination standards appear together in an EIIA. However, each of these standards raises complex issues of interpretation and application, some of which are only briefly alluded to here.<sup>82</sup>

Both the national treatment and MFN standards have been widely applied in trade law. In trade matters, national treatment of imported products with respect to internal measures is one of the basic principles of agreements that seek to liberalize international trade. It serves the purpose of ensuring that internal measures are not used to nullify or impair the effect of tariff concessions and other international rules applicable to border measures. In relation to investment, national treatment involves a similar economic aim: foreign and domestic investors should be subject to the same competitive conditions in the host country market, and therefore no government measure should unduly favour domestic investors (UNCTAD, 1999c, p. 8). Similar considerations apply *mutatis mutandis* to the MFN standard with respect to investments from other countries (UNCTAD, 1999d).

At the same time, the relative importance of these two standards is not the same in the case of trade and investment. In the context of multilateral trade, the MFN principle is of fundamental significance. The standard is also particularly relevant to relations arising out of EIIA members with third countries. On the other hand, national treatment has acquired increasing importance with respect to trade in the context of deeper trade integration, and, of course, is of major importance in matters of investment.

Thus, unlike in the case of trade, one of the key questions that arise with regard to the scope of application of the national treatment standard in the investment field is whether the principle shall apply to the entry of foreign investment or only to the treatment of the investment after entry. A number of EIAs provide both national treatment and MFN, but only after entry. These are agreements that do not pursue the liberalization of investment flows but deal nevertheless with investment protection, guaranteeing after-entry non-discrimination. An

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<sup>82</sup> A comprehensive and in-depth discussion of the complex issues raised by the national and MFN treatment standards exceeds the limits of this study. For further details about the national and MFN treatment standards in relation to investment, see UNCTAD (1999c, 1999d and 2005a).

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example is the Free Trade Agreement between Colombia, Mexico and Venezuela.<sup>83</sup> Article 17-03 (12) and (2) provides that:

1. *Each Party shall accord to investors of another Party, and to their investments, treatment not less favorable than that it accords, in like circumstances, to its own investors and investments.*
2. *Each Party shall grant investors from another Party, and to their investments, treatment no less favorable to that it accords, in like circumstances, to investors, and their investments of another or of a non-Party.*

In contrast, agreements that pursue both liberalization and protection of investments tend to extend the scope of national and MFN treatment to the pre-entry and post-entry phases of the investment. This is the case with NAFTA and many EIAs that follow the NAFTA model. It is also the case with other types of agreements, such as the MERCOSUR Colonia Protocol for the treatment of investments from other MERCOSUR countries, the Framework Agreement on the ASEAN Investment Area and the Free Trade Agreement between CARICOM and the Dominican Republic. For example, annex III, article III(1), of the Free Trade Agreement between CARICOM and the Dominican Republic provides that:

*[e]ach Party shall admit and treat investments in a manner not less favourable than the treatment granted in similar situations to investments of its investors except for investments in areas identified in the Appendix to this Annex.*

MFN treatment is guaranteed by Annex III, article III(2), which provides that:

*[e]ach Party shall admit and treat investments in a manner not less favourable than the treatment granted in similar situations to areas related to Most-Favoured-Nation treatment except for investments in the areas identified in the Appendix to this Annex.*

As noted earlier (section IV.B.1), EIAs that provide for pre-establishment and post-establishment national and MFN treatment typically provide for country-specific exceptions to these standards to be set forth in an annex.

The approach followed by the European Community Treaty (as amended) to national treatment goes beyond a general national treatment clause. Other than a general prohibition against discrimination on the grounds of nationality (article 12) national treatment is present in the content of substantive rules rather than in any single statement of the standard. It is indeed a fundamental part of the Community legal order, particularly as regards entry and establishment (articles 43-48). In addition, European Community law applies a wider concept of non-discrimination between nationals of member States to specific policy areas, such as State monopolies (article 31), free movement of workers (article 39(2)), freedom to provide services (articles 49-55), free movement of capital (articles 56-60), competition (article 81(1) (d) and 82 c), State aid (articles 87-88) and discriminatory taxation (articles 90-91), thereby helping to

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<sup>83</sup>. Other examples include the Agreement on Promotion, Protection and Guarantee of Investments among Member States of the Organization of the Islamic Conference, the Agreement between the States Members of ASEAN for the Protection and Promotion of Investments (which only provide for MFN treatment), the FTAs between Mexico and Costa Rica, between Mexico and Nicaragua, and between Central America and the Dominican Republic.

harmonize national standards and to develop an integrated single market for trade and investment (UNCTAD, 1999c, p. 17).

At the other end of the spectrum stands Decision 292 of the Commission of the Cartagena Agreement: Uniform Code on Andean Multinational Enterprises. Article 14 of Decision 292, for example, provides that Andean multinational companies may participate in economic sectors reserved for national companies in accordance with the respective legislation of the member countries. Thus, Decision 292 prescribes the national treatment for Andean companies but leaves discretion to its member countries to establish their own rules in this respect. To qualify for Andean multinational company status, a company must meet a number of requirements, including the requirement that at least 60 per cent of the capital of the company be owned by investors from two or more Andean countries.

The application of the national treatment standard raises two main questions. First, what are the factual situations in which national treatment apply? Second, in what manner and to what extent is the treatment of foreign investors assimilated to that of nationals? The first issue defines the scope of factual comparison, while the second deals with the criteria for determining discrimination, the application of which is limited to the factual situations identified in the first question. A related question that arises is whether national treatment covers not only *de jure* treatment (i.e. treatment provided for in national laws and regulations), but also *de facto* treatment, as where the measure in fact works against national treatment. One example may be licensing requirements, which depend on the possession of professional qualifications that can be obtained only in the host country, therefore *de facto* discriminating against foreigners (UNCTAD, 1999c, pp. 11-12).

Similarly, the MFN treatment standard does not mean that foreign investors have to be treated equally irrespective of their characteristics or activity in the host country. Different treatment is justified *vis-à-vis* investors from different foreign countries if they are in different objective situations.

To address some of these difficulties in the application of the national and MFN standards, EIAs often contain an explicit provision according to which the treatment applies only to investments that are in "similar" or "like" situations. Nonetheless, the general terms used in the formulation of these standards leave a substantial degree of discretion for their application and interpretation by tribunals, as a number of arbitration cases under NAFTA have shown.<sup>84</sup>

It is also common — even among groups that have achieved deep levels of economic integration — to include a number of exceptions to the application of the general standards of pre-national and MFN treatment. These exceptions tend to be particularly significant when national and MFN treatment is granted pre- and post-establishment. The use of exceptions enables host countries to exclude certain types of enterprises, activities or industries from the operation of national and MFN treatment. In the example of the Free Trade Agreement between CARICOM and the Dominican Republic, the provisions allow the parties to specify in an annex sectors of the economy to which the non-discrimination provisions do not apply. This modality of exception is quite usual in a non-discrimination provision that applies to the right of establishment. It offers a way by which host countries can provide a generally favourable investment climate while excluding foreign investment from certain sectors of the economy.

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<sup>84</sup> For a detailed analysis of arbitration cases dealing with the application of the national treatment and MFN standards in relation to NAFTA, see UNCTAD (2005b, forthcoming).

With regard to MFN treatment, two different versions of this modality may be noted. First, under the GATS type of approach a member may maintain a measure inconsistent with the unconditional MFN clause provided that such measure is listed in, and meets the conditions of, the annex to that clause. The annex typically specifies that the MFN exception should not apply for more than ten years, and is subject to revision in subsequent negotiations. This approach is often followed in the trade in services chapters of EIAs. (The GATS type approach to national treatment (both pre- and post-establishment) is for it to be granted only when a party makes commitments on liberalization of specific industries and measures (see section IV.B.1.) Another modality, exemplified by NAFTA, article 1108 (1), allows for an exception similar to that found in the GATS (MFN does not apply to non-conforming measures maintained at federal, state or local levels). However, NAFTA permits member countries to adopt new non-conforming measures with both national and MFN treatment in the future, with regard to sectors or activities which a country has set out in a specific schedule (article 1108 (3)). This approach is characteristic of the NAFTA-type investment provisions of EIAs. These two approaches are often found together in the respective chapters of an EIA dealing with trade in services and investment.

Other exceptions are also specific to MFN treatment regardless of whether the standard is granted at pre- or post-establishment phases. Thus, it is common in agreements guaranteeing MFN treatment to include, in addition to any sectoral exceptions, a general exception for advantages provided to a third party under a customs union or free trade agreement, or treatment afforded under a treaty on taxation. For example, annex III, article III(3), of the Free Trade Agreement between CARICOM and the Dominican Republic provides that:

*[t]he obligation to grant treatment no less favourable than is granted to third States does not apply to:*

- (i) any treatment or advantage resulting from any existing or future customs union or free trade area or common market or monetary union or similar agreement to which a Party is a party; or*
- (ii) any international agreement or arrangement relating wholly or mainly to taxation.*

The first exception, also known as the REIO clause, is needed because it is in the nature of an EIA to grant special privileges to the other parties in exchange for reciprocal treatment. The first exception ensures that these special privileges are not generalized to other States with which the first State has extended the MFN guarantee but which, unlike the EIA members, have not promised reciprocal treatment.<sup>85</sup>

This exception is especially important to a developing country that has entered into an EIA with other developing countries and has granted concessions to those countries that it does not wish to extend to third States. To avoid that result, it should include this exception in any other agreement that it concludes and that contains an MFN commitment. Indeed, it may be useful to include this exception in all of its MFN commitments in order to preserve the ability to enter into future EIAs with other developing States and to grant other developing States special concessions not granted to third States with which it has an MFN commitment.

Of course, including such an exception opens a developing country to the possibility that its treaty partners will themselves extend more favourable treatment to some third country and invoke the exception to justify not extending it to the developing country. This problem has

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<sup>85</sup> For a detailed analysis of the implications of the REIO clause, see UNCTAD (2005a).



been addressed in a few recent EIAs. For example, article 40(2) of the Free Trade Agreement between the EFTA States and Singapore contains an exception to the MFN obligation for treatment extended under a customs union or a free trade agreement, but allows the parties to this agreement to negotiate to obtain the more favourable treatment under the customs union or other free trade agreement. Specifically, the article provides that:

*[i]f a Party accords more favourable treatment to investors of any other State or their investments by virtue of a free trade agreement, customs union or similar agreement that also provides for substantial liberalisation of investments, it shall not be obliged to accord such treatment to investors of another Party or their investments. However, upon request from another Party, it shall afford adequate opportunity to negotiate the benefits granted therein.*

The second exception is often included because the complexity of tax treaties requires that tax matters be addressed individually with other States through bilateral agreements and that provisions on tax matters not be extended automatically to every other State with which a State has concluded an MFN provision. This exception is not intended to have any special consequences for development. It merely reflects the complexity of tax laws and the need, in many cases, to address tax issues in a specialized agreement.

Some EIAs include additional exceptions in relation to national and MFN treatment. For example, NAFTA includes national and MFN treatment exceptions with regard to public procurement and subsidies provided by a contracting party or a State enterprise, including government-supported loans, guarantees and insurance (article 1108(7)). In addition, there are national and MFN treatment exceptions in connection with intellectual property rights (article 1108(5)) and MFN exceptions with regard to other international agreements that the parties have set out in their schedule (article 1108 and (6)).

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A common standard granted by EIAs that address investment protection issues is non-discrimination for reason of nationality, meaning MFN treatment, national treatment, or both. MFN treatment raises fewer objections in principle because a country usually has little reason to prefer foreign investors of one nationality to foreign investors of another. Nevertheless, MFN treatment does have a generalizing effect, which means that it offers to all treaty partners the highest level of treatment afforded to any other treaty partner in any other agreement, whether in the past or future. If the host party is not prepared to offer to its EIIA partners the highest form of treatment, provision for exceptions to MFN treatment must be made. Allowing exceptions, of course, will enable the other parties to the EIIA also to withhold their highest level of treatment, although this may be of less concern if investment flows are expected to move in only one direction. Furthermore, potential investors may be discouraged by the possibility that they will be placed at a competitive disadvantage relative to competitors from other countries. This problem can be addressed by a provision for listing exceptions in an annex or by limiting the exceptions to those already in existence, either of which can provide some level of certainty for potential investors.

National treatment, by contrast, raises greater policy concerns because it eliminates the host country's ability to favour local investors over investors from other EIIA countries. Again, these concerns can be addressed through provisions for exceptions. If exceptions can be added

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at any time in the future, the national treatment commitment as a practical matter may be of very limited value. If exceptions are limited to those that can be identified at the time the treaty is concluded, the commitment retains greater force, but the host country's future discretion is correspondingly diminished.

### **b. General protection provisions**

General protection provisions typically appear in EIAs that address investment protection issues, such as those following the NAFTA model. They are not included in liberalization agreements such as the European Community or the EIAs signed by the EC. When EIAs include general protection provisions, the most common ones are guarantees of “*fair and equitable treatment*” or “*full protection and security*.” These provisions often appear together. For example, article 909 of the FTA between Australia and Thailand provides that:

2. *Each Party shall ensure fair and equitable treatment in its own territory of investments.*
3. *Each party shall accord within its territory protection and security to investments.*

Other agreements guarantee only fair and equitable treatment. Article 159 of the Treaty Establishing the Common Market for Eastern and Southern Africa, for example, provides that

*[i]n order to encourage and facilitate private investment flows into the Common market, Member States shall . . . accord fair and equitable treatment to private investors .*

These provisions are common to many investment agreements and raise few issues in negotiations. They are intended to signal a favourable investment climate by offering a specific commitment. A country is either willing to make that commitment or not, but there are few variations in the commitment to be found in the agreements.

An issue that does arise is determining precisely what the nature of the commitment is.

Two different views of the “fair and equitable treatment” commitment have emerged. One is that it is synonymous with the treatment of foreign investment required by customary international law — what has become known as the international minimum standard. The other is that “fair and equitable treatment” means something different from the international minimum standard, although there may well be areas of overlap. In this latter view, the fair and equitable treatment commitment probably sets a higher standard than customary international law requires.

Some recent EIAs have sought to define the commitment as limited to the protection provided by customary international law and to specify at some level what that protection is. For example, article 15.5.1 of the Singapore-United States FTA initially provides that:

*[e]ach Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.*

Article 15.5.2 goes on to clarify the meaning:

*For greater certainty, paragraph 1 prescribes the customary international law minimum standards 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.*

- (a) The obligation in paragraph 1 to provide “fair and equitable treatment” includes the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world; and*
- (b) The obligation in paragraph 1 to provide “full protection and security” requires each Party to provide the level of police protection required under customary international law.*

Thus, the text of the agreement explicitly treats fair and equitable treatment as an element of customary international law. Other agreements, however, do not couple the reference to fair and equitable treatment with a reference to international law and thus do not take a position on the relationship between the two. One such agreement is the Australia-Thailand FTA cited above.

The requirement for “full protection and security” is somewhat better defined. It has been understood to mean an obligation on the part of the host State to exercise due diligence or reasonable care to protect foreign investment against injury, including injury by private citizens.

The fair and equitable treatment provision in particular is among those most likely to be relied upon in an investment dispute with an investor. The language is broad enough to apply to virtually any adverse circumstance involving an investment. Thus, developing countries need to weigh the beneficial impact that this assurance can have on the investment climate against the potential for disputes involving its meaning.<sup>86</sup>

At the same time, it should be noted that if a country already has provided this guarantee in at least one BIT, that level of protection must be provided to investors or investments of all other States with which the State has concluded an EIIA with an MFN clause, unless the MFN clause is drafted so as to exclude that provision. Thus, in many cases, it may make no practical difference whether this provision explicitly appears in an EIIA.

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General protection provisions of EIAs, such as a guarantee of fair and equitable treatment, are significant because they are potentially applicable to virtually all host country conduct with respect to covered investments. Such provisions, together with the non-discrimination provisions, are among those that do the most to shape the overall investment climate in the host country, although, because of their breadth of application and vagueness of meaning, they are also among those most likely to trigger disputes.

### **c. Expropriation**

The issue of expropriation was the first and the most important single protection issue addressed in investment agreements. EIAs that deal with protection issues almost invariably include provisions on expropriation. These provisions recognize the right of the host State to

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<sup>86</sup> For analyses of arbitral decisions on investor-State disputes involving the meaning of “fair and equitable treatment”, see UNCTAD (2005b).

expropriate investment, but impose conditions that must be satisfied when an expropriation occurs. These provisions raise two principal issues. These issues are not specific to EIAs but their significance may increase in the context of EIAs, as these agreements address a wider range of investment-related issues.

*(i) Scope of the expropriation provision*

The first issue is to define the sorts of host country actions to which the provision applies. In other words, what is meant by an expropriation? EIAs rarely define the term. Some EIAs are explicit in stating that an expropriation includes measures “equivalent” or “tantamount” to an expropriation. They may also state that expropriation includes “creeping expropriation”. Such language is intended to ensure that the term refers to expropriations that occur through a series of actions rather than by a single act. For example, the Free Trade Agreement between El Salvador, Guatemala, Honduras and Mexico provides in article 14-11 that:

*No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such investment ...*

This provision is typical of EIAs that follow the NAFTA model. Its 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. 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. Acts that only partially devalue an investment, however, may be viewed by the host State as merely routine regulatory acts that are not the equivalent of an expropriation. The issue of what constitutes an expropriation is thus important to host countries because a definition that is too broad could be interpreted to the effect that routine regulatory acts constitute an expropriation, requiring that all investments affected by the regulations be compensated. Until recently, most EIAs typically did not include language that defined clearly the scope of the expropriation provision. This situation led to investment disputes, mainly in the context of NAFTA, regarding the type of government measures to which the expropriation provision applies (UNCTAD, 2005b).

A few recent FTAs are beginning, however, to address the issue. For example, annex 10-D of the Free Trade Agreement between Chile and the United States states initially that:

*[a]n action or series of actions by a Party cannot constitute an expropriation unless it interferes with a tangible or intangible 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:

*The second situation addressed by [the expropriation article] is indirect expropriation, where an action or series of actions by a Party has an effect equivalent to direct expropriation without formal transfer of title or outright seizure.*

- (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, nondiscriminatory 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) seems to create a presumption that regulatory actions do not constitute an expropriation, but it does not exclude that possibility entirely since:

- The paragraph applies only to regulatory actions that are designed and applied to protect legitimate public welfare objectives.
- The paragraph applies only to non-discriminatory regulations. This presumably reflects the fact that legitimate public welfare regulations would rarely be discriminatory and thus their application only to selected investments would call into question whether they were truly motivated by legitimate public welfare objectives.
- Even a regulation designed and applied to protect legitimate public welfare objectives may still be considered in rare circumstances to be an expropriation, taking into account the character of the government acts, their economic impact and the extent of interference with reasonable, investment-backed expectations.

The factors listed in the annex of the Chile-United States FTA echo some of the considerations that have been utilized in United States constitutional law to determine whether government conduct constitutes a “taking” of property for which the Government must pay “just compensation”. The inquiry seems to focus on the extent of the interference with the property and on whether the investor’s reasonable expectations have been defeated. Recall that the Chile-United States FTA is among those that define investment in economic terms, as involving the commitment of capital and the assumption of risk in the expectation of gain. The core concept behind this definition seems to be that government action that undermines the asset’s character as investment that extensively interferes with the gain that an investor reasonably expected when it put capital at risk is more likely to be considered an expropriation. Other constitutional systems have also influenced the approach of EIAs to regulatory takings (box IV.1).

**Box IV.1. The European Community's approach to regulatory takings**

The need to determine the scope of expropriation in relation to regulatory measures arises very often in a purely national context. Governments need to adopt regulations to pursue social, environmental and other goals in the interest of their communities and these can affect, to a greater or lesser degree, the rights of individuals and corporations, including their property rights. The right of individuals to hold, possess and enjoy property is, nevertheless, one of the values most deeply felt in most societies. This is particularly true in market-oriented democratic societies. Thereby, a tension is often created between the duty of the State to protect the private rights of individuals and its obligation to regulate in the public interest. The manner in which these competing rights are balanced depends very much on the mix of cultural and social values upheld by a particular society.

Most European countries uphold the notion that property must serve a social function and that individual rights are subject to the prior right of society to secure the public good. These countries therefore tend to allow wide scope for the exercise of regulatory powers before recognizing these as regulatory takings. Thus, while the right to private property is understood to be a part of the general human rights regime of the Council of Europe, a/ the European Court of Human Rights has addressed the issue of expropriation, and generally has regarded regulatory action without compensation not to be in violation of expropriation rights. b/ Member States of the Council of Europe are seen as having a wide margin of appreciation in these matters, at least so far as such regulatory action affects their own nationals, as opposed to foreign nationals. Crucial here is the need to strike a balance between the right to peaceful enjoyment of possessions guaranteed by article 1 of the First Protocol to the European Convention on Human Rights and the legitimate regulatory aims of the member State concerned. Any interference with these rights must be for a legitimate regulatory aim and be *proportionate* to that aim.

The European Community has approached the question of the right to regulate along similar lines. Although there is no provision in the European Community treaties recognizing the right to property, such right has been recognized as part of the fundamental rights protected by Community law. The European Court of Justice laid down its doctrine on the issue of regulatory takings in its decision of 14 May 1974 in the case of *Nold v. Commission* (C-4/73). The Court first held that the rights guaranteed by Community law "must be inspired in the common constitutional traditions of the member states, and should not therefore admit measures incompatible with the fundamental rights recognized and guaranteed by the constitutions of these states". The ECJ interpretation of the approach of the constitutions of member States to this matter may be summarized as follows:

- Whereas the constitutional regimes of all member States guarantee the protection of the right to private property, and similar guarantees protect the free exercise of business, work and other professional activities, the protection of such rights, far from constituting an absolute prerogative, must be seen in the light of the social function of the protected assets and activities.
- Consequently, this category of rights is generally guaranteed with the reservation of the limitations established in the public interest.
- It seems also legitimate to maintain certain limitations in the Community regime with respect to these rights as this may be justified by the public interest objectives pursued by the Community, so long as they do not contradict the essence of such rights by reason of being proportionate responses to the objectives being pursued.

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### Box IV.1. The European Community's approach to regulatory takings (concluded)

It can be deduced from this doctrine that Community regulation altering private property rights is not considered to be subject to a duty to pay compensation in every case. Community law, especially in the field of the Common Agricultural Policy, is constantly altering the property regime of agricultural owners, without its giving rise to compensation, except in cases in which the Commission has created in relation to concrete agricultural owners a legitimate expectation which has been later frustrated. Indeed, Community regulation offers persuasive examples with respect to the *use of property*, especially in the field of environmental and consumer protection, in which it has ordered the destruction of assets or products for ecological or sanitary reasons, without compensation. The ECJ in its Decision of 6 April 1995 in the case of *Flip v. Verdegem* (C-315/93) established that the Community regulation applicable in the fight against swine fever was to be interpreted in the sense that it did not require the member States to establish a compensation regime for the owners of the pigs slaughtered by order of the authorities.

It follows from the foregoing that under the ECJ jurisprudence the distinction between *deprivation of property* and the *regulation of the use of property* is fundamental for determining whether compensation is required. The former refers to concrete situations in which, as a result of a decision by a public authority taken in the framework of a legal mandate, the property rights are transferred to another subject, whether a public authority or a private beneficiary. In these cases, compensation is a guarantee of the property right. However, in the case of the latter, the limitations on the use of an asset apply generally to all owners and there is no transfer of property. Therefore, there is no requirement to compensate. In this respect, it needs to be taken into account that while the introduction of security measures for the use of certain products or assets involves a public cost, not only does the property in such cases remain in the hands of the private owner, but also the owner directly benefits from a higher level of security or from the increased security in the use that others made of its property.

This doctrine was reflected in the Charter of Fundamental Rights of the European Union, which is included in the Draft Treaty of the European Constitution. The Charter establishes a distinction between measures of individual deprivation of property and general regulation of the use of private goods. It affirms that:

1. *Every person has the right to enjoy the property of the assets acquired legally, to use them, to dispose of them and to bestow them. No person can be deprived of its property except for a public purpose, in the cases and under the conditions prescribed by the law, and in exchange, within a reasonable time, of a just compensation for its loss. The use of property may be regulated by law to the extent that it is necessary in the public interest.*
2. *Intellectual property is protected.*

In conclusion, European Community law, as a result of its interpretation of the constitutional rights of its member states, has established that there is compatibility between, on the one hand, guaranteeing the right to hold private property which, if interfered with will attract compensation, and, on the other hand, imposing on such property obligations of use that are not subject to compensation.

Source: Ortega (2003).

<sup>a</sup> Protocol to the European Convention for the Protection of Human Rights and Fundamental Freedoms, as amended by Protocol No. 11, article 1.

<sup>b</sup> See, for example, the case of *Pine Valley Development LTD & Others v. Ireland*, 14 Eur. Ct. H.R. (ser. A) 319, 356 (1991); see also *Orelemans v. The Netherlands*, 15 Eur. H.R. Rep. 561 (1992).

A few recent EIAs have also sought to exclude explicitly certain interferences with intellectual property rights from the definition of expropriation. For example, article 10.13 of the Free Trade Agreement between Chile and the Republic of Korea 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, a party may modify intellectual property rights without being required to pay compensation under the expropriation article, but only if the modification is consistent with the TRIPS Agreement. The granting of a compulsory licence for intellectual property rights is also not to be considered an expropriation.

### ***(ii) Conditions for lawful expropriation***

The second issue is to define the requisites imposed on a host country for the expropriation to be considered legal. Among those conditions imposed are that the expropriation be for a public purpose, non-discriminatory, in accordance with due process of law, and accompanied by the payment of compensation. These are the conditions recognized by customary international law. The most debated of these conditions is the requirement of compensation. The compensation clause may specify the amount of compensation, the currency in which it is to be paid, and the time period within which it is to be paid. The most common standards for determining the amount of compensation required are “fair market value”, or simply “fair” or “just” compensation, but in some cases the more specific meaning of these terms is not specified.

As this suggests, the provisions vary in the level of detail with which they prescribe the conditions. Among the most detailed of such provisions is article 1110 of NAFTA, which provides as follows:

1. *No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment (“expropriation”), except:*
  - (a) for a public purpose;*
  - (b) on a non-discriminatory basis;*
  - (c) in accordance with due process of law and Article 1105(1)[requiring treatment in accordance with international law, including fair and equitable treatment and full protection and security];*
  - (d) on payment of compensation in accordance with paragraphs 2 through 6.*
2. *Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place (“date of expropriation”), and shall not reflect any change in value occurring because the intended expropriation had become known earlier. Valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.*
3. *Compensation shall be paid without delay and be fully realizable.*

4. *If payment is made in a G7 currency, compensation shall include interest at a commercially reasonable rate for that currency from the date of expropriation until the date of actual payment.*
5. *If a Party elects to pay in a currency other than a G7 currency, the amount paid on the date of payment, if converted into a G7 currency at the market rate of exchange prevailing on that date, shall be no less than if the amount of compensation owed on the date of expropriation had been converted into that G7 currency at the market rate of exchange prevailing on that date and interest had accrued at a commercially reasonable rate for that G7 currency from the date of expropriation until the date of payment.*
6. *On payment, compensation shall be freely transferable as provided in Article 1109 [the general transfers provision].*

The NAFTA provision requires payment in accordance with the traditional Hull formula of “prompt, adequate and effective” compensation. The Hull formula, named for the former Secretary of State of the United States Cordell Hull, reflects the position of the developed countries concerning what level of compensation should be paid for expropriated foreign investment. Upon further elaboration, these standards have been interpreted to mean that the compensation requires payment of fair market value without delay in a freely convertible currency. The trend among more recent EIAs has been to incorporate language consistent with the Hull formula.

Another example of a relatively detailed provision is article VI of the ASEAN Agreement for the Protection and Promotion of Investment, which provides that:

*[i]nvestments of nationals of companies of any Contracting Party shall not be subject to expropriation or nationalisation or any measure equivalent thereto (in this article referred to as “expropriation”), except for public use, or public purposes, or in the public interest, and under due process of law, on a non-discriminatory basis and upon payment of adequate compensation. Such compensation shall amount to the market value of the investments affected, immediately before the measure of dispossession became public knowledge and it shall be freely transferable in freely-usable currencies from the host country. The compensation shall be settled and paid without unreasonable delay. The national or company affected shall have the right, under the law of the Contracting Party making the expropriation, to prompt review by a judicial body or some other independent authority of that Contracting Party in accordance with principles set forth in this paragraph.*

Again, this provision adheres to the standards of prompt, adequate and effective compensation.

Other EIAs, particularly older ones, use terms such as “fair” or “reasonable”, but do not elaborate on the specific level of compensation. For example, article 9 of the Unified Agreement for the Investment of Arab Capital in the Arab States, states that:

*[i]t shall, however, be permissible to:*

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- (a) *Seize property for the public benefit in accordance with the authority vested in the State or its institutions to perform their functions in implementing public projects, provided that this is done on a non-discriminatory basis in return for fair compensation and according to general legal provisions regulating the seizure of property for the purposes of the public benefit. The Arab investor shall be given the opportunity to challenge the legitimacy of any dispossession and the amount of compensation before the domestic courts. Compensation shall be made with a period not exceeding one year from the date when the decision to dispossess became final.*

Similarly, article 5 of the Agreement on Investment and Free Movement of Capital Among Arab Countries provides that:

*[a]dmitting the inalienable right of the state recipient of the capital to nationalize, confiscate and expropriate within the framework of the public interest, the Arab investor shall be entitled in such cases to fair and effective compensation within a reasonable period of time.*

In some cases, the formula seems to reflect the Hull formula at least in part. For example, the Treaty Establishing the Common Market for Eastern and Southern Africa states that member States shall:

- (a) *subject to the accepted principle of public interest, refrain from nationalizing or expropriating private investment; and*  
(b) *in the event private investment is nationalized or expropriated, pay adequate compensation.*

The term “adequate” appears to be drawn from the Hull formula, but the elements of promptness and effectiveness are omitted. By contrast, article 42 of the Free Trade Agreement between the EFTA States and Singapore provides that:

*None of the Parties shall take, either de jure or de facto, measures of expropriation or nationalisation against investments of investors of another Party, unless such measures are in the public interest; non-discriminatory; carried out under due process of law; and accompanied by the payment of compensation. The amount of compensation shall be settled in a freely convertible currency and paid without delay to the person entitled thereto without regard to residence or domicile.*

Thus, this agreement does not address the amount of compensation, but does require that it be paid promptly and in a freely convertible currency.

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The standard of compensation to be paid upon expropriation has been, and remains, one of the most important issues of expropriation provisions. EIAs vary in the degree of specificity with which they describe the compensation that must be paid, but to the extent that any detail is provided the formula usually suggests fair market value. Recently, an issue that has raised greater concerns is the scope of the expropriation provision. Host countries may fear that a regulatory action, such as the enactment of environmental regulations, that impairs the value of an investment may be regarded as an expropriation requiring payment of compensation that a

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developing country in particular may not be able to afford. One potential solution is to craft the expropriation provision so as to clarify its scope, although no formula that is acceptable to all parties is likely to remove all doubt. A second potential solution is to narrow the definition of “investment” so as to limit the types of assets to which the provision might apply, although this has the effect of limiting the applicability of the entire agreement and thus potentially undermining its effectiveness. Another potential solution is to take certain regulatory actions, such as environmental measures, outside the scope of the agreement through the use of general exceptions. Here can be seen the important interaction between the provisions on the scope of the agreement and the substantive provisions. Alternatively, a narrower exception to the expropriation provision alone can be drafted. Whichever approach is adopted, the usual caveats about exceptions apply, although they can undermine the effectiveness of the treaty and create their own uncertainties.

#### d. Intellectual property

Provisions specifically addressing the protection of intellectual property rights traditionally were not part of the investment protection package granted by IIAs. However, they have become increasingly common in EIAs since the 1990s. They appear in most types of EIAs, including agreements that address investment liberalization as well as agreements that cover both liberalization and protection.<sup>87</sup> In some EIAs, the protection of intellectual property rights is dealt with in a separate chapter with detailed provisions. This is the case of recent NAFTA-type EIAs, such as the Australia-Thailand and Japan-Singapore agreements.

EIAs 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 intellectual property rights protection.

The first approach is to ensure that the protection of intellectual property rights meets existing international standards. For example, article 37 of the Euro-Mediterranean Agreement with Egypt provides that:

*Pursuant to the provisions of this Article and of Annex VI, the Parties shall grant and ensure adequate and effective protection of intellectual property rights in accordance with the prevailing international standards, including effective means of enforcing such rights.*

Annex VI then lists a number of multilateral agreements on the protection of intellectual property which Egypt commits itself to joining within four years, and confirms the importance of the obligations under several additional agreements.

A number of agreements, particularly those negotiated by the EFTA States with transitional economies and North African states, include a similar provision, but also provide for

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<sup>87</sup> For example, intellectual property protection provisions appear in most types of EIA signed by the European Community and EFTA, and they also appear in the NAFTA and NAFTA-type agreements, including recent FTAs signed by the United States, as well as recent bilateral EIAs signed between developing countries (e.g. CARICOM-Costa Rica, Mexico-Uruguay and Chile-Republic of Korea).

national and MFN treatment, subject to exemptions in accordance with the TRIPS Agreement. For example, article 17 of the agreement with the Slovak Republic provides:

2. *The States Parties to this Agreement shall accord to each other's nationals treatment no less favourable than that they accord to their own nationals. Exemptions from this obligation must be in accordance with the substantive provisions Article 3 of the TRIPS Agreement.*
3. *The States Parties to this Agreement shall accord to each other's nationals treatment no less favourable than that accorded to nationals of any other State. Exemptions from this obligation must be in accordance with the substantive provisions of the TRIPS Agreement, in particular Articles 4 and 5 thereof.*

EIIAs also may create their own substantive rules for the protection of intellectual property rights. For example, the Free Trade Agreement between Australia and the United States requires adherence to certain international conventions, but in a series of articles in chapter 15 sets forth detailed protections 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.

Some agreements do not provide for any absolute standards of protection for intellectual property rights, but do provide for national treatment or non-discrimination with respect to protection of intellectual property. For example, article 5 of the Common Convention on Investments in the States of the Customs and Economic Union of Central Africa provides that:

*[f]oreign undertakings shall enjoy the same rights and protection regarding trade-marks and patents, trade labels and names and any other industrial properties as undertakings possessing the nationality of the member countries of the Union.*

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 EIIA. Most EIIAs provide only limited protection, however, against private interference. The significance of the specific provisions on intellectual property protection is that they do protect intellectual property against private interference.

As noted in the previous section, a few recent EIIAs have begun to include provisions clarifying the extent to which intellectual property is protected even against host country interference, specifically expropriation. Thus, even while EIIAs are including increasingly elaborate provisions to protect intellectual property rights against private infringement, they are circumscribing slightly the protection against host country interference.

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Provisions for the protection of intellectual property rights may provide only for non-discriminatory treatment in this respect and, if investment is defined to include intellectual property rights, may not provide any more protection than was already provided by the treaty's general provisions on non-discrimination. Alternatively, these provisions may require the parties to adhere to various existing multilateral agreements on investment protection. Whether to adhere to each of these agreements raises its own policy concerns, which can be addressed



through the decision to include or exclude such agreements in drafting the list of multilateral treaties to which the parties agree to adhere. It is important to consider, however, whether the parties have agreed to adhere to the other agreements or whether the parties have actually incorporated by reference the content of the other agreements into the EIIA. If the latter is the case, violations of the other agreements may be remediable under the dispute resolution provisions of the EIAs.

#### **e. Investor-State dispute settlement**

EIAs often provide for the possibility of settling disputes by means of consultations and negotiations between the parties. Some EIAs (e.g. association agreements and partnership and cooperation agreements concluded by the EC) specifically entrust these consultations and negotiations to the body (e.g. cooperation or association councils) charged with monitoring and implementing the agreement.

Certain EIAs include provisions authorizing arbitration of disputes involving the treaty between foreign investors and host States without the involvement of the investor's home State. These provisions are found mainly in EIAs that address investment protection issues only, as well as in EIAs that address both investment protection and liberalization.<sup>88</sup> However, many EIAs, particularly those that emphasize investment liberalization rather than investment protection, do not include a right to investor-State dispute resolution. Thus, EIAs signed by the EC with third countries, for example, do not have special provisions on the settlement of investment disputes. Instead, investment disputes arising from these agreements are dealt with under the general disputes settlement provisions, which are at the State-to-State level. Finally, some highly integrated groups have set up permanent institutions to address and adjudicate on issues relating to the interpretation and application of the EIA (e.g. the EC European Court of Justice).<sup>89</sup>

Under customary international law, a State is not subject to the jurisdiction of an international tribunal unless the State consents. Moreover, under customary international law foreign investors are subject to the jurisdiction of the host State. For these reasons, typically the investor-State EIA provision includes the consent of the host State to arbitration of certain investment-related disputes, usually those arising under the investment provisions of the EIA.

Occasionally, an EIA contains language that provides for investor-State dispute resolution only upon further agreement of the parties. For example, article 48 of the Free Trade Agreement between the EFTA States and Singapore authorizes international arbitration of disputes between investors and the host State, but only if both parties mutually agree. The agreement authorizes submission of the dispute to ICSID, the Additional Facility of ICSID or an ad hoc tribunal under the UNCITRAL Rules.

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<sup>88</sup> For a comprehensive and detailed discussion of issues involved in investor-State disputes settlement, see UNCTAD (2003b). For a review of investor-State arbitration cases and the issues they raise, see UNCTAD (2005b, forthcoming).

<sup>89</sup> For a comprehensive and in-depth discussion of issues involved in State-State disputes settlement, see UNCTAD (2003c).

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Similarly, the Australia-United States FTA includes a provision that calls for consultations in the event that either party wishes to establish an investor-State dispute resolution mechanism. Article 11.16 provides that:

*[i]f a Party considers that there has been a change in circumstances affecting the settlement of disputes on matters within the scope of [the investment chapter] and that, in light of such change, the Parties should consider allowing an investor of a Party to submit to arbitration with the other Party a claim regarding a matter within the scope of this Chapter, the Party may request consultations with the other Party on the subject, including the development of procedures that may be appropriate...*

It appears from the language that both parties believed that an investor-State dispute resolution mechanism was unnecessary, presumably in the light of the nature of the legal system in the two countries, and thus both parties preferred that disputes be submitted to domestic courts. At the same time, however, a provision was made for creating an investor-State dispute resolution mechanism in the event that the situation changed and either party believed such a mechanism to be desirable.

One issue that arises in this type of provision involves the selection of arbitral mechanisms that may be used. It has become fairly common practice for EIAs to permit the investor to select from among more than one mechanism. Because EIAs are often regional agreements, arbitral mechanisms based in a particular region are sometimes identified as a potential dispute resolution mechanism in an EIA.

For example, the ASEAN Agreement for the Protection and Promotion of Investments provides for arbitration of any dispute between the investor and the host State arising directly out of an investment. Arbitration may be before ICSID, an ad hoc panel under the UNCITRAL Rules, the Regional Center for Arbitration in Kuala Lumpur or any other regional centre for arbitration in ASEAN. Unlike some EIAs, the ASEAN agreement does not allow the investor to choose the arbitral procedure, but calls for selection through mutual agreement. If agreement cannot be reached, the agreement specifies a mechanism for formation of an ad hoc tribunal that will determine its own procedure.

The most elaborate provision for investor-State arbitration may be found in the NAFTA and some of the recent FTAs that follow the NAFTA model. The NAFTA authorizes the investor to submit claims that the host State has breached the investment chapter of the NAFTA to arbitration before ICSID, the Additional Facility or an ad hoc tribunal under the UNCITRAL Arbitration Rules. The NAFTA provision, which is far too detailed to quote here, addressed a number of issues on which other provisions found in EIAs are often silent, such as the submission of the same dispute to local courts, the place of arbitration, appointment of experts, remedies available, including interim measures, and finality and enforcement of awards (UNCTAD, 2003b).

Although investor-State dispute settlement provisions originate from BIT practice, several provisions of the NAFTA investor-State dispute resolution provision reflect the fact that an agreement with more than two parties may raise concerns that do not originate from a bilateral investment treaty. Article 1128 allows a party to the treaty that is not a party to the dispute to make submissions to the tribunal on issues involving the interpretation of the agreement, while article 1129 allows any party to obtain copies of the evidence and arguments submitted by the

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disputants. Article 1126 authorizes the formation of a special tribunal to assume jurisdiction over separate claims that have a question of law or fact in common, a mechanism to promote efficient dispute resolution as well as to avoid inconsistent results.

Recent EIAs that follow the NAFTA model have added provisions intended to address certain concerns that have arisen over the years as investor-State dispute resolution mechanisms have been applied to resolve disputes. One such concern involves the lack of transparency of the proceedings. Two groups in particular have reason for concern. First, investors protected by the agreement, but not parties to the dispute, as well as the home country (which presumably will also not be a party to the dispute) may be concerned that provisions that affect their interests will be interpreted, without their participation, in ways that will affect them adversely in the future. Second, various groups within the territories of the parties may be concerned that the arbitration could affect their interests, without their participation. For example, an overly broad interpretation of the expropriation provision that restricted the host country's ability to enact environmental regulations could affect adversely the regulatory powers of the home State as well as the host State, and could also affect those interested in protecting the environment in the territories of the parties. In response to such concerns, article 10.20 of the Free Trade Agreement between Chile and the United States, for example, 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. That article also requires that the hearings be open to the public, although provisions are made for the protection of confidential business information. These provisions do not require the parties to make public any settlement discussions, nor do they interfere with the confidentiality of the tribunal's deliberations. They do, however, ensure that the public has access to the evidence submitted (other than confidential proprietary information), the legal arguments made and the decisions rendered.

The Chile-United States FTA also expands upon article 1128 in the NAFTA, which authorizes the parties that are not involved in the dispute to submit briefs. Specifically, article 10.19 authorizes the tribunal to consider submissions from anyone. Thus, any person can observe the proceedings and potentially make submissions. Transparency provisions serve certain important goals but, like most treaty provisions, impose costs and circumscribe the discretion of the parties (see UNCTAD (2005b, forthcoming).

Another concern that has arisen is the possibility of incorrect or at least inconsistent decisions. Some have proposed that arbitrations be subject to appeal. For example, the same Chile-United States FTA provides in annex 10-H 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. Furthermore, article 10.19 provides that if the parties are parties to a multilateral agreement that establishes an appellate body to review awards by tribunals established 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 FTA. The free trade agreement concluded by the Central American States, the United States and the Dominican Republic goes even further. Annex 10-F provides that, within three months of entry into force of the agreement, the commission created by the agreement shall establish a negotiating group to develop an appellate body to review awards rendered by a tribunal established through the investor-State dispute resolution mechanism. The appellate body "*shall be designed to provide coherence to the interpretation of investment*

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*provisions in the Agreement*". The negotiating group is instructed to take into account certain issues, including but not limited to:

- (a) *the nature and composition of an appellate body or similar mechanism;*
- (b) *the applicable scope and standard of review;*
- (c) *transparency of proceedings of an appellate body or similar mechanism;*
- (d) *the effect of decisions by an appellate body or similar mechanism;*
- (e) *the relationship of review by an appellate body or similar mechanism to the arbitral rules that maybe selected under [the investor-State dispute resolution mechanism]; and*
- (f) *the relationship of review by an appellate body or similar mechanism to existing domestic laws and international law on the enforcement of arbitral awards.*

The negotiating group is charged with providing a draft amendment to the agreement within one year of the formation of the group.

A related concern is that the same investment dispute may be submitted to multiple forums, which will thus require the host State to respond to the same claims more than once and raise the possibility of inconsistent decisions. Of special concern is the possibility that the investor may submit a dispute to the domestic courts of the host State and to international arbitration. In the past, this problem has been at least partially addressed in EIAs by a provision that the dispute may be submitted to arbitration under the investor-State dispute resolution mechanism only if it has not already been submitted to local tribunals. That is, if the investor submits the dispute to the domestic courts, the right to submit it to arbitration under the investor-State dispute resolution mechanism is lost. More recent provisions appearing in the EIAs attempt to foreclose another approach by investors, which is to submit the dispute to arbitration and then submit it to local courts. For example, article 14.3 of the Australia-Singapore agreement conditions the consent of the host State to arbitration upon the investor's waiving of:

*"its right to initiate or continue any proceedings (excluding proceedings for interim measures of protection . . . before any of the other dispute settlement fora referred to [this article] in relation to the matter under dispute."* The other forums to which the waiver would apply include *"the courts or administrative tribunals of the disputing Party"*.

Some EIAs have limited the parties that can file claims, thus potentially reducing the number of claims submitted arising out of the same dispute. For example, article 10.21 of the Free Trade Agreement between Chile and the Republic of Korea provides that an investment may not submit a claim under the investor-State dispute resolution mechanism. Thus, only the investor may submit a claim. Of course, an investment may have many investors, not all of whom have the same nationality. Thus, this provision does not entirely prevent the submission of the same dispute to multiple forums. The provision serves another purpose in any event. Because the investment is made in the territory of the host country, the provision avoids the possibility that a host State will be engaged in an international arbitration with a company that is its own national (though owned by foreign nationals). Investors are covered by the treaty only if they are nationals of the other party, and so the concern does not arise in their case.

Investor-State dispute resolution mechanisms in EIAs sometimes apply to disputes concerning an investment and are not explicitly limited in their application to disputes arising out of a violation of a provision of the EIA. Thus, while they may appear in an investment chapter,

they could potentially be invoked to enforce provisions of other agreements, including other multilateral agreements, as long as those disputes relate to covered investment.

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The negotiation of an EIIA is likely to raise the issue of whether to include a provision for investor-to-State dispute resolution and, in particular, how to define the scope of the provision. No agreement, no matter how well crafted, can anticipate every question that may arise and the spread of foreign investment means that disputes concerning investments are inevitable. Historically, investment disputes were resolved by negotiation or even arbitration between the home and host States, which meant that these disputes could become a political issue between the two States. The investor-State dispute resolution mechanism is intended to remove the home State from the dispute, without depriving the investor of a means of resolving the dispute. Its inclusion, however, also means that the host State's future investment policy decisions may be subject to review by arbitral tribunals formed in cooperation with affected investors. Defining the range of disputes to which the provision applies is an important way of circumscribing the category of policy decisions subject to arbitral review.

Some EIAs give potentially wide scope to the investor-State dispute resolution mechanism by making it applicable to disputes concerning an investment, which may include disputes that do not arise under the agreement. This gives the broadest assurance to a potential investor, but also opens the possibility that disputes arising under other agreements or even under domestic law will be subject to international arbitration. Other EIAs limit the scope of the provision to disputes arising under the agreement or, if the agreement involves subjects other than investment, to disputes arising under the investment chapter of the agreement. In that situation, the scope of the investor-to-State dispute resolution mechanism depends upon the scope of the substantive provisions of the agreement. The interactions can be complex. For example, the MFN clause of an investment agreement could entitle an investor of one State to treatment guaranteed to investors of another State by a different agreement, with the result that the investor-State dispute resolution provision could be used ultimately to interpret and apply to the circumstances of an investor commitment made to other States in other agreements. Similarly, to the extent that an EIIA refers to or incorporates obligations under other agreements, such as the GATS, TRIPS or TRIMs agreements, disputes involving the interpretation or application of those agreements could be subject to the investor-State dispute resolution mechanism of the EIIA.

Complexities may also arise where multiple chapters of an agreement apply to the same investment. For example, services that are delivered through a commercial presence could be protected by both the trade-in-services chapter and the investment chapter of an EIIA. A regulatory act by the host State might be alleged to have violated both chapters, thus allowing the investor to invoke the investor-State dispute resolution mechanism of the investment chapter as well as the dispute resolution mechanism applicable to the services chapter. To the extent that the commitments made under the services chapter parallel commitments made under the GATS, the dispute may simultaneously be presented to both the WTO dispute resolution procedures and the investor-to-State dispute resolution mechanism. Countries may wish to incorporate language into the agreement that would require an election of remedies and prevent resolution of the same dispute through multiple processes.

Because EIAs often have more than two parties, the investor-to-State dispute resolution mechanism can raise policy issues that do not arise under BITs. For example, one party may be

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involved in an investment dispute that will result in an interpretation of the agreement that will affect the other parties in the future. To protect their interests, all parties may wish to have the opportunity to participate in any dispute resolution procedure involving the interpretation or application of the agreement. Such a provision, however, may limit the ability of the State involved in the dispute to control or maintain the confidentiality of the proceedings.

Numerous policy choices present themselves in the details of the investor-to-State dispute resolution mechanism. One of the most important decisions is the choice of mechanisms that will be available. As noted above, many EIAs specify arbitration through ICSID or an ad hoc tribunal operating under the UNCITRAL rules, but other alternatives are available and each has its own peculiarities. The parties are also free to agree on matters not covered by the rules of the applicable dispute resolution mechanism. For example, the parties may wish to specify the location of any arbitration, a matter that can affect the cost of arbitration as well as the enforceability of the arbitral decision.

#### 4. *Investment Promotion*

A fourth set of investment issues addressed in EIAs concerns investment promotion. A major objective of an EIA's liberalization and protection provisions is to encourage investment flows between the parties. In addition, many EIAs, especially EIAs involving countries at different levels of development, or between developing countries, include provisions requiring the parties to cooperate in promoting investment flows among themselves. This is the case, for example, with the EC partnership and cooperation agreements, Euro-Mediterranean agreements and some EFTA agreements. Other EIAs only require the parties to engage in cooperation, one aim of which is investment promotion.<sup>90</sup> On the other hand, agreements signed by the United States and involving developing countries do not normally contain specific promotion commitments.

Investment promotion provisions in EIAs may be analysed according to several characteristics. These include the nature of the obligation assumed, the intended beneficiary of the promotion efforts and the party upon whom the obligation is placed.

The nature of the obligation assumed is generally of one of three types.

The first type is a general commitment to promote investment flows, often stated as part of a larger commitment to economic cooperation. For example, article 3 of the Framework Agreement for Cooperation between the European Economic Community and the Cartagena Agreement provides that.

*The Contracting Parties, taking into account their mutual interest and medium- and long-term economic objectives, undertake to establish between themselves economic cooperation of the widest possible scope, from which no field of activity is excluded in principle. The aims of such cooperation shall be in particular to... encourage the flow of investment and the transfer of technology and reinforce investment protection....*

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<sup>90</sup> This is the case, for example, with the recent agreements signed between Australia and Japan, between Australia and China, between ASEAN and China, between India and Thailand, between Canada and South Africa, and SAFTA, among others.



The second type of commitment specifies certain activities that the parties may undertake to promote investment flows. These may include, for example, information exchange, technical assistance or encouraging cooperation among private entities. Thus, article 4 of the Cooperation Agreement between the European Community and the Republic of India on Partnership and Development, after stating one of its aims to be to “*encourage the two-way flow of Community-Indian trade and investments*”, lists the following means which the parties:

*shall consider. . .to achieve these aims:*

- *exchange of information and ideas,*
- *preparation of studies,*
- *provision of technical assistance,*
- *training programmes,*
- *establishment of links between research and training centres, specialized agencies and business organizations,*
- *promotion of investment and joint ventures,*
- *institutional development of public and private agencies and administrations,*
- *access to each other’s existing data bases and creation of new ones,*
- *workshops and seminars,*
- *exchanges of experts.*

The third type of provision authorizes preferences for certain covered investors. This type of provision, which is typically too lengthy to be quoted here, is generally found in older agreements among African or Arab States.<sup>91</sup>

EIIAs are often written as if all parties are intended to be the beneficiaries of efforts to promote investment flows. For example, the investment promotion provisions of article 13-16 of the Free Trade Agreement between Costa Rica and Mexico are intended to “*increasing reciprocal investments*”. The same approach is found in many free trade agreements between Latin American countries.

Some agreements, however, specify that the intent of the provision is to promote investment in the territory of one of the parties to the agreement only. For example, article 74 of the association agreement between the European Community and Romania provides that:

1. *Cooperation shall aim to establish a favourable climate for private investment, both domestic and foreign, which is essential to economic and industrial reconstruction in Romania.*
2. *The particular aims of cooperation shall be:*
  - *for Romania to establish a legal framework which favors and protects investment,*
  - *the conclusion by the Member states and Romania agreements for the promotion and protection of investment,*
  - *to implement suitable arrangements for the transfer of capita,*
  - *to bring about better investment protection,*
  - *to proceed with deregulation and to improve economic infrastructure,*

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<sup>91</sup> For example, the 1970 Agreement on Investment and Free Movement of Arab Capital among Arab Countries signed by the members of Arab Economic Community, the 1965 Common Convention on Investments signed by the members of the UDEAC, and the 1982 Community Investment Code signed by the members of the Great Lakes Economic Community.

- to exchange information on investment opportunities in the form of trade fairs, exhibitions, trade weeks and other events.

Similarly, article 46 of the Euro-Mediterranean Agreement between the European Communities and Egypt provides that “[c]ooperation shall aim at increasing the flow of capital, expertise and technology to Egypt...” and then lists a variety of mechanisms to be used.

In these agreements, both parties have assumed an obligation. The obligation, however, is to promote investment flows into the territory of one of the parties only. The Cotonou Agreement provides another example (box IV.2).

#### **Box IV.2. Investment promotion provisions in the Cotonou Agreement**

The Partnership Agreement between the Members of the African, Caribbean and Pacific Group of States, of the One Part, and the European Community and Its Member States, of the Other Part does not include substantive provisions on investment liberalization or protection, leaving instead these matters to be developed in future reciprocal partnership agreements. The agreement does include, as part of its cooperation strategies, detailed provisions aimed at encouraging development-oriented private investment flows to the ECP countries.

##### **Investment promotion**

In article 75 of the Agreement, the EC and ACP States recognize the importance of private investment in the promotion of their development cooperation and acknowledge the need to take *inter alia* the following steps to promote such investment:

- Implement measures to encourage participation in their development efforts by private investors who comply with the objectives and priorities of ACP-EC development cooperation and with the appropriate laws and regulations of their respective States;
- Take measures and actions which help to create and maintain a predictable and secure investment climate, as well as enter into negotiations on agreements which will improve that climate;
- Encourage the EU private sector to invest and to provide specific assistance to its counterparts in the ACP countries under mutual business cooperation and partnerships;
- Facilitate partnerships and joint ventures by encouraging co-financing;
- Sponsor sectoral investment forums to promote partnerships and external investment;
- Support efforts of the ECP countries to attract financing, with particular emphasis on private financing, for infrastructure investments and revenue-generating infrastructure critical for the private sector;
- Support capacity building for domestic investment promotion agencies and institutions involved in promoting and facilitating foreign investment;
- Disseminate information on investment opportunities and business operating conditions in the ACP countries; and
- Promote national, regional and ECP-EU private sector business dialogue cooperation and partnerships, in particular through an ACP-EU private sector business forum.

##### **Investment guarantees**

In article 77 of the partnership agreement, the parties recognize also that investment guarantees are an increasingly important tool for development finance as they contribute to reducing risks and generating private capital flows. They therefore agree that cooperation shall ensure the increasing availability and use of risk insurance as a risk-mitigating mechanism in order to boost investment confidence in the ACP countries.

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### Box IV.2. Investment promotion provisions in the Cotonou Agreement (concluded)

In addition, they agree that cooperation shall offer guarantees and assist with guarantee funds covering risks for qualified investment. Specifically, cooperation shall provide support to:

- Reinsurance schemes to cover foreign direct investment by eligible investors against legal uncertainties and the major risks of expropriation, currency
- Investors may insure projects for any combination of the four types of coverage;
- Guarantee programmes to cover risk in the form of partial guarantees for debt financing. Both partial risk and partial credit guarantee shall be available; and
- National and regional guarantee funds, involving, in particular, domestic financial institutions or investors, for encouraging the development of the financial sector.

Cooperation shall also provide support to capacity-building, institutional support and participation in the core funding of national and/or regional initiatives to reduce the commercial risks for investors (*inter alia* guarantee funds, regulatory bodies, arbitration mechanisms and judiciary systems to enhance the protection of investments improving the export credit systems).

Cooperation shall provide such support on the basis of complementary and added value with respect to private and/or public initiatives and, whenever feasible, in partnership with private and other public organizations. The ACP and the EC within the framework of the ACP-EC Development Finance Corporation Committee shall undertake a joint study on the proposal to set up an ACP-EC guarantee agency to provide and manage investment guarantee programmes.

#### Investment protection

In article 78, the ACP and the European Community States affirm, within the scope of their respective competencies, the need to promote and protect each party's investments on their respective territories, and in this context affirm the importance of concluding, in their mutual interest, investment promotion and protection agreements which could also provide the basis for insurance and guarantee schemes.

In addition, in order to encourage European investment in development projects of special importance to, and promoted by, the ACP States, the Community and the ACP States may also conclude agreements relating to specific projects of mutual interest where the Community and the European enterprises contribute to their financing.

The parties also agree to introduce, within the economic partnership agreements, and while respecting the respective competencies of the Community and its member States, general principles of protection and promotion of investments, which will endorse the best results agreed in the competent international forums or bilaterally.

Source: UNCTAD (1996-2005, vol. VI, pp. 452-455).

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When negotiating investment promotion provisions, policy issues arise concerning the level of detail at which to specify the parties' obligations, the identity of the parties who are intended to benefit from investment promotion activities, and the identity of the parties who are obligated to engage in the specified activities. For example, where the EIIA is a bilateral agreement between a developed and a developing country or is an agreement between a group of developed countries, such as EFTA, and a developing country, the agreement may call for investment promotion in the developing country. Where the EIIA is a regional agreement among

developing countries, all parties are likely to be intended beneficiaries. Among the most critical issues may be whether the agreement creates a mechanism to ensure that investment promotion activities actually occur. This may be done, for example, through the creation of a standing body or through a requirement for periodic consultations.

### 5. Investment Regulation

A fifth set of policy issues involves investment regulation. EIAs often include provisions intended to regulate investment. The most common provision of this kind is one intended to limit practices that restrict or distort competition. Provisions regulating restrictive business practices appear in most types of EIAs signed by the European Community and EFTA countries with third countries, as well as in the recent bilateral free trade agreements that expand and elaborate on the NAFTA model. The breadth and depth of these provisions vary considerably between different types of EIA.

Provisions on competition in EIAs can be traced to the Treaty of Rome. Article 81 of that treaty (consolidated text) provides that:

*[t]he following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which has as their object or effect the prevention, restriction or distortion of competition within the common market and in particular those which:*

- (a) directly or indirectly fix purchase or selling prices or any other trading conditions;*
- (b) limit or control production, markets, technical development, or investment;*
- (c) share markets or sources of supply;*
- (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;*
- (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.*

Article 81 goes on to state that “[a]ny agreements or decisions prohibited pursuant to this Article shall be automatically void”. It allows exceptions, however, for some agreements, decisions and practices that contribute to improving the production or distribution of goods or to promoting technical or economic progress. Article 82 requires the parties to prohibit any abuse of a dominant position within a substantial portion of the common market. Additional articles create mechanisms for implementing the principles of articles 81 and 82.

The agreements of association concluded by the European Community with transitional economies in Europe contain a provision on competition that is similar in scope. For example, article 64 of the agreement with Bulgaria declares incompatible with the functioning of the agreement not only decisions, practices or agreements which have as their object or effect the prevention, restriction or distortion of competition and abuses of dominant position, but also any public aid that distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods. Practices contrary to that article are to be assessed on the basis of criteria arising from the application of the provisions of the Treaty of Rome. The agreement

establishes a mechanism for adopting rules to implement article 64. The Euro-Mediterranean Agreements take a similar approach.

The EFTA free trade agreements with non-member States have a similar scope, but are different in operation. For example, article 18 of the EFTA agreement with Romania declares as incompatible with the proper functioning of the agreement those decisions, practices and agreements that have as their object or effect the prevention, restriction or distortion of competition and abuse of dominant position. After three years, this provision will also apply to public undertakings and undertakings for which the Parties grant special or exclusive rights insofar as the application of the provisions does not obstruct the performance of the particular public tasks assigned to them. The EFTA provision, however, does not establish a mechanism for adopting directives nor does it declare such activities automatically void. Rather, it allows a party to the agreement to take appropriate measures in the event that it considers that a given practice is incompatible with article 18 and that the practice threatens serious prejudice to the interests of that State or material injury to its domestic industry.

Extensive provisions on competition policy have also begun to appear in recent EIAs that do not involve a European State, although such provisions typically take a different approach from the European provisions. For example, the Free Trade Agreement between Australia and the United States contains a separate chapter on competition-related matters. Article 14.2 provides that “[e]ach Party shall maintain or adopt measures to proscribe anticompetitive business conduct and take appropriate action with respect thereto...” Thus, the Australia-United States agreement does not define as precisely the sorts of conduct to which it applies nor does it declare such conduct unlawful. Rather, it obligates the parties to proscribe “*anticompetitive business conduct*,” without defining the term, and requires each party to maintain an authority responsible for enforcing its national competition laws. Article 14.3 of the Australia-United States agreement permits each party to designate monopolies, although these designated monopolies are subject to certain restrictions. For example, a designated monopoly must act in a manner not inconsistent with the party’s obligations under the agreement when exercising any regulatory, administrative or other governmental authority delegated to it, must act solely in accordance with commercial considerations in purchasing or selling the monopoly good or service in the relevant market, must provide non-discriminatory treatment to covered investment and to goods and service suppliers of the other party in purchasing or selling the monopoly good or service, and may not use its monopoly position to engage in anticompetitive practices in a non-monopolized market in its territory where such practices adversely affect covered investment. Under article 14.4, State enterprises may not act in a manner that is inconsistent with the party’s obligations under the agreement when exercising any regulatory, administrative or other governmental authority or must accord non-discriminatory treatment in the sale of its goods or services. The agreement, at articles 14.8, 14.9, and 14.10, respectively, requests the parties to make available to the other party upon request certain public information concerning anticompetitive business conduct, to cooperate to promote competition policies and to enter into consultations upon the request of either party. The agreement, however, excludes from any dispute settlement mechanism under the agreement matters arising under article 14.2 (the article that requires the parties to proscribe anticompetitive business conduct).

On the other hand, NAFTA's chapter on competition (Chapter Fifteen) does not directly regulate anticompetitive practices. Instead, article 1501(1) calls upon each party to adopt measures to proscribe anticompetitive business conduct. The article further provides for consultations to discuss the effectiveness of the measures undertaken by each party. Article

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1501(2) calls for cooperation and coordination on issues of competition law enforcement, including mutual assistance, notification, consultation and exchange of information relating to the enforcement of competition laws and policies in the free trade area.

The competition provision differs from other EIIA provisions in that, while most other provisions seek to insulate foreign investment from host country regulation, this provision requires the host country (or a competent intergovernmental body) to impose restrictions on the operation of investments. It is also unusual in that, by its terms, it applies equally to foreign and domestic investment, although where the host country fails to restrict the anticompetitive behaviour of a foreign investment, an injured domestic investor often 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 in practice may actually be principally a restriction on domestic investors. Of course, in the case of an EIIA with more than two parties, one of the parties other than the home or host State might object if the host State fails to restrict anticompetitive behaviour 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.

In any event, it is easy to conclude that this provision, despite being structured as a restriction on investment, is intended principally to protect foreign investment against natural or State-created advantages enjoyed by domestic investors. Thus, the competition provisions may be seen as investment protection provisions in that they protect foreign investment against the conduct of private parties. In that sense, they are similar to the intellectual property provisions that have been common in EIAs. Competition provisions may also be regarded as investment liberalization provisions in that they are intended to remove potential barriers to the entry of foreign investment. They differ from other investment liberalization provisions, however, in that the barriers being removed may be created by private competitors rather than the host country itself. In any event, to the extent that the host country wishes to allow a particular domestic firm to enjoy a monopoly position as part of its development policy, it will need to exclude, or negotiate an exception to, this provision.

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In existing EIAs investment regulation mainly takes the form of provisions to restrict anticompetitive behaviour and they are widely found in agreements with the European Community or with EFTA. The core provisions normally apply to anticompetitive behaviour by investments and to that extent the provisions are nominally even-handed in that they apply to local and foreign investment equally, although local investors may lack the means to enforce the provisions. Some provisions, however, go further and apply to State action, such as public aid, that favours one investment over another, action that may also be inconsistent with the agreement's non-discrimination provisions, depending upon who the recipient of the public aid is. This raises the question whether the host country may wish to preserve the prerogative to spend its tax revenues for the benefit of certain industries in at least some cases, which may require the negotiation of narrower language in the competition provision or the insertion of exceptions.<sup>92</sup> Policy questions also arise concerning how these restrictions are to be enforced, given that they are directed at non-parties to the agreement, namely investments, rather than the States. The EIIA may require that a mechanism be established to enforce the provisions or it may simply

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<sup>92</sup> It also raises issues of the relationship between competition provisions and any provisions dealing with subsidies and other incentives contained in the agreement in question.



require consultations in the event that one party believes a violation exists. Some agreements declare certain anticompetitive behaviour unlawful, thus creating the possibility, depending upon the domestic legal system of the State, that a foreign investment might be able to directly challenge the anticompetitive behaviour in local courts on the basis of its illegality under the treaty.<sup>93</sup>

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The foregoing comparative analysis of investment provisions in EIAs confirms the earlier observation that the majority of these provisions have been influenced by previous EIAs and by other investment agreements, notably by the BITs and the WTO Agreements. At the same time, important differences remain between EIAs and other investment agreements.

Moreover, while it is possible to identify a number of patterns in relation to the purposes, structures and the approaches to investment in recent EIAs, even similar types of EIAs exhibit important variations with respect to the coverage of investment issues and the formulation of specific investment provisions. These variations indicate different degrees of depth in the level of investment integration afforded by EIAs.

In the final analysis, the scope and content of individual investment provisions of an EIA depend to a significant extent on their interaction with other provisions of the agreement. The interaction may involve specific provisions on investment among themselves and/or with general provisions of the agreement, as well as with specific provisions on trade or other economic transactions. In turn, these interactions between an expansive set of rules within an EIA addressing investment as well as other economic transactions, such as trade in goods, services, knowledge and labour, increase the risk of overlaps and inconsistencies. In these circumstances, the interpretation and application of EIA rules become increasingly difficult and prone to disputes. To avoid or minimize these difficulties, EIAs have developed a number of devices that are discussed in the next chapter.

At the same time, the proliferation of EIAs (and other investment agreements) with overlapping membership is creating a multilayered and multifaceted web of interrelated investment rules and commitments (see the “spaghetti bowl”, figure I.1. above). This raises a number of policy challenges. In particular, while EIAs and other agreements may generally be consistent with or complement each other, there may also be cases of overlap and inconsistencies. The next chapter examines also a number of specific issues that arise with the interaction between agreements, and considers various solutions.

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<sup>93</sup> For a more elaborate discussion of competition issues in relation to IAs, see UNCTAD (2004c).

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## **V. INTERACTIONS**

There are three main types of interactions affecting the investment rules of EIAs. The first type of interaction occurs between investment rules within the EIA. The second type of interaction takes place when an EIA's rules on trade, investment and/or other types of transactions affect related aspects of the same activity. The third type of interaction is between EIAs and between EIAs and other types of investment agreements.

### **A. Interactions between Provisions within EIAs**

As the investment rules of an EIA become increasingly comprehensive and complex, and especially since investment is only one of various disciplines addressed by these agreements, investment provisions of EIAs sometimes interact such that the full impact of a provision cannot be determined by reading that provision alone. Such interactions fall into two broad categories. One broad category includes those situations in which different provisions of EIAs interact to provide meaning to each other and thereby to define the obligations of the parties. A second broad category of interactions includes those situations in which there is overlap and inconsistency between two or more provisions applying to related aspects of the same activity.

#### ***1. Interactions between Investment Provisions***

The most common types of interactions between investment provisions in an EIA take place in the context of the first category, that is when two or more investment provisions interact to complement or qualify the obligations of the parties. The first of the situations in which this occurs involves the interaction of the definitions provisions of agreements with the substantive provisions. For example, the expropriation provision found in many EIAs 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 second situation involves the interactions of general exceptions with the substantive provisions of the agreements. For example, the expropriation of assets within the definition of "investment" might nevertheless not require the payment of compensation if the seizure of the assets were within a general exception for measures necessary for protecting national security interests. That is, the meaning of a substantive provision, such as the expropriation provision, can be ascertained only by reference to the general exception provisions as well as the definitions provisions. The definitions and general exceptions, moreover, are themselves effectively meaningless until considered with the substantive provisions.

The third situation involves the interaction of the substantive provisions with the dispute resolution mechanisms. For example, some EIAs contain an investor-State dispute resolution mechanism that applies to disputes involving the provisions of the EIA. Thus, the disputes that are within the jurisdiction of any tribunal formed in accordance with this provision can be identified only by referring to the relevant substantive provisions. Without the substantive provisions, the dispute resolution provision is meaningless. At the same time, the substantive provisions gain much of their force by the presence of the dispute resolution mechanism.

## 2. *Interactions between Investment and Other Provisions*

When investment provisions overlap with other provisions of an EIIA, obvious problems arise if there is inconsistency or conflict between them. One situation in which this might happen occurs in agreements that have a chapter on investment and a separate chapter on trade in services. This situation can give rise to some special complexities because, as has been noted above, the admission and establishment provisions of the investment chapter are more likely to use a negative list approach, while the market access provisions of the trade-in-services chapter are more likely to use a positive list approach. Issues may arise concerning the interaction of the two chapters if the same sector is listed in the annexes to both chapters or in the annexes to neither. In the latter case, for example, the investment chapter would seem to grant a right of establishment in that sector, even though it was in a services sector and no market access commitments had been made in the market access list under the trade-in-services chapter. 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.

Several EIAs contain provisions that explicitly state which chapter shall prevail in the event of any inconsistency. One such provision in an EIIA appears in NAFTA, article 1112(1) of which 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”. Therefore, in the NAFTA, the investment chapter is subordinated to the other chapters. At the same time, however, the NAFTA seeks to ensure that all investments are covered by the investment chapter. Thus, article 1213 provides that the term “*cross-border trade in services*” does not include the provision of services by an investment. Accordingly, an investment of one party that provides services in the territory of another party is covered by the investment chapter, not the services chapter.

The interaction is extremely complex in some recent agreements, such as the Free Trade Agreement between Singapore and the United States. That agreement includes chapters on investment, services and financial services. Article 15.3 of the investment chapter contains the provision found in other NAFTA-inspired agreements, stating that in the event of any inconsistency between the investment chapter and another chapter, the other chapter shall prevail to the extent of any inconsistency. Article 8.1 of the chapter on cross-border trade in services contains the provision, also found in NAFTA, defining cross-border trade in services to exclude services supplied by an investment of one party in the territory of another party. Notwithstanding this general exclusion of investment from the services chapter, article 8.2 states that certain provisions of the services chapter do apply to measures by a party affecting the supply of services in its territory by an investor of the other party or a covered investment. Those provisions that do apply are those on market access, domestic regulation and transparency. Thus, not only do some portions of the services chapter apply to investment affecting cross-border trade in services, but also, under article 15.3, they actually prevail over the investment chapter provisions to the extent of any inconsistency. Article 8.2 also states that the cross-border trade in services chapter does not apply to financial services, except for the provisions on market access, domestic regulation and transparency. Article 15.3 provides that the investment chapter does not apply to financial services either. Thus, financial services, including financial services provided by covered investments, are governed by the financial services chapter. Article 10.1 of the financial services chapter, however, explicitly states that certain provisions of the services and investment chapters do apply to financial services, including those on expropriation, transfers and investor-State dispute resolution.

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As this indicates, where there are separate chapters on services and specific service sectors, the tendency is for the more specific chapter to prevail in the event of any inconsistency. This is to be expected because a separate chapter on one sector of the economy, such as financial services, is an indication that that sector raises special concerns. For example, because of the key role that the financial services sector plays in the stability of the entire economy, host States may wish to afford different treatment in that sector than in services sectors generally. If the general services chapter prevailed over the more specific chapter, the host State's purpose of having a separate chapter on a specific sector would be defeated. As the example of the Singapore-United States free trade agreement shows, however, the financial services chapter may well follow the same approach as the general services chapter in many respects.

Another situation in this category occurs where one provision of an EIIA amplifies the effect of another provision. For example, a host State that includes an EIIA with a chapter on trade in services modelled on the GATS may grant market access with certain limitations to service providers in a particular sector of the economy. Once a service provider has established a commercial presence in the host State 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. In that situation, the investment chapter has amplified the effect of the market access provisions of the trade-in-services chapter. Indeed, if the definition of "investment" is broad enough, even assets brought into the host State by a cross-border service provider that do not constitute a commercial presence might nevertheless be considered investment and be subject to the investment protection provisions of the EIIA.

Policymakers negotiating an EIIA must be careful to consider the combined effect of different provisions. It must be kept in mind that a transaction that is facilitated, promoted or protected by one provision might also be protected by other provisions, so that the effect of implementing one provision may be trigger the application of other provisions, perhaps in other chapters of the agreement.

Occasionally, EIAs have provisions intended to prevent one provision from amplifying the effects of other provisions. For example, the NAFTA includes a provision intended to prevent the investment chapter from being applied to services in certain cases. The concern was that financial security that a host State might require a foreign service provider to offer as a condition for being entitled to deliver cross-border services might be defined as investment, resulting in the application of the investment chapter to the service. To prevent that result, Article 1112(2) provides that:

*A requirement by a Party that a service provider of another Party post a bond or other form of financial security as a condition of providing a service into its territory does not of itself make this Chapter applicable to the provisions of that cross-border service. This Chapter applies to that Party's treatment of the posted bond or financial security.*

In other words, a bond or financial security would be considered investment and protected by the provisions of the investment chapter, but the investment chapter would not, merely by virtue of the posting of the bond, become applicable to the provision of the service.

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## **B. Interactions between Agreements Dealing with Investment**

The coexistence of an increasing number of EIAs and other types of investment agreements inevitably gives rise to multiple interactions between investment rules at all levels. EIAs sometimes include provisions that address the interaction between the EIA and another agreement. The most common types of provisions addressing these interactions fall into two categories: provisions aimed at ensuring consistency and those intended to address inconsistencies.

### **1. Ensuring Consistency**

Most commonly, EIA provisions addressing interactions between agreements assume consistency between the purposes of the EIA and those of the other agreement, and the EIA provisions are intended in some way to ensure adherence to, or at least action consistent with the provisions of, the other agreement. Several different approaches can be found in the EIAs.

#### **a. Concluding another agreement**

First, EIAs sometimes require the parties to conclude another agreement. This approach is typical of EIAs between the European Community or EFTA and a non-member State in which the parties agree to accede to a number of conventions for the protection of intellectual property. In those situations, the only obligation is to accede to the other agreements. A violation of the other agreements presumably would not also violate the EIA, except perhaps to the extent that the violation of the other agreement called into question whether the obligation to enter into the other agreement had been performed in good faith.

#### **b. Reaffirming commitments under other treaties**

Second, EIAs 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. Thus, article 29 of the European Community's Euro-Mediterranean agreement with Egypt "reaffirms" the parties' GATS commitments, particularly those relating to MFN treatment, and also incorporates the exceptions to MFN treatment provided for by the GATS. This provision presumably refers to evolving commitments under the GATS. That is, the parties reaffirm not only existing GATS obligations, but also future commitments made under the GATS. Similarly, article 12(1) of the Framework Agreement on the ASEAN Investment Area provides that "*Member States affirm their existing rights and obligations under the 1987 ASEAN Agreement for the Promotion and Protection of Investments and its 1996 Protocol*".

#### **c. Requiring observance of obligations under another agreement**

Third, EIAs sometimes require the parties to observe obligations under another agreement. The European Community has concluded treaties requiring the non-European party to abide by the TRIMs Agreement. For example, article 74 of the association agreement between the European Community and Bulgaria provides that "*Bulgaria shall honour the rules on Trade-*

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*Related Aspects of Investment Measures (TRIMs)*". Similarly, article 17(2) of the Free Trade Agreement between EFTA and the Czech Republic provides that:

*[t]he States Parties to this Agreement shall accord to each other's nationals treatment no less favourable than that they accord to their own nationals. Exemptions from this obligation must be in accordance with the substantive provisions Article 3 of the TRIPS Agreement.*

Article 17(2) has a parallel provision with respect to MFN treatment. A number of other agreements, negotiated by the EFTA States, include a similar provision, but also provide for national and MFN treatment, subject to exemptions in accordance with the TRIPS Agreement.

The effect of a provision in an EIIA requiring the parties to observe another agreement is to make a violation of the other agreement a violation of the EIIA. This in turn would often permit submission of a dispute involving an alleged violation of the other agreement to the dispute resolution mechanism of the EIIA. Language such as that described in the third approach would seem to have that effect. Language such as that described in the second approach might have it as well. If the other agreement has its own dispute resolution mechanism, presumably the dispute could be submitted to either mechanism, or to both.

#### **d. Incorporating obligations under other agreements: The MFN clause**

Fourth, EIAs may incorporate obligations under other agreements. For example, article 35 of the EFTA free trade agreement with Singapore provides that "[a]rticles 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 be literal. Article VIII of the ASEAN Framework Agreement on Services provides that:

*[s]chedules of specific commitments and Understandings arising from subsequent negotiations under this Framework Agreement and any other agreements or arrangements, action plans and programmes arising thereunder shall form an integral part of this Framework Agreement.*

The incorporation may also be quite broad, going beyond a few specific provisions. For example, article XIV of the ASEAN Framework Agreement on Services provides that:

*[t]he terms and definitions and other provisions of the GATS shall be referred to and applied to matters arising under this Framework Agreement for which no specific provision has been made under it.*

The free trade agreement between the Central American States and Chile incorporate five BITs already concluded between Chile and individual Central American States.

One provision common to EIAs that, in effect, incorporates the provisions of numerous other treaties is the MFN clause, requiring the host State to provide covered investment with treatment no less favourable than that provided to any other foreign investment. As a result of this provision, the host State is obligated under the EIIA to honour, with respect to covered investments, commitments made with respect to foreign investment in any other agreements. The

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obligations under those agreements in effect become obligations under the EIIA (UNCTAD, 1999d).

Alternatively, EIAs may treat other agreements as baseline agreements setting standards that the EIAs are intended to exceed. Article IV of the ASEAN Framework Agreement on Services 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, and under Article X may be modified or withdrawn after three years, provided that compensatory adjustments are made.

Or, the EIIA may treat the other agreement not as a floor, but as a ceiling, setting forth the maximum protection that may be provided under the EIIA. For example, article 51 of the Partnership Agreement between the European Community and the Russian Federation provides that:

*[t]reatment granted by either Party to the other hereunder shall, as from the day one month prior to the date of entry into force of the relevant obligations of the GATS, in respect of sectors or measures covered by the GATS, in no case be more favourable than that accorded by such first Party under the provisions of the GATS, and this, in respect of each service sector, subsector and mode of supply.*

The balance of the article includes a mechanism under which obligations under the EIIA may be adjusted in the light of the parties' obligations under the GATS.

EIAs often 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. An illustration of this approach is article VII(1) of the ASEAN Framework Agreement on Services, which provides that:

*[t]he Protocol on Dispute Settlement Mechanism for ASEAN shall generally be referred to and applied with respect to any disputes arising from, or any differences between Member States concerning the interpretation or application of, this Framework Agreement or any arrangements arising therefrom.*

To provide flexibility, however, Article VII(2) provides that “[a] specific dispute settlement mechanism may be established for the purposes of this Framework Agreement which shall form an integral part of this Framework Agreement”.

## **2. Addressing Inconsistencies**

All of the foregoing provisions assume consistency between the EIIA and another agreement. The question arises, however, as to how to address potentially inconsistent obligations under other agreements. Several approaches can be identified.

### a. Commitment not to modify parties' obligations under other agreements

One approach is to provide that the EIIA shall not modify or affect a party's obligations under any other agreement. For example, Article 30 of the EFTA free trade agreement with Singapore provides that:

*Any such recognition [of credentials and certifications of service providers] conferred by a Party shall be in conformity with the relevant provisions of the WTO and, in particular, Article VII of the GATS.*

Similarly, 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 agreements to which they are parties.*

A footnote to the provision indicates that “*Existing Agreements are not affected as these have been notified in the MFN Exemption List of the GATS*”. Thus, the ASEAN language would preserve any existing inconsistent obligation in another agreement. At the same time, the ASEAN language implies that the parties intend that future inconsistent obligations not be assumed. Specifically, Article IX(2) states that:

*[n]othing in this Framework Agreement shall affect the rights of the Member States to enter into other agreements not contrary to the principles, objectives and terms of the Framework Agreement.*

### b. EIIA provisions to prevail over other agreements

An alternative approach is to stipulate that the EIIA's provisions prevail over those of the 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.*

Note that this provision does not apply to agreements between a party and third countries.

### c. Establishing a mechanism for resolving inconsistencies

Yet another approach is not to resolve the inconsistency, but to establish a mechanism for resolving it in the future. For example, article 5 of chapter 17 of the Australia-Singapore free trade agreement provides that:

*[i]n the event of any inconsistency between this Agreement and any other agreement to which both Parties are parties, 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.*

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Thus, in this approach, resolution of any inconsistencies is left to future consultations. This provides flexibility, which may be important because the parties very likely cannot anticipate the inconsistencies that may be discovered later and thus may wish to reserve their position on how conflicts are to be resolved until the specific conflicts have been identified. Of course, consultations may not result in agreement on how to resolve the conflict and the result may be that one party observes the obligations of one agreement and the other party observes the inconsistent obligations of the other agreement, resulting in claims by each that the other has violated one of the agreements and invocation of any State-State dispute resolution mechanisms available, which could result in submissions to different forums and inconsistent results.

#### **d. Termination of a prior inconsistent agreement**

Conclusion of an EIIA may even result in the termination of a prior, potentially inconsistent agreement. For example, article 21.4 of the Free Trade Agreement between Chile and the Republic of Korea provides that upon entry into force of the FTA, the BIT between the two parties shall no longer be in effect. Neither shall the rights and obligations derived from the BIT. This latter clause is important because BITs typically provide that the protection they afford shall continue for some period of time, often 10 years, following termination of the agreement. The language of the Chile-Republic of Korea FTA in effect would repeal that provision of the BIT and extinguish rights and obligations intended to survive the termination of the BIT.

#### **e. Requiring the higher level of protection to prevail**

In some cases, the provisions of an EIIA and another agreement may be different, though not inconsistent. This occurs, for example, where two investment protection provisions require different levels of protection for investment. In this situation, EIAs sometimes explicitly require that the higher level of protection provided by the two different agreements be afforded. For example, article 12 of the Framework Agreement on the ASEAN Investment Area, after reaffirming the parties' rights and obligations under the ASEAN Agreement for the Protection and Promotion of Investment and its 1996 Protocol, states that:

*[i]n the event that this Agreement provides for better or enhanced provisions over the said Agreement and Protocol, then such provisions of this Agreement shall prevail.*

The provision may also contemplate that the other agreement may provide the more favourable treatment, in which case the other agreement should prevail. For example, article I of the Free Trade Agreement between Jordan and the United States states that:

*This Agreement shall not be construed to derogate from any international legal obligation between the Parties that entitles a good or service, or the supplier of a good or service, to treatment more favorable than that accorded by this Agreement.*

#### **f. Allowing the parties to choose**

Alternatively, the agreements may allow a party to choose which agreement shall be applied, where more than one agreement is applicable. For example, article 12 of the Australia-Singapore free trade agreement provides that the investment chapter shall not apply to:

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*a natural person who is a permanent resident but not a citizen of a Party where . . . the provisions of an investment agreement between the other Party and the country of which the person is a citizen have already been invoked in respect of the same matter...*

This provision addresses the situation where a natural person is a permanent resident of a party but a citizen of another State and is protected by investment agreements concluded by both States. If the natural person invokes the protection of the other State's investment agreement, it may not invoke the protection of the investment agreement concluded by the State of which he or she is a permanent resident. In effect, the person may choose to be protected by only one of the two agreements.

In addition to potential conflicts in substantive obligations, EIAs may have dispute resolution mechanisms that overlap with those under other agreements. This is particularly true with respect to the services provisions that may create obligations similar to those under the GATS and that may therefore give rise to disputes that could also fall within the WTO dispute resolution mechanism. One approach is to allow the parties to select the forum in which the dispute shall be resolved. For example, Article 56 of the EFTA free trade agreement with Singapore 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.*

Article 56(2) states that “[b]efore a Party initiates a dispute settlement proceeding under the WTO Agreement against another Party or Parties, or vice-versa, that Party shall notify all other Parties of the intention”.

The EIA may allow a choice only if both the parties agree. For example, article 17(4)(c) of the Free Trade Agreement between Jordan and the United States 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 same 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 both parties agree otherwise.

#### **g. Including an exception to the MFN clause**

Finally, just as an EIA may amplify the effects of another treaty by requiring that provisions in that other treaty be applied to investments covered by the EIA, another treaty may amplify the effects of the EIA. This occurs where obligations under the EIA are incorporated into another treaty, such as where the other treaty has an MFN clause that requires an EIA party to afford to the parties to the other treaty the same treatment as it provides to parties to the EIA. This may be undesirable for the party because the party may have extended favourable treatment to other parties under the EIA in exchange for certain commitments from those parties under the EIA that were not made by the parties to the other agreement. A party that wishes to avoid this result should insert into all other investment-related agreements that include an MFN clause an

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exception for the EIIA, under which the MFN obligation in that agreement does not apply to treatment afforded under the EIIA. However, this MFN exception would be effective only with respect to newly concluded other investment-related agreements (Karl, 1996).

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## VI. POLICY CHALLENGES

The number of EIAs has increased greatly, especially since the 1990s, and there are indications that it will continue to grow in the near future. Increasingly, EIAs involve countries with dissimilar economic characteristics and levels of development. A country contemplating the negotiation of an EIA faces a number of policy challenges, some of which are addressed here.

First, a country wishing to provide investors with assurances of a favourable investment climate may choose to do so through the inclusion of investment provisions in an EIA or through negotiation of another type of investment agreement. Therefore, an initial issue that arises concerns the nature of the agreement. To some extent, the choice of instruments between an EIA and another type of IIA, for example BITs, may depend upon a country's objectives in negotiating the agreement. The goal of attracting selected foreign investment by offering certain protections perhaps militates in favour of concluding a BIT type of agreement, while the goal of seeking some level of real integration into the regional or global economy by lowering at least some barriers to the international flow of capital may militate in favour of an EIA. Certain advantages of negotiating either EIAs or BITs relate not to the type of agreement but to the number of parties involved (UNCTAD, 1996). One of the main advantages of EIAs *vis-à-vis* other types of IIA is that, by addressing related economic transactions in a single framework, these agreements can provide policy coherence and coordination in the economic area.

Indeed, as noted in the introduction, the inclusion of investment provisions as part of an economic integration agreement covering trade and other types of economic transactions reflects a desire to expand and deepen integration efforts among a number of economies by facilitating investment flows between the parties. However, EIAs' approaches to investment issues vary considerably and reflect different visions concerning the policies that will best promote the economic welfare and development of the parties involved. A few EIAs, particularly some of the EIAs that include only developing countries and that date from the period before the late 1980s, assume that economic development rests on providing preferential treatment to investment from within the EIA area. The majority of recent EIAs, however, including many that involve only developing countries, assume that liberalizing investment flows among different economies will promote economic development by fostering the efficient allocation of resources and augmenting the factors of production available to developing economies.

Second, once the decision to negotiate an EIA has been made, a country faces a large number of more specific policy choices relating to the inclusion of particular investment provisions. Negotiation of an EIA does not occur in a vacuum, but in the context of the 218 EIAs that have already been concluded. Countries will inevitably come to the bargaining table with expectations about what should be included, based on their prior negotiating history or on the prior negotiating history of other States whose practices they consider instructive or wish to emulate.

As has been shown in this study, there are strong regional patterns among EIAs. For example, a country preparing to negotiate an EIA with the European Community or with EFTA will very likely find investment liberalization, competition policy and intellectual property protection high on the agenda. A country preparing to negotiate an EIA with a country from the Americas will find liberalization and intellectual property issues on the agenda, but also issues involving many of the kinds of investment protection provisions found in a traditional BIT. Many factors play a role in choosing a country with which to negotiate an agreement, but these



strong regional preferences are one consideration that may influence the choice of potential treaty partners.

As noted also in the introduction, a key driving force behind the conclusion of EIAs is the insertion of national economies in the globalization process as a means of counteracting the risk of economic marginalization. Thus, for many developing countries in particular, EIAs may be considered in themselves a development option. This consideration is of critical importance because, as the process of economic integration through an EIA intensifies, the lock-in effect of the agreement would affect an increasingly wider range of policies and options, thus limiting the policy space available for the adoption (or reconsideration) of appropriate development-oriented strategies (UNCTAD, 2003a; Abugattas, 2004, p. 3). Thus, developing countries negotiating EIAs must consider how best to incorporate a development dimension into the agreements. At a basic level, this raises the question of how an EIA contributes to economic development, a question that may not be answered in the same way for all countries. Some countries may be at a stage of development where they regard rapid and extensive integration into the global economy as an appropriate development strategy and will thus be willing to conclude high-standard agreements that apply equally to all parties. Other countries may be at a stage of economic development where integration must be slower and less extensive. They may wish to conclude agreements that have a narrower scope, fewer or weaker commitments, more exceptions, and transitional periods for implementation, and that apply differently to different parties at different stages of development.

Thus the most important development challenge, especially for the negotiation of future EIAs involving countries at different levels of development, is to strike a balance between the potential for the EIA to increase investment flows and the flexibility of countries to pursue their particular policy objectives in the light of their characteristics and changing circumstances. Economic development is more complex than merely increasing the total quantity of resources or ensuring their most efficient use. No country promotes economic development through a purely liberal investment policy. As part of their development policies, countries need to balance a series of potentially conflicting interests, some of which advocate in favour of excluding or regulating foreign investment and others of which may advocate in favour of promoting or protecting international investment flows.

This implies, among other things, that the EIA needs to allow a sufficient level of policy autonomy to national Governments of member countries to pursue their investment objectives. This autonomy may be best reflected in a number of investment issues on which diverging views exist. These include, notably, the substantive scope of the agreement, whether to afford the right of establishment, the scope of the national treatment provisions, regulation of the use of performance requirements and incentives, and competition policy, because they determine whether, and to what extent, preferences can be given to domestic enterprises. The flexibility instruments alluded to before may be specifically applied to these issues (UNCTAD 2003a, p. 173).

Furthermore, all countries have vital non-economic interests, which may be political, social or cultural, that require priority attention. Investment issues, such as the scope of expropriation actions and the recourse to investor-State dispute resolution, are sensitive because they directly affect the sovereignty of the host country to regulate in the public interest and to adjudicate on national public policy issues. As noted in chapter IV, various solutions to these issues are reflected in existing EIAs (UNCTAD 2003a, p.171).

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Indeed, the negotiation of investment provisions in an EIIA often involves difficult policy issues that touch upon a range of social and environmental concerns traditionally thought to belong to the domestic policy domain. As a result, EIAs are becoming one of the most visible manifestations of the growing internationalization of the domestic policy agenda. This implies that EIAs need to reflect in a balanced manner the rights and obligations of foreign investors and states. Failure to address this balance, either within the same instrument or by establishing bridges with other instruments, can have important development implications for host countries.

The key point is that economic development is the goal of every EIIA and development concerns must therefore be addressed in every provision of the agreement, although for different countries those concerns might well be addressed in quite different ways. Thus, the value of a given EIIA must be assessed in the light of all the economic circumstances of each party and that party's own economic development policy.

Third, the growing proliferation of EIAs and other investment agreements is resulting in a multilayered and multifaceted web of interrelated investment rules and commitments, and this is creating increasing difficulties for the interpretation and application of the rules (see the spaghetti bowl figure (figure I.1)). The types of difficulties that arise with the cross-membership of investment agreements of various types and at various levels have been illustrated in the preceding chapter. Other difficulties arising from the complexity and ambiguity of investment rules at all levels are even more difficult to tackle. Some relate, for example, to the lack of comparability in the scheduling of commitments and reservations. Others refer to the lack of consistency in the implementation of rules requiring national policy changes. Yet other inconsistencies may arise from the application of MFN obligations, as MFN clauses differ in their scope and coverage (UNCTAD, 2004a, pp. 237-238).

Several solutions exist to mitigate some of these problems. However, some of the difficulties are likely to persist, and this raises the broader policy issue of whether the elaboration of investment rules could proceed in a more consistent way through the establishment of adequate interpretation mechanisms and institutions.

Clearly, the difficulties of interpretation and implementation created by the interaction of an increasingly complex web of investment rules are particularly problematic for countries suffering from insufficient human resource and institutional capacity to interpret and implement EIAs. Unclear and complex rules are likely to translate into lengthy and costly disputes and, again, the most directly affected are likely to be the poorer countries. It is therefore crucially important that countries engaging in the negotiation of an EIIA bear in mind these potential difficulties and make provision for avoiding them. In particular, the provision of technical cooperation to the less developed parties of an EIIA should be an important way of ensuring the accomplishment of the EIIA's goals.

In the final analysis, the fundamental policy question becomes whether the proliferation of EIAs is likely to result in a large number of countries, especially the poorer countries, facing discrimination and exclusion, or whether EIAs can contribute to the global expansion of investment flows through investment rules that are clear, predictable, consistent and fair. Some existing implementation and interpretation arrangements are already contributing to the latter. But more institutional efforts might still be needed in that direction. In sum, EIAs are not a substitute for the lack of a multilateral system in the area of investment — just as they are not a substitute for the multilateral trading system established by the WTO — but, in the absence of

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such a system, policymakers need to ensure that the expansion of EIAs is supported by institutional mechanisms that contribute to the elaboration of a clear, predictable, consistent and fair framework of international investment rules for the benefit of all countries.

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## Annex Table. Economic Integration Investment Agreements 1945-2005

No.	Agreement	Year	Geographical scope
1	Treaty Establishing the European community (Treaty of Rome), amended by the Single European Act, the Treaty on European Union, the Treaty of Nice and the European Constitution	1957/1986/1992/ 2001/2004	Regional (1 group)
2	Agreement on Arab Economic Unity (League of Arab States)	1957	Interregional (1 group)
3	Central American Multilateral Agreement on Free Trade and Economic Integration; Treaty on Economic Association between Guatemala, El Salvador, Honduras and Nicaragua; General Treaty on Central American Economic Integration	(1958) 1960/1960	Regional (1 group)
4	Code of Liberalization of Capital Movements (OECD) <sup>1</sup>	1961	Interregional (1 group)
5	Common Convention on Investments in the States of the Customs and Economic Union of Central Africa (UDEAC or CEMAC)	1964	Regional (1 group)
6	Agreement on Andean Sub-regional Integration (Cartagena Agreement)	1969	Regional (1 group)
7	Agreement on Investment and Free Movement of Arab Capital among Arab Countries (League of Arab States)	1970	Interregional (1 group)
8	Joint Convention on the Freedom of Movement of Persons and the Right of Establishment in the Central African Customs and Economic Union (UDEAC)	1972	Regional (1 group)
9	Treaty Establishing the Economic Community of West African States; Protocol A/P1/5/79 on Free Movement of Persons, Right of Residence and Establishment; Protocol A/P1/11/84 Relating to Community Enterprises (ECOWAS)	1975/1979/1984	Regional (1 group)
10	Treaty Establishing the Caribbean Community (Treaty of Chaguaramas)	1973/1997/2001	Regional (1 group)
11	Declaration on International Investment and Multinational Enterprises (OECD)	1976/1991/2000	Interregional (1 group)
12	Cooperation Agreement between the European Community and Its Member States and the Member Countries of ASEAN	1980	Interregional (2 groups)
13	Unified Agreement for the Investment of Arab Capital in the Arab States (League of Arab States)	1980	Interregional (1 group)
14	Treaty Establishing the Latin American Association (ALADI or LAIA)	1980	Regional (1 group)
15	South Pacific Regional Trade and Economic Cooperation Agreement (SPARTECA)	1981	Regional (1 group)
16	Agreement on Promotion, Protection and Guarantee of Investments amongst the Member States of the Organization of the Islamic Conference	1981	Interregional (1 group)
17	Treaty for the Establishment of the Preferential Trade Area for Eastern and Southern African States; Charter on a Regime of Multinational Industrial Enterprises (MIEs) in the Preferential Trade Area for Eastern and Southern African States	1981/1990	Regional (1 group)
18	Unified Economic Agreement between the Countries of the Gulf Cooperation Council (GCC)	1981	Regional (1 group)
19	Community Investment Code of the Economic Community of the Great Lakes Countries (CEPGL)	1982	Regional (1 group)
20	Treaty for the Establishment of the Economic Community of Central African States (ECCAS)	1983	Regional (1 group)
21	Basic Agreement on ASEAN Industrial Joint Ventures and Revised Agreement	1983/1987	Regional (1 group)
22	Agreement on the Establishment of a Free Trade Area between the Government of Israel and the Government of the United States of America	1985	Interregional (bilateral)
23	Trade and Cooperation Agreement between the European Community and Its Member States and China	(1978) 1985	Interregional (1 group + 1 country)
24	Agreement for the Establishment of a Regime for CARICOM Enterprises	1987	Regional (1 group)
25	Free Trade Agreement between Canada and the United States of America	1988	Regional (bilateral)
26	ASEAN Agreement for the Promotion and Protection of Investments, amended by the 1996 Protocol	1987/1996	Regional (1 group)
27	Cooperation Agreement between the European Community and Its Member States and the States of the Gulf	1988	Interregional (2 groups)
28	Revised Convention Establishing the European Free Trade Association (EFTA)	1991/2001	Regional (1 group)
29	Decision 291 of the Commission of the Cartagena Agreement: Common Code for the Treatment of Foreign Capital and on Trademarks, Patents, Licenses and Royalties (Andean Community)	1991	Regional (1 group)
30	Decision 292 of the Commission of the Cartagena Agreement: Uniform Code on Andean Multinational Enterprises (Andean Community)	1991	Regional (1 group)
31	Treaty Establishing the African Economic Community/African Union	1991/2001	Regional (1 group)
32	Agreement on Trade and Commercial Relations between the Government of Australia and the Government of Papua New Guinea	(1976) 1991	Regional (bilateral)
33	Framework Agreement for Cooperation between the European Community and the Eastern Republic of Uruguay	1991	Interregional (1 group + 1 country)

No.	Agreement	Year	Geographical scope
34	Framework Agreement for Cooperation between the European Community and Its Member States and Paraguay	1992	Interregional (1 group + 1 country)
35	Framework Agreement between the European Economic Community and the Republic of Albania on Trade and Commercial and Economic Cooperation	1992	Regional (1 group + 1 country)
36	Agreement on Trade and Economic Cooperation between the European Economic Community and Its Member States and Mongolia	1992	Interregional (1 group + 1 country)
37	Agreement Establishing the European Economic Area (EC-EFTA)	1992	Regional (2 groups)
38	North American Free Trade Agreement (NAFTA)	1992	Regional (1 group)
39	Framework Agreement for Cooperation between the European Community and it is Member States and Brazil	1992	Interregional (1 group + 1 country)
40	Free Trade Agreement between the EFTA States and Israel	1992	Interregional (1 group + 1 country)
41	Free Trade Agreement between the EFTA States and Romania	1992	Regional (1 group + 1 country)
42	Agreement for Trade and Co-operation between the European Economic Community and Macao	1992	Interregional (1 group + 1 economy)
43	Agreement between the Caribbean Community (CARICOM) and Venezuela on Trade and Investment	1992	Interregional (1 group + 1 country)
44	Treaty Establishing the Southern African Development Community (SADC)	1992	Regional (1 group)
45	Treaty Establishing the Common Market for Eastern and Southern Africa (COMESA)	1993	Regional (1 group)
46	Revised Treaty of the Economic Community of West African States and Energy Protocol (ECOWAS)	1993/2003	Regional (1 group)
47	Free Trade Agreement between the Republic of Chile and the Republic of Venezuela	1993	Regional (bilateral)
48	Economic Complementarity Agreement N.22 between the Government of the Republic of Bolivia and the Government of the Republic of Chile	1993	Regional (bilateral)
49	Cooperation Agreement between the European Community and the Republic of India on Partnership and Development	(1981) 1993	Interregional (1 group + 1 country)
50	Europe Agreement Establishing an Association between the European Communities and Their Member States, of the One Part, and the Republic of Bulgaria, of the Other Part	1993	Regional (1 group + 1 country)
51	Europe Agreement Establishing an Association between the European Economic Communities and Their Member States, of the One Part, and Romania, of the Other Part	1993	Regional (1 group + 1 country)
52	Protocol of Colonia for the Promotion and Reciprocal Protection of Investments within MERCOSUR	1994	Regional (1 group)
53	Protocol on Promotion and Protection of Investments coming from Non-members of MERCOSUR	1994	Regional (1 group)
54	Free Trade Agreement between the Republic of Colombia, the Republic of Venezuela and the United Mexican States	1994	Regional (1 group)
55	APEC Non-Binding Investment Principles <sup>1</sup>	1994	Interregional (1 group)
56	Agreement between Canada and Ukraine on Economic Cooperation	1994	Interregional (bilateral)
57	Free Trade Agreement between the Republic of Costa Rica and the United Mexican States	1994	Regional (bilateral)
58	Treaty Establishing the West African Economic and Monetary Union (WAEMU or UEMOA)	1994	Regional (bilateral)
59	Free Trade Agreement between the Republic of Bolivia and the United Mexican States	1994	Regional (bilateral)
60	Economic Complementarity Agreement N.24 between the Republic of Chile and the Republic of Colombia	1994	Regional (bilateral)
61	Free Trade Agreement between the Republic of Chile and the Republic of Ecuador	1994	Regional (bilateral)
62	Cooperation Agreement between the European Community and Its Member States and the Democratic Socialist Republic of Sri Lanka on Partnership and Development	(1975) 1994	Interregional (1 group + 1 country)
63	Agreement on Partnership and Cooperation Establishing a Partnership between the European Communities and Their Member States, of One Part, and the Russian Federation, of the Other Part	(1989) <sup>2</sup> 1994	Regional (1 group + 1 country)
64	Partnership and Cooperation Agreement between the European Communities and Their Member States and Ukraine	1994	Regional (1 group + 1 country)
65	The Energy Charter Treaty	1994	Interregional (1 group)
66	Cooperation Agreement Establishing a Partnership between the European Communities and Their Member States, of the One Part, and the Republic of	1994	Regional (1 group + 1 country)

No.	Agreement	Year	Geographical scope
	Moldova, of the Other Part		
67	ASEAN Framework Agreement on Services	1995	Regional (1 group)
68	Interregional Framework Cooperation Agreement between the European Community and Its Member States, of the One Part, and the Southern Common Market (MERCOSUR) and Its Member States, of the Other Part	1995	Interregional (2 groups)
69	Euro-Mediterranean Agreement Establishing an Association between the European Communities and Their Member States, of the One Part, and the Republic of Tunisia, of the Other Part	(1976) 1995	Interregional (1 group + 1 country)
70	Euro-Mediterranean Agreement Establishing an Association between the European Communities and Their Member States, of the One Part, and the State of Israel, of the Other Part	(1975) 1995	Interregional (1 group + 1 country)
71	Partnership and Cooperation Agreement between the European Communities and Their Member States and the Republic of Kazakhstan, of the Other Part	1995	Regional (1 group + 1 country)
72	Partnership and Cooperation Agreement Establishing a Partnership between the European Communities and Their Member States, of the One Part, and the Kyrgyz Republic, of the Other Part	1995	Regional (1 group + 1 country)
73	Partnership and Cooperation Agreement Establishing a Partnership between the European Communities and Their Member States, of the One Part, and Belarus, of the Other Part	1995	Regional (1 group + 1 country)
74	Trade and Economic Cooperation Arrangement between the Government of Canada and the Government of Australia	1995	Interregional (bilateral)
75	Partnership and Cooperation Agreement Establishing a Partnership between the European Communities and Their Member States, of the One Part, and Nepal, of the Other Part	1995	Interregional (1 group + 1 country)
76	Free Trade Agreement between the European Economic Community and Turkey	1963/1995	Regional (1 group + 1 country)
77	Cooperation Agreement between the European Community and Vietnam	1995	Interregional (1 group + 1 country)
78	Economic Complementation Agreement N. 36 Establishing a Free Trade Area between the Governments of the States Parties of MERCOSUR and the Government of the Republic of Bolivia	1996	Regional (1 group + 1 country)
79	Free Trade Agreement between Canada and the Republic of Chile	1996	Regional (bilateral)
80	ASEAN Protocol on Enhanced Dispute Settlement Mechanism	1996	Regional (1 group)
81	Euro-Mediterranean Agreement Establishing an Association between the European Communities and Their Member States, of the One Part, and the Kingdom of Morocco, of the Other Part	(1976) 1996	Interregional (1 group + 1 country)
82	Framework Agreement for Trade and Cooperation between the European Community and Its Member States, on the One Hand, and the Republic of Korea, on the Other Hand	1996	Interregional (1 group + 1 country)
83	Partnership and Cooperation Agreement between the European Communities and Their Member States, of the One Part, and the Republic of Armenia, of the Other Part	1996	Regional (1 group + 1 country)
84	Partnership and Cooperation Agreement between the European Community and Their Members States, of the One Part, and the Republic of Azerbaijan, of the Other Part	1996	Regional (1 group + 1 country)
85	Partnership and Cooperation Agreement Establishing a Partnership between the European Communities and Their Member States, of the One Part, and the Republic of Uzbekistan, of the Other Part	1996	Regional (1 group + 1 country)
86	Partnership and Cooperation Agreement Establishing a Partnership between the European Communities and Their Member States, of the One Part, and Georgia, of the Other Part	1996	Regional (1 group + 1 country)
87	Economic Complementation Agreement N. 35 between MERCOSUR and the Republic of Chile	1996	Regional (1 group + 1 country)
88	Protocol of Montevideo on Trade in Services in the Southern Common Market (MERCOSUR)	1997	Regional (1 group)
89	Free Trade Agreement between the United Mexican States and the Republic of Nicaragua	1997	Regional (bilateral)
90	Arrangement on Trade and Economic Cooperation between the Government of Canada and the Government of the Kingdom of Norway	1997	Interregional (bilateral)
91	Free Trade Agreement between the Republic of Romania and the Republic of Turkey	1997	Interregional (bilateral)

No.	Agreement	Year	Geographical scope
92	Euro- Mediterranean Interim Association Agreement on Trade and Cooperation between the European Community, of the One Part, and the Palestine Liberation Organization (PLO) for the Benefit of the Palestinian Authority of the West Bank and the Gaza Strip, of the Other Hand	1997	Interregional (1 group + 1 country)
93	Cooperation Agreement between the European Community and the Republic of Yemen	1997	Interregional (1 group + 1 country)
94	Cooperation Agreement between the European Community and the Lao People's Democratic Republic	1997	Interregional (1 group + 1 country)
95	Cooperation Agreement between the European Community and the Kingdom of Cambodia	1997	Interregional (1 group + 1 country)
96	Revised Treaty of Chaguaramas Establishing the CARICOM Single Market and Economy	1997/2001	Regional (1 group)
97	Free Trade Agreement between the European Free Trade Association (EFTA) and the Kingdom of Morocco	1997	Interregional (1 group + 1 country)
98	Free Trade Agreement between the Republic of Turkey and the Republic of Bulgaria	1998	Regional (bilateral)
99	Andean Community, Decision 439: General Framework of Principles and Rules for Liberalizing Trade in Services in the Andean Community	1998	Regional (1 group)
100	Memorandum of Understanding on Trade and Investment between the Government of Canada and the Governments of Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua	1998	Interregional (1 group + 1 country)
101	Framework Agreement on the ASEAN Investment Area (ASEAN)	1998	Regional (1 group)
102	Arrangement on Trade and Economic Cooperation between the Government of Canada and the Government of the Swiss Confederation	1998	Interregional (bilateral)
103	Framework Agreement for the Creation of a Free Trade Area between the Andean Community and MERCOSUR	1998	Regional (2 groups)
104	Free Trade Agreement between Central America and the Dominican Republic	1998	Regional (bilateral)
105	Free Trade Agreement between the Republic of Chile and the United Mexican States	1998	Regional (bilateral)
106	Free Trade Agreement between the United Mexican States and the Republic of Nicaragua	1998	Regional (bilateral)
107	Arrangement on Trade and Investment Cooperation between Canada and Republic of South Africa	1998	Interregional (bilateral)
108	Arrangement on Trade and Economic Cooperation between the Government of Canada and the Government of the Republic of Iceland	1998	Interregional (bilateral)
109	Economic Complementarity Agreement N.38 between the Republic of Chile and the Republic of Peru for the Establishment of a Free Trade Area	1998	Regional (bilateral)
110	Partnership and Cooperation Agreement between the European Community and Its Member States, of the One Part, and Turkmenistan, of the Other Part	1998	Regional (1 group + 1 country)
111	Interim Agreement between the European Free Trade Association (EFTA) States and the Palestine Liberation Organization (PLO) for the Benefit of the Palestinian Authority	1998	Interregional (1 group + 1 country)
112	Trade and Investment Cooperation Arrangement and Action Plan between Canada and the MERCOSUR	1998	Regional (1 group + 1 country)
113	Agreement Establishing a Free Trade Area between the Caribbean Community (CARICOM) and the Dominican Republic	1998	Regional (1 group + 1 country)
114	Treaty for the Establishment of the East African Community (EAC)	1999	Regional (1 group)
115	Free Trade Agreement between the Governments of the Central American States and the Government of the Republic of Chile	1999	Regional (bilateral)
116	Agreement between the Government of the Republic of Turkey and the Government of the United States of America Concerning the Development of Trade and Investment Relations	1999	Interregional (bilateral)
117	Free Trade Agreement between Turkey and the Former Yugoslav Republic of Macedonia	1999	Regional (bilateral)
118	Agreement between the Government of the Arab Republic of Egypt and the United States of America Concerning the Development of Trade and Investment Relations	1999	Interregional (bilateral)
119	Agreement between the Government of the Republic of Ghana and the United States of America Government of the Concerning the Development of Trade and Investment Relations	1999	Interregional (bilateral)
120	Agreement Concerning the Development of Trade and Investment Relations between the Government of the Republic of South Africa and the Government of the United States of America	1999	Interregional (bilateral)

No.	Agreement	Year	Geographical scope
121	Agreement between Australia and Fiji on Trade and Economic Cooperation	1999	Regional (bilateral)
122	Agreement on Trade, Development and Cooperation between the European Community and Its Member States, of the One Part, and the Republic of South Africa, of the Other Part	(1994) 1999	Interregional (1 group + 1 country)
123	Trade and Investment Cooperation Arrangement between the Government of Canada and the Governments of the Andean Community	1999	Regional (1 group + 1 country)
124	Free Trade Agreement between the United Mexican States and the Republics of El Salvador, Guatemala and Honduras	2000	Regional (1 group)
125	Partnership Agreement between the Members of the African, Caribbean and Pacific Group of States of the One Part, and the European Community and Its Member States, of the Other Part (Cotonou Agreement)	(1989) 2000	Interregional (2 groups)
126	Agreement between the United States of America and the Socialist Republic of Vietnam on Trade and Investment Relations	2000	Interregional (bilateral)
127	Agreement between New Zealand and Singapore on Closer Economic Partnership	2000	Regional (bilateral)
128	Agreement between the Government of the United States of America and the Government of the Federal Republic of Nigeria Concerning the Development of Trade and Investment Relations	2000	Interregional (bilateral)
129	Partnership, Political Coordination and Cooperation Economic Agreement between the European Community and Its Member States, of the One Part, and the United Mexican States, of the Other Part; Decision N.2/2001 Implementing the Agreement	(1991) 2000/2001	Interregional (1 group + 1 country)
130	Agreement between the United States of America and the Hashemite Kingdom of Jordan on the Establishment of a Free Trade Area	2000	Interregional (bilateral)
131	Free Trade Agreement between the EFTA States and the Republic of Macedonia	2000	Regional (1 group + 1 country)
132	Free Trade Agreement between the EFTA States and the United Mexican States	2000	Interregional (1 group + 1 country)
133	Trade and Economic Cooperation Agreement between CARICOM and Cuba	2000	Regional (1 group + 1 country)
134	Free Trade Agreement between the Republic of Croatia and Bosnia Herzegovina	2000	Regional (bilateral)
135	Free Trade Agreement between the Government of Canada and the Government of the Republic of Costa Rica	2001	Regional (bilateral)
136	Agreement between the Government of the United States of America and the Government of the People's Democratic Republic of Algeria Concerning the Development of Trade and Investment Relations	2001	Interregional (bilateral)
137	Stabilization and Association Agreement between the European Communities and Their Member States, of the One Part, and the Republic of the Republic of Croatia, of the Other Part	2001	Regional (1 group + 1 country)
138	Stabilization and Association Agreement between the European Community, of the One Part, and the Former Yugoslav Republic of Macedonia, of the Other Part	2001	Regional (1 group + 1 country)
139	Euro-Mediterranean Agreement Establishing an Association between the European Communities and Their Member States, of the One Part, and the Arab Republic of Egypt, of the Other Part	(1977) 2001	Interregional (1 group + 1 country)
140	Free Trade Agreement between the EFTA States and the Hashemite Kingdom of Jordan	2001	Interregional (1 group + 1 country)
141	Free Trade Agreement between the EFTA States and the Republic of Croatia	2001	Regional (1 group + 1 country)
142	Free Trade Agreement between the European Community and the Overseas Countries and Territories (OCT)	2001	Interregional (2 groups)
143	Agreement between the Common Market For Eastern And Southern Africa (COMESA) and the United States of America Concerning the Development of Trade and Investment Relations	2001	Regional (1 group + 1 country)
144	Agreement on Trade in Services and Investment between Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua.	2002	Regional (1 group)
145	Free Trade Agreement between the Republic of Albania and the Republic of Croatia	2002	Regional (bilateral)
146	Free Trade Agreement between Central America and Panama	2002	Regional (1 group + 1 country)
147	Agreement between Japan and the Republic of Singapore for a New-Age Economic Partnership	2002	Regional (bilateral)
148	Agreement between the Government of the United States of America and the Kingdom of Bahrain Concerning the Development of Trade and Investment Relations	2002	Interregional (bilateral)
149	Trade and Investment Framework Agreement between the Government of the United States of America and the Government of Brunei Darussalam	2002	Interregional (bilateral)
150	Trade and Investment Framework Agreement between the United States of America and the Democratic Socialist Republic of Sri Lanka	2002	Interregional (bilateral)



No.	Agreement	Year	Geographical scope
151	Euro-Mediterranean Agreement Establishing an Association between the European Communities and Their Member States, of the One Part, and Algeria, of the Other Part	(1976) 2002	Interregional (1 group + 1 country)
152	Euro-Mediterranean Interim Association Agreement between the European Community and Its Members, of the One Part, and the Republic of Lebanon, of the Other Part	(1977) 2002	Interregional (1 group + 1 country)
153	Agreement Establishing an Association between the European Community and the Republic of Chile	2002	Interregional (1 group + 1 country)
154	Euro-Mediterranean agreement between the European Communities and Kingdom of Jordan	(1977) 2002	Interregional (1 group + 1 country)
155	Free Trade Agreement between the Republic of Albania and the Republic of Macedonia	2002	Regional (bilateral)
156	Free Trade Agreement between the Republic of Albania and the Republic of Bosnia Herzegovina	2002	Regional (bilateral)
157	Free Trade Agreement between the EFTA States and Singapore	2002	Interregional (1 group + 1 country)
158	Agreement Between the Government of the United States of America and the West African Economic and Monetary Union (WAEMU) Concerning the Development of Trade and Investment Relations	2002	Interregional (1 group + 1 country)
159	Framework Agreement between ASEAN and China	2002	Regional (1 group + 1 country)
160	Economic Complementation Agreement N.54 and N.55 between MERCOSUR and the United Mexican States	2002	Regional (1 group + 1 country)
161	Political Dialogue and Co-operation Agreement between the European Community and its Member States, of the one part, and the Andean Community and its Member States, Bolivia, Colombia, Ecuador, Peru and Venezuela, of the Other Part	(1993) (1996) 2003	Interregional (2 groups)
162	Free Trade Agreement Between the Government of Chile and the Government of the United States of America	2003	Interregional (bilateral)
163	Free Trade Agreement between the Republic of Korea and the Republic of Chile	2003	Interregional (bilateral)
164	Free Trade Agreement between the Republic of Albania and the Republic of Bulgaria	2003	Regional (bilateral)
165	Free Trade Agreement between the Republic of Bulgaria and the Republic of Serbia Montenegro	2003	Regional (bilateral)
166	Free Trade Agreement between the Republic of Croatia and the Republic of Turkey	2003	Interregional (bilateral)
167	Agreement on Trade Relations between the Lao Peoples' Democratic Republic and the United States of America	2003	Interregional (bilateral)
168	Free Trade Agreement between Singapore and the United States of America	2003	Interregional (bilateral)
169	Framework Agreement for Establishing a Free Trade Area between the Republic of India and the Republic of Thailand	2003	Regional (bilateral)
170	Free Trade Agreement between Australia and Singapore	2003	Regional (bilateral)
171	Trade and Economic Framework Agreement between Australia and Japan	2003	Regional (bilateral)
172	Agreement on Closer Economic Partnership Arrangement between Mainland China and Hong Kong	2003	Regional (bilateral)
173	Free Trade Agreement between Panama and Taiwan, Province of China	2003	Interregional (bilateral)
174	Agreement on Closer Economic Partnership Arrangement between Mainland China and Macao	2003	Regional (bilateral)
175	Economic Complementation Agreement N. 58 between MERCOSUR and the Republic of Peru	2003	Regional (1 group + 1 country)
176	Trade and Economic Framework Agreement between Australia and China	2003	Regional (bilateral)
177	Agreement Between the Government of the Government of the United States of America and the Government of the Kingdom of Saudi Arabia Concerning the Development of Trade and Investment Relations	2003	Interregional (bilateral)
178	Political Dialogue and Cooperation Agreement between the European Community and its Member States and the Republics of Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama	(1993) 2003	Interregional (2 groups)
179	Free Trade Agreement between the EFTA States and the Republic of Chile	2003	Interregional (1 group + 1 country)
180	Economic Complementation Agreements N.56 and N.59 between the Governments of the Republic of Argentina, the Federal Republic of Brazil, the Republic of Paraguay and the Eastern Republic of Uruguay, States Parties of MERCOSUR and the Governments of the Republic of Colombia, the Republic of Ecuador and the Bolivarian Republic of Venezuela, Countries Members of the Andean Community	2002/2003	Regional (2 groups)
181	Framework Agreement between ASEAN and the Republic of India	2003	Regional (1 group + 1 country)
182	Framework Agreement for Comprehensive Economic Partnership between Japan and ASEAN	2003	Regional (1 group + 1 country)

No.	Agreement	Year	Geographical scope
183	Framework Agreement between the Republic of India and MERCOSUR	2003	Interregional (1 group + 1 country)
184	Framework Agreement on the BIMST-EC Free Trade Area	2004	Regional (1 group)
185	Free Trade Agreement between the EFTA States and the Republic of Tunisia	2004	Interregional (1 group + 1 country)
186	Free Trade Agreement between the Government of the United Mexican States and the Republic of Uruguay	2004	Regional (bilateral)
187	Framework Agreement on the South Asia Free Trade Area (SAARC)	2004	Regional (1 group)
188	Free Trade Agreement between the Kingdom of Morocco and the United States of America	2004	Interregional (bilateral)
189	Free Trade Agreement between Australia and Thailand	2004	Regional (bilateral)
190	Free Trade Agreement between Australia and the United States of America	2004	Interregional (bilateral)
191	Agreement Concerning the Development of Trade and Investment Relations between the Government of the United States of America and the Government of the State of Qatar	2004	Interregional (bilateral)
192	Agreement Concerning the Development of Trade and Investment Relations between the Government of the United States of America and the Government of the United Arab Emirates	2004	Interregional (bilateral)
193	Agreement Concerning the Development of Trade and Investment Relations between Mongolia and the United States of America	2004	Interregional (bilateral)
194	Agreement Concerning the Development of Trade and Investment Relations between the Government of the United States of America and the Government of the State of Kuwait	2004	Interregional (bilateral)
195	Agreement Concerning the Development of Trade and Investment Relations between Malaysia and the United States of America	2004	Interregional (bilateral)
196	Agreement Concerning the Development of Trade and Investment Relations between the Government of the United States of America and Government of the Republic of Yemen	2004	Interregional (bilateral)
197	Free Trade Agreement between the Kingdom of Bahrain and the United States of America	2004	Interregional (bilateral)
198	Free Trade Agreement between the Republic of Albania and the Republic of Romania	2004	Regional (bilateral)
199	Free Trade Agreement between the Republic of Albania and the Republic of Serbia and Montenegro	2004	Regional (bilateral)
200	Free Trade Agreement between the Hashemite Kingdom Jordan and the Republic of Singapore	2004	Interregional (bilateral)
201	Cooperation Agreement between the European Community and Pakistan	(1985) 2004	Interregional (1 group + 1 country)
202	Free Trade Agreement between the EFTA States and Lebanon	2004	Interregional (1 group + 1 country)
203	Free Trade Agreement between the Republic of Bosnia Herzegovina and the Republic of Moldova	2004	Regional (bilateral)
204	Free Trade Agreement between the Republic of Bosnia Herzegovina and the Republic of Romania	2004	Regional (bilateral)
205	Free Trade Agreement between Central America, the Dominican Republic and the United States of America (CAFTA)	2004	Regional (1 group + 2 country)
206	Partial Reach Agreement for Economic, Trade and Investment Promotion between the Republic of Argentina and the Republic of Bolivia	2004	Regional (bilateral)
207	Economic Complementation General Agreement on Integration, Economic and Social Cooperation for the Establishment of a Common Market between the Republic of Bolivia and the Republic of Peru	2004	Regional (bilateral)
208	Framework Agreement Between the Government of the United States of America, the Government of the Republic of Kazakhstan, The Government of the Kyrgyz Republic, the Government of the Republic of Tajikistan, the Government of Turkmenistan, and the Government of the Republic of Uzbekistan Concerning the Development of Trade and Investment Relations	2004	Interregional (1 group + 1 country)
209	Free Trade Agreement between the Caribbean Community (CARICOM) and Costa Rica	2004	Regional (1 group + 1 country)
210	Interim Free Trade Agreement between the Republic of Turkey and the Palestinian Authority	2004	Regional (bilateral)
211	Framework Agreement between MERCOSUR and the Arab Republic of Egypt	2004	Interregional (1 group + 1 country)
212	Trade and Investment Framework Agreement between Afghanistan and the United States	2004	Interregional (bilateral)
213	Framework Agreement on Economic Cooperation Agreement between the Gulf Cooperation Council (GCC) and India	2004	Regional (1 group + 1 country)

No.	Agreement	Year	Geographical scope
214	Agreement for the Establishment of a Free Trade Area between the Gulf Cooperation Council and Lebanon	2004	Regional (1 group + 1 country)
215	Agreement between Japan and the United Mexican States for the Strengthening of Economic Partnership	2004	Interregional (bilateral)
216	Comprehensive Economic Cooperation Agreement between the Republic of India and the Republic of Chile	2005	Interregional (bilateral)
217	Comprehensive Economic Cooperation Agreement between India and Singapore	2005	Regional (bilateral)
218	Agreement on Closer Economic Partnership between New Zealand and Thailand	2005	Regional (bilateral)

Source: UNCTAD.

Notes:

Regional EIAs means EIAs signed by countries located in the same geographical region.

Interregional EIAs means EIAs signed by countries at least one of which is located in a different geographical region.

Bilateral EIAs means EIAs signed between two countries whether they are situated in the same geographical region or in different geographical regions.

Excluded from this list are EIAs that have been terminated as a result of the relevant countries' accession to the European Union. Also EIAs that have been superseded by new EIAs are not included.

A year in brackets means the parties signed a treaty that year which was superseded by a more recent treaty.

<sup>1</sup> Agreement is part of a broader economic cooperation framework that falls short of an 'economic integration framework'.

<sup>2</sup> Agreement signed between the European Community and the USSR.

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Division on Investment, Technology and Enterprise Development  
Palais des Nations, Room E-10054  
CH-1211 Geneva 10, Switzerland  
Telephone: (41-22) 907-5651  
Telefax: (41-22) 907-0498  
E-mail: [natalia.guerra@unctad.org](mailto:natalia.guerra@unctad.org)  
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