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APEC Workshop on Non-Discrimination Treatment in Investment Agreements

Program

September 1, 2006

Opening Ceremony (09:00-09:30)

Session 1 (09:30-10:30)
General introduction of Non-discrimination Treatment in investment agreement
Moderator: Dr. Deunden Nikomborirak (Thailand)
- Speaker: Mr. Joachim Karl (UNCTAD)

Q&A

Tea break (10:30-11:00)

Session 2 (11:00-12:00)
Part1: MFN: introduction of key issues and implication
- Moderator: Dr. TEJIMA Shigeki (Japan)
- Speaker: Mr. Roberto Echandi (UNCTAD)

Lunch break (12:00-13:30)

Session 2 (13:30-17:00) (Continued)
Part2 (13:30-14:30)
MFN: common and different approach adopted in international agreement
- Moderator: Mr. Anthony Hinton (Australia)
- Speaker: Mr. Roberto Echandi (UNCTAD)

Tea break (14:30-15:00)

Part3 (15:00-16:00)
MFN: the economic and development implications and policy options of those different elements.
- Moderator: Mr. Anthony Hinton (Australia)
- Speaker: Dr. Deunden Nikomborirak (Thailand)
Panel Discussion (16:00-17:00)  
Moderator: Ms. Li Yihong

18:00-19:30  
Welcome dinner hosted by the Ministry of Commerce

September 2, 2006

Session 3 (09:30-17:00)  
Part 1 (09:30-10:30)  
National Treatment: introduction of key issues and implication  
- Moderator: Mr. Joachim Karl (UNCTAD)  
- Speaker: Mr. Anthony Hinton (Australia)

Tea break (10:30-11:00)

Part 2 (11:00-12:00)  
National Treatment: common and different approach adopted in international agreement  
- Moderator: Ms. Rebecca Fatima Sta Maria (Malaysia)  
- Speaker: Mr. Roberto Echandi (UNCTAD)

Lunch break (12:00-13:30)

Part 3 (13:30-15:30)  
National Treatment: the economic and development implications and policy options of those different elements.  
- Moderator: Mr. Roberto Echandi (UNCTAD)  
- Speakers: Dr. TEJIMA Shigeki (Japan)  
Ms. Rebecca Fatima Sta Maria (Malaysia)

Tea break (15:30-16:00)

Panel Discussion (16:00-17:00)  
Moderator: Mr. Joachim Karl (UNCTAD)
September 3, 2006

**Session 4 (09:00-10:00)**
Fair and Equitable treatment: introduction of key issues and implication
- Moderator: Ms. Rebecca Fatima Sta Maria (Malaysia)
- Speaker: Mr. Joachim Karl (UNCTAD)

Tea break (10:00-10:30)

**Session 5 (10:30-12:00)**
Negotiation skills and lessons from member economies
Moderator: Ms. Li Yihong
1) Case study from Mexico
2) Case study from Malaysia
3) Case study from China

Q&A

**Session 6 (12:30)**
Conclusion
Non-Discrimination Treatment in IIAs

Joachim Karl

Overview of Presentation

- Non-discrimination and investment protection;
- Non-discrimination and development policies;
- Non-discrimination and the growing IIA universe – The issue of policy coherence.
- Implications.

I. Non-discrimination and investment protection
Non-discrimination and investment protection

- ND is a key element of investment protection;
- Serves to establish a level playing field in the host country between investors irrespective of their nationality;
- Is an important means to establish investor confidence and to increase the attractiveness of host countries in the global competition for FDI;
- Enhances the effective functioning of an increasingly integrated world economy.

The double-effect of IIAs
Reduction of restrictions and improvement of protection

<table>
<thead>
<tr>
<th>Restrictions</th>
<th>Standards of treatment &amp; protection</th>
</tr>
</thead>
<tbody>
<tr>
<td>Admission and establishment;</td>
<td>Transparency</td>
</tr>
<tr>
<td>Propriety and control;</td>
<td>Treatment:</td>
</tr>
<tr>
<td>operational restrictions;</td>
<td>(F&amp;ET, NT, MFN)</td>
</tr>
<tr>
<td>establishment and reporting - etc.</td>
<td>Expropriation &amp; compensation</td>
</tr>
</tbody>
</table>

Origins of the Non-Discrimination Standard

- ND standard was first recognized in trade relations (first traces in the Hanseatic League in the 12th/13th century);
- International copyright and patent conventions (e.g. Paris Convention 1883);
- US FCN Treaties from the 1950s;
- GATT/WTO: Ensure non-discrimination in respect of trade in goods/services.
Non-discrimination in IIAs

- Core element of all kinds of IIAs;
- Different approaches in IIAs concerning the nature, scope and content of the ND principle:
  - Legally binding or voluntary;
  - Different treaty provisions (NT, MFN, F&E treatment);
  - Pre-establishment phase covered?
  - Positive- or negative-list approach;
  - Degree of specificity of treaty language;
  - Exceptions and reservations.

Non-discrimination: Crucial questions

- Who can claim ND? Definition of «investor »;
- Who can be the object of a discrimination? Definition of « investment » and « investor »;
- What investment-related activities are covered by the ND principle? Scope of provision;
- When does the ND principle apply (issues of « like circumstances » and « de-jure/de-facto » discrimination)?
- What does ND mean in treaty terms (different ND-related provisions/ exceptions)?
- Reciprocity issue and « Free rider » issue.

II. Non-discrimination and development policies
Non-discrimination and development policies

- Depending on the specific policies that host countries pursue, the ND principle may promote or jeopardize development objectives (by reducing policy space);
- ND principle may reinforce «open door» policies;
- ND principle may interfere with the strategies of host countries to promote their domestic industries, and may prevent to bring about operative equality between «weak» domestic and «strong» foreign companies (economic asymmetry).
- **Challenge to find the right «policy» concerning scope of ND principle.**

Non-discrimination and development policies: Sensitive areas

- Promotion of infant industries;
- Protection of strategically important industries;
- Strengthening regional economic integration.

ND Principle and Development Policies

- Attract FDI
- Development Objectives
- Optimise the positive effects of FDI
- Minimise the potential negative effects of FDI
ND principle can contribute to maximising positive effects of FDI

- Long-term financial inflows;
- Transfer of competences in the area of technology and R&D;
- Transfer of know-how, management and marketing;
- Spillover effects to domestic enterprises;
- Access to foreign markets;
- Integration in TNC network;
- Social contributions.

Minimising potential negative effects of FDI

Likely Impact of the ND Principle

- Likely
  - "Crowding out" effect of FDI.
- Unlikely
  - Volatility of capital and balance-of-payments;
  - Anti-competitive behaviour and abuse of dominant position;
  - Transfer pricing;
  - Socio-cultural effects.

- FDI effects on labour and the environment?

ND Principle and Development Policies

Examples of different country strategies

- Passive "open door" policies (e.g. Hong Kong-China);
- Selective promotion of domestic enterprises; no intervention in export industries (e.g. Thailand, Malaysia);
- Active intervention to promote the participation of foreign subsidiaries in local manufacturing (e.g. Singapore);
- FDI restrictions in favour of "external" transfers of know how and capital (Korea, CP of Taiwan, Japan).
ND Principle and Development Policies: The Need for Flexibility

- Main Objective: Maintain sufficient flexibility for developing countries to implement their development policies in accordance with their specific circumstances and needs.
- ND Principle leaves considerable flexibility to host countries concerning their right to regulate;
- However, additional "safeguards" might be needed in specific policy areas (e.g. admission of FDI, intellectual property, taxation).

Means to ensure Flexibility in IIAs

- ND in Pre-/Post-Establishment Phase;
- Positive/negative list approach to non-discrimination;
- General exceptions and country-specific reservations;
- Additional treaty clarifications on ND;
- ND Safeguards in arbitration proceedings.

III. Non-discrimination and the increasing IIA universe – The issue of policy coherence
**ND and the increasing IIA universe**

- The growing IIA universe confirms the key role of the ND principle in international investment rulemaking.
- Despite its wide use, IIAs show important differences concerning the nature, scope and content of the ND principle.
- As a result, identifying existing differences and keeping the overall IIA network coherent becomes more of a challenge.
- Additional need to ensure coherence between IIAs and national (development) laws and policies.
- With more IIAs in place, the MFN principle gains in importance. At the same time, there are new uncertainties about the application of this standard.

**Potential Risks to Policy Coherence related to the ND Principle**

- Establishment rights for foreign investors – yes or no?
- Different modes of investment liberalization;
- Different substantive IIA provisions (e.g. definition of investment, expropriation, transfer of funds, performance requirements);
- Different kind and scope of exceptions/reservations;
- Different rules on dispute settlement;
- And: Unintended coherence as a result of MFN clause;
- In general: The more issues an IIA addresses, the greater the likelihood of overlaps and inconsistencies of the entire IIA network.

**Coherence between the ND principle and Development Policies**

- Increasing complexity of IIA patchwork might render it more difficult to maintain development policy coherence.
- Increasing complexity of IIAs may make it more difficult for foreign investors to assess degree of protection.
- But greater variation also presents an opportunity for adopting different approaches to better reflect the special needs of developing countries.
IV. Implications

The expected role of the ND principle in IIAs

- ND is a core element of a stable, predictable and transparent regulatory framework for FDI.
- The modalities of ND are likewise of key importance for the design and implementation of domestic development policies.

Implications for IIA negotiations

- The negotiation of the ND principle has increasingly far-reaching consequences as more and more countries, and more and more issues, are involved.
- The ND principle, by definition, limits the autonomy of the contracting parties; therefore, they have to assess whether this limitation affects their domestic policy objectives and – if yes – how to secure the required flexibility.
- This task may be a particular challenge for developing countries.
Thank you.
MFN Treatment in IIAs

Roberto Echandi

MFN TREATMENT IN IIAs

APEC Workshop, Xiamen, 1-3 September 2006

Roberto Echandi
Consultant
UNCTAD/DITE

MFN clauses in IIAs

Overview

- The MFN principle is a core standard in IIAs;
- IIAs differ in the nature and scope of the MFN principle and the MFN exceptions;
- No significant evolution of the MFN clause in treaty practice;
- More recently: Uncertainties about the interpretation of MFN clause in the light of diverging arbitration awards.

The Nature of the MFN Clause
## The Nature of the MFN Clause

<table>
<thead>
<tr>
<th>Legally binding</th>
<th>Non-legally binding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Is most common approach in IIAs. Examples: BITs, GATS, NAFTA, ECT.</td>
<td>Rarely used approach. Examples: APEC Non-Binding Investment Principles</td>
</tr>
</tbody>
</table>

### Non-legally binding (« best efforts »)

Rarely used approach.

Examples: APEC Non-Binding Investment Principles

## The Scope of the MFN Principle

### The Distinction between the Pre- and Post-establishment Phase

<table>
<thead>
<tr>
<th>MFN treatment in the pre- and post-establishment phase only;</th>
<th>MFN treatment in the post-establishment phase only;</th>
</tr>
</thead>
<tbody>
<tr>
<td>Examples: Majority of BITs, ECT, ASEAN Investment Agreement</td>
<td>Examples: US, Canadian, and recent Japanese BITs, most APEC FTAs with investment chapters</td>
</tr>
</tbody>
</table>
« Top-down » and « Bottom-up » MFN Treatment

« Top-down »: MFN treatment is granted unless there are exceptions or reservations.
Examples: BITs, NAFTA, ECT, GATS.

« Bottom-up »: MFN treatment is only granted if a specific individual commitment is made.
No example known.

Scope of MFN

A number of IIAs make the MFN principle subject to the domestic law of the host country (e.g. BIT between Saudi-Arabia and Malaysia).

Some IIAs include an explicit « standstill» clause (prohibition to introduce new non-MFN conforming measures). Example: BIT between China and Netherlands

Some IIAs apply the MFN horizontally in the post-establishment phase

Investment Activities covered by MFN

IIAs usually specify that MFN treatment applies with regard to all investment-related activities. Three main approaches:
- Enumeration of activities: e.g. (establishment), (acquisition), (expansion), management, operation, use, disposition, sale, liquidation;
- General: all investment-related activities (e.g. French model BIT).
- Open-ended: MFN treatment to “investment” (e.g. BIT between Mauritius and Singapore).
Other Issues

- A number of IIAs clarify that MFN treatment applies only « in like circumstances » (e.g. Art. 1103 NAFTA);
- Approach entails a comparative analysis
- What is the appropriate comparator?
- Whether difference in treatment is justified on a rational policy objective that is not based on a preference on the basis of nationality

MFN Treatment and Dispute Settlement

- Some contradictory arbitration awards have created uncertainty of whether the MFN clause extends to dispute settlement.
- Some IIAs explicitly clarify that MFN treatment extends to dispute settlement (e.g. BIT between Austria and Saudi-Arabia).
- Some IIAs provide that MFN only applies to establishment, acquisition, management, disposition, sale and liquidation of an investment.
- No IIA is known that explicitly excludes dispute settlement from the MFN clause.

Exceptions/Reservations to the MFN Principle
**Exceptions/Reservations to the MFN Principle**

IIAs contain – to various degrees – exceptions/reservations to the MFN clause.

Distinguish:
- General exceptions;
- Subject-specific exceptions;
- Country-specific reservations.

---

**General Exceptions**

General exceptions that might apply to the MFN principle include:
- Public order (e.g. BIT between Japan and Korea);
- Prudential measures (e.g. Canadian model BIT);
- Essential security interests (e.g. BIT between Australia and India);
- Protection of health and the environment (e.g. BIT between Armenia and Canada).

---

**Subject-specific MFN exceptions**

- Taxation (taxation treaties only or all taxation matters);
  - Examples: BIT between Argentina and New Zealand.
- Intellectual property;
  - Examples: US Model Agreement.
- Regional economic integration;
  - Examples: ECT.
- Mutual recognition;
  - Examples: Art. 1210.2 NAFTA; Art. VII GATS.
- Transportation agreements.
**Subject-specific MFN exceptions II**

Some IIAs (GATS, NAFTA) also include subject-specific exceptions in the following areas:
- Public procurement (Art. XIII GATS; Art. 1108.7 NAFTA);
- Subsidies (Art. 1108.7 NAFTA);

These exceptions only apply with regard to those sectors, activities or government measures that the country concerned has identified in a list.

**Country-specific MFN reservations**

- Contrary to MFN exceptions, IIAs allowing individual MFN reservations are less frequent (examples: GATS, NAFTA, US Model BIT).
- It gives CPs the freedom to exclude any economic sector or activity from the application of the MFN principle.
- Various options exist concerning the details: e.g. limitation in time, limitation to pre-establishment treatment, subsequent review, standstill commitment.

**Conclusions**
Conclusions

- The MFN principle is a standard clause in IIAs
- Scope of MFN principle varies significantly among the different IIAs
- Most frequently used exceptions relate to taxation and regional economic integration
- Recent ISDS jurisprudence has shown that the particular wording of MFN provisions does matter, and can lead to very different outcomes in the application of IIAs

Thank you.
MFN: Introduction and Key Issues
Roberto Echandi

MFN: Introduction and key issues

APEC Workshop, Xiamen, 1-3 September 2006

Roberto Echandi
Consultant
UNCTAD/DITE

MFN: content

Standard entails that investment or investors of a Contracting Party are entitled to a treatment by the other Contracting Parties which is no less favourable than the treatment the latter grants to investments or investors of any other third State.

MFN: Rationale and Effects

- Links IIAs by ensuring that each Contracting Party grants investments and/or investors the best treatment granted to any other investments/investors of any other country
- Impact in terms of harmonization of norms and disciplines
- Impact in terms of liberalization of investment (depending on scope of IIA)
- Levels the playing field in international negotiations
- Important for developing countries
**MFN: Rationale and Effects II**

- Countries tend to have several IIAs which differ in their contents
- With more than 5,000 IIAs, practical impact of MFN can be significant
- MFN can lead to obligations applying to different contexts than originally envisaged by the Contracting Parties
- Countries must fully understand impact of MFN when negotiating and implementing IIAs

**MFN: Main Issues**

- Issues that often arise in the context of negotiations of IIAs
- Issues that have arisen in the context of investor-State dispute settlement procedures

**MFN Issues: Negotiating IIAs**
MFN Issues: Scope of the Standard

- Only to established investment?
- Also in the pre-establishment phase?
- Obligation applies subject to domestic legislation?
- Standstill?
- Applies horizontally to all investment once admitted into the host country?
- Only to certain activities of the investment?
- To all investments and/or investors?

MFN Issues: Application in federal systems of government

- Some countries have different laws and regulations depending on provinces or states
- MFN obligation usually applies at all levels of government
- However, what happens if the sub-national government discriminates against investment/investors from other states or provinces of the same country?
- Which MFN standard applies?
- Best “in-State” treatment?
MFN Issues: Application of the standard

- Discrimination can be explicitly provided in a given measure
- Discrimination may not be evident, but an effect of the application of a given measure
- Standard usually applies against "de jure" and "de facto" discrimination

MFN Issues: « Like circumstances »

- Some IIAs provide that MFN standard applies only in “like circumstances”
- Approach entails a comparative analysis
- What is the appropriate comparator?
- ISDS practice suggests that difference in treatment is justified on a rational policy objective that is not based on a preference on the basis of nationality

MFN Issues: Exceptions/Reservations

- Need to distinguish between:
- General exceptions
- Subject-specific exceptions
- Country-specific reservations
**MFN Issues: recent ISDS practice**

**MFN Issues: Dispute Settlement**

- Does MFN applies to dispute settlement procedures?
- *Maffezini vs. Spain; Siemens vs. Argentina*
- Broad language used in MFN clause leads to apply MFN to ISDS procedures

**Limitations:**
- *Ejusdem generis* principle
- Public policy considerations as fundamental conditions for the acceptance of the agreement

---

**The *ejusdem generis* principle**

- MFN clause can only attract matters belonging to the same subject matter or the same category of subject as to which the clause relates
- Rights of beneficiary are limited to the subject matter in two ways:
  - The clause itself, which refers to a certain matter
  - By the rights conferred by the granting State on the third State
Public policy considerations as fundamental conditions for the acceptance of the agreement

Maffezini

"... As a matter of principle, the beneficiary of the clause should not be able to override public policy considerations that the Contracting Parties might have envisaged as fundamental conditions for their acceptance of the agreement in question, particularly if the beneficiary is a private investor…"

MFN Issues: Dispute Settlement

Salini vs. Jordan; Plama vs. Bulgaria

Cases where tribunals rejected to “import” other ISDS from other BITs

Salini:
- Situation is different from Maffezini
- BIT explicitly refers to domestic forum
- MFN clause does not apply to “all matters covered by the agreement”

Plama:
- Agreement to arbitrate must be clear and unambiguous, and cannot incorporated by reference to another IIA unless parties explicitly state otherwise
- How can it be determined which ISDS is more favourable?

Suez/AWG v. Argentina (August 2006) follows Maffezini and Siemens

MFN and Other Standards: ISDS Practice

MFN and Fair and Equitable Treatment Standard

MTD Equity Bhd v. Chile

Article 3.1 of the BIT between Chile and Malaysia:

“Investments made by investors of either Contracting Party in the territory of the other Contracting Party shall receive treatment which is fair and equitable, and not less favourable than that accorded to investments made by investors of any third State.”
MFN and Other Standards: ISDS Practice

- *MTD Equity Bhd v. Chile*
- Tribunal imports provisions from other BITs negotiated by Chile
- Fair and Equitable Treatment standard must be interpreted in the manner most conducive to fulfill objective of the BIT
- BIT has exceptions from MFN principle, and does not exclude Fair and Equitable Treatment Standard
- *A contrario sensu,* other matters that can be construed to be part of the fair and equitable treatment of investors would be covered by the clause

Conclusions

- Recent ISDS jurisprudence has shown that the particular wording of MFN provisions does matter, and can lead to very different outcomes in the application of IIAs
- MFN can be an useful intrument to level the playing field:
  - Externally, among countries with different bargaining power
  - Internally, leading to a single foreign investment policy
- Countries must clarify their policy towards MFN
- Risk of “treaty shopping”

Thank you.
MFN: The Economic and Development Implications and Policy Options

Deunden Nikomborirak

APEC Workshop on Non-Discrimination Treatment in Investment Agreements

1-3 September, 2006
Xiamen, China

MFN: the economic and development implications and policy options.

Deunden Nikomborirak
Thailand Development Research Institute

A. Pre-establishment Rights

1. The MFN Dilemma

- Economic versus Strategic
- Protectionist (infant industry/social factors) versus capitalist (investment hub)
2. Does MFN matter?

1. How broad is the definition of “investor of a Party”? How restrictive is the “denial of benefits” provision? (exporters’ view)
   - Place of incorporation (branch operation?)
   - Substantial business operation
   - owned/controlled by “investor of a Party”

2. How restrictive is the regime facing third-party investors? (importer’s view)

3. How binding is the regime on actual foreign investment?

4. How important is “first-mover advantage”?
   - Size of sunk investment
   - Availability of scarce resources (license/quota?)
   - Effectiveness of local Competition law and access regulation

---

**Composition of Banks in 5 ASEAN Countries**

Fink, Carsten and Nikomborirak, Deunden, Rule of Origin in Services in 5 ASEAN countries (forthcoming)
3. Policy Recommendations

- assess implications of different investment ROO on market competition (capital importers’ view) and market opportunities (K exporter's view)
- Select ROO most suitable for the country/sector

---

3. Policy Recommendations

- reduce investment barriers facing third-party investors (minimize the number of sectors where foreign equity share is limited) – or at least provide for greater flexibility to allow third-party access if need be.
3. Policy Recommendations

- put effort in building a pro-competition regulatory authority and competition authority

B. Post Establishment Protection

1. Is MFN investment protection desirable?

- What is the discrepancy between the level of protection afforded most favorably to an “investor of the other Party” and that of your own investor? (National Treatment)
- Are local institutions, personnel and administrative procedures supportive of an elevated foreign investor protection?
2. Recommendations

- It is best to unilaterally amend domestic rules and regulations that would support uniform protection on and MFN and NT basis to ensure level playing field across investors of all nationalities.
- Overhaul domestic regulatory regime and institutions to ensure a more transparent and predictable administration of rules and regulations.

THANK YOU
Key Issues for National Treatment Obligations in International Investment Agreements

Tony Hinton

National Treatment Issues

- Underlying objective of national treatment
- National treatment definition
- National treatment with qualifications
- Economic policy flexibility
- Pre-establishment and post-establishment

National Treatment Issues

- Powers of sub-national authorities
- Relationship with other general standards of treatment
- De jure and de facto treatment
- Dispute resolution
- Conclusion
Underpinning Objective of Non-Discrimination

- FDI engine of economic growth
  - Both developed and developing countries

- Many factors influence investment
  - Including a welcoming foreign investment policy

Underpinning Objective of Non-Discrimination

- National treatment is probably the most important standard
  - However, very sensitive issues
  - and qualifications to national treatment usually apply

National Treatment Definition

- The obligation on a host country to extend foreign investors' treatment that is at least as favourable as the treatment that it accords to national investors in like circumstances

- Some wording variations, but essentially the same effect
National Treatment Definition

- Issue of “at least as favourable as” (ref. “the same as”)
- Issue of “in like circumstances”

National Treatment with Qualifications

- Challenge is to keep them to a minimum and as transparent as possible
- General exception (national security, health, public order)
- Subject specific (eg, culture)

National Treatment with Qualifications

- Some industry exceptions
- Negative list
- Positive list
Economic Policy Flexibility

- NT without qualifications should not inhibit macroeconomic policy flexibility
  - Also scope for temporary derogations
- Industry policy flexibility possible, if needed, via industry specific exceptions

Pre – Establishment and Post - Establishment

- Key Scope issue
  - pre-establishment stage
  - post-establishment stage
- Post – entry is most common
- Scope for combinations/variations
  - using exceptions
  - screening systems

Powers of Sub – National Authorities

- Particularly relevant for federations
- Difficulties include
  - participation in international negotiations
  - constitutional power to commit sub- national authorities
  - transparency
Powers of Sub-National Authorities

- An issue more generally for IIA not just national treatment

Relationship to Other General Standards of Treatment

- NT generally occurs along with other treatment standards
  - MFN, fair and equitable
- Separate or combined, or more favourable
- Is this an issue

De Jure and De Facto National Treatment

- NT through laws/regulations for foreign investors
- Other laws/regulations may discriminate
  eg, branches of foreign controlled companies and prudential requirements
De Jure and De Facto National Treatment

- Perhaps acceptable if “no greater than necessary”

Dispute Resolution

- Dispute resolution processes and obligations bring rigour
- A range of issues arise

Dispute Resolution

- However, these have more general interest for international investment agreements
  - not just in relation to national treatment
Conclusion

- National treatment is an important principle for foreign investors
  - crucial/key component of international investment agreements
- Sensitivities exist
  - However, there is a range of mechanisms to address those difficulties
NT Treatment in IIAs

The NT Principle in IIAs: Overview

- Is a core element of investment promotion and protection;
- Serves to eliminate distortions in competition and to enhance an efficient economy;
- Is a key instrument for pursuing national development policies in IIAs (either by confirming the NT principle or by deviating from it).

The Nature and Scope of the NT Principle
The Basic Approaches to NT in IIAs

- NT principle not included (e.g. ASEAN, early Chinese BITs, some Australian, Singaporean and Indonesian IIAs);
- « Best efforts » clause to grant NT (e.g. APEC, ECT on pre-establishment);
- NT principle subject to domestic law (e.g. BIT between Hong Kong-China and New Zealand);
- Legally binding NT principle (the most common approach; e.g. BITs, NAFTA, APEC, MERCOSUR);
- Right of establishment (e.g. EU Treaty).

The Basic Approaches to NT II

- Some IIAs include an explicit « standstill» clause (prohibition to introduce new non-NT conforming measures). Example: BIT between China and Netherlands;
- Some IIAs emphasise particular issues to which the NT principle applies (e.g. BIT between Japan and Russia – access to courts);

The Distinction between the Pre- and Post-establishment Phase

- NT in the post-establishment phase only;
- Examples: Majority of BITs, ECT, ASEAN Investment Agreement
- NT in the pre- and post-establishment phase;
- Examples: US, Canadian and recent Japanese BITs, most APEC FTAs with investment chapters
The Distinction between « Top-down » and « Bottom-up » NT treatment

« Top-down »: NT treatment is granted unless there are exceptions or reservations.
Examples: BITs, NAFTA, ECT.

« Bottom-up »: NT treatment is only granted if a specific individual commitment is made.
Example: GATS.

Investment Activities covered by the NT Principle

IIAs use different approaches:
- Enumeration of activities: (establishment), (acquisition), (expansion), management, operation, use, disposition, sale, liquidation – closed list;
- General: all investment-related activities (e.g. French model BIT) –open-ended.
- Open-ended: NT treatment to “investment” (e.g. BIT between Japan and Bangladesh).

Beneficiaries of NT Principle

Under most IIAs, investors and their investments receive NT treatment, but
- E.g. ECT: only investments;
- E.g. French model BIT: only investors.
The Issue of Like Circumstances

Many IIAs do not contain any standard of comparison (e.g. French, UK, Swiss model BITs);
Numerous IIAs refer to « like circumstances » (e.g. US, Canadian BITs, several FTAs with investment chapters in Asia-Pacific region) or « like investors and investments » (e.g. ASEAN).

Definition of the NT Principle

The « same » or « as favourable as » treatment (e.g. World Bank Guidelines, Cartagena Agreement);
"No less favourable" treatment (most commonly used approach; e.g. many BITs, NAFTA, GATS, MERCOSUR, APEC, ASEAN, ECT).

Exceptions/Reservations to the NT Principle
## Exceptions/Reservations to the NT Principle

IIAs contain – to various degrees – exceptions/reservations to the NT clause.

**Distinguish:**
- General exceptions;
- Subject-specific exceptions;
- Country-specific reservations.

### General Exceptions

General exceptions that might apply to the NT principle include:
- Public order (e.g. BIT between Japan and Korea);
- Prudential measures (e.g. Canadian model BIT);
- Essential security interests (e.g. BIT between Australia and India);
- Protection of health and the environment (e.g. BIT between Armenia and Canada).

### Subject-specific NT Exceptions

Some IIAs contain NT exceptions in the following areas:
- Intellectual property granted under int. conventions;
- Prudential measures;
- Incentives;
- Public procurement;
- Cultural industries;
- Special establishment formalities;
- Taxation (taxation treaties only or all taxation matters).
Country-specific NT reservations

- It gives CPs the freedom to exclude any economic sector or activity from the application of the NT principle.
- More frequent concerning pre-establishment issues;
- Various options exist concerning the details: e.g. limitation in time, subsequent review, standstill commitment.

Conclusions

- The NT principle is a standard clause in IIAs;
- IIAs contain to various degrees exceptions and reservations to NT;
- IIAs differ in particular on whether the NT principle extends to the pre-establishment phase;
- NT reservations may be an important means to design host countries' development policies.
Thank you.
National Treatment: the Economic and Development Implications and Policy Options of Those Different Elements from a View Point of Japan’s Cases

Shigeki TEJIMA

2006 APEC Workshop on Non-discrimination Treatment in Investment Agreements

National Treatment: the economic and development implications and policy options of those different elements from a view point of Japan’s cases

Shigeki TEJIMA PhD.
Professor
Nishogakusha University, Tokyo, Japan

Effects of FDI liberalization in Investment agreement on Trade, Investment and Development (produced by Shigeki Tejima)

(1) FDI liberalization in investment agreements cause an acceleration of international trade and FDI growth through improving predictability of foreign investors

(2) Accelerated FDI inflow stimulates higher employment in host countries, more advanced technological capability and, in general, more vitalized economy of host countries.

(3) On the other hand, FDI liberalization have to provide good investment environments, which will lead to a sustainable development of host countries.

Changing policy for international investment treaties by Japan (produced by Shigeki Tejima)

- From very strong orientation toward multilateral investment framework to more comprehensive approach, including conclusion of bilateral and regional framework of FTA (Free Trade Agreement) /EPA (Economic Partnership Agreement) with neighboring countries, which may also stimulate domestic economic reform in Japan
- Difficulties in negotiation for multilateral investment liberalization led by WTO; bilateral and regional framework of FTA/EPA will lead to “WTO plus (“deeper integration” or “going beyond the WTO”)”?
- Prominent performance of “trade creation” effects and “dynamic effects” of FTA/EPA on related economies may exceed “trade diversion” effects.
Basic Characteristics of Japan’s FDI
(produced by Shigeki Tejima)

- Greater role of FDI than international trade
- Prominent regionalization in Japan’s FDI and International Trade in Asia
- Greater Export, Import and Japanese Affiliates’ sales in Asia than in other regions
- Higher profit on FDI in Asia than in other regions

Japan’s Trade Balance of Goods and Services and Income Balance (produced by Shigeki Tejima with MOF (Ministry of Finance) data: Unit: 100 million Japanese Yen = about 1 million US dollar)

Japan’s Export to USA and China and Japanese Affiliates sales in USA and China
(produced by Shigeki Tejima with MOF and METI (Ministry of Economy, Trade and Industry data))
Japanese Affiliates sales by region in all industries (produced by Shigeki Tejima with METI data: Unit: 100 million Japanese Yen = about 1 million US dollar)

Japanese affiliates electronics/IT industries sales by country and sub-region (Produced by Shigeki Tejima with METI data)

Sales profit ratio of Japanese affiliates by region (METI)
Japan's Export by region (produced by Shigeki Tejima with MOF data: Unit: 100 million Japanese Yen = about 1 million US dollar)

Japan's Import by region (produced by Shigeki Tejima with MOF data: Unit: 100 million Japanese Yen = about 1 million US dollar)

Japan's BITs (Bilateral Investment Treaties) with foreign countries

- Egypt  1977 signed
- Sri Lanka 1982 signed
- China  1988 signed
- Turkey  1992 signed
- Hong Kong 1997 signed
- Pakistan  1998 signed
- Bangladesh 1998 signed
- Russia   November 1998 signed, May 2000 effectuate
- Mongolia 2001 signed
- Singapore 2002 signed; 2002 effectuated
- (pre-establishment National Treatment)
- Korea    2002 signed; January 2003 effectuate
- Vietnam  2003 signed
Japan’s EPA (Economic Partnership Agreement) with foreign countries/region

- Mexico: Signed September 2004, Effectuated April 1st 2005
- Malaysia: Signed December 13th 2005
- Thailand: Agreed
- Philippines: Agreed
- Indonesia: in negotiation
- Vietnam: in negotiation
- ASEAN: in negotiation

Strengthened liberalization of FDI in EPA, especially in National Treatment (produced by Shigeki Tejima)

- Japan’s preferring EPA to FTA, because the former includes comprehensive liberalization of trade and investment
- “The Doha Declaration recognizes that regional trade agreements can play an important role in promoting the liberalization and expansion of trade and in fostering development (OECD, 2003)”
- Pre-establishment National Treatment in the Japan’s EPA with Singapore, Mexico and Malaysia
- Prohibition of Performance requirement has been decided in the Japan’s EPA with Singapore, Mexico and Malaysia

Developing countries’ concern: the bad effects of inward FDI and non-discrimination Treatment on them (produced by Shigeki Tejima)

- Inward FDI may give bad effects on the economic development, political regime, culture, environment and labor markets.
- Furthermore, Investment promotion competition, including non-discrimination Treatment in Investment Agreements, among host countries may lead to races to the bottom of host countries in their inward FDI incentive systems, labor conditions, market competition, environment etc.
The efforts by multilateral organizations to accelerate FDI liberalization and to diminish the concern in developing countries (produced by Shigeki Tejima)

- OECD, Declaration on International Investment and Multinational Enterprises
- United Nations, UNCITRAL
- World Bank Group, Convention of the Settlement of Investment Dispute between States and Nationals from other States: 1965
- World Bank Group, ICSID
- Multilateral Investment Guarantee Agency
- APEC Non-Binding Investment Principles: 1994

The efforts have been and will be achieved by both Multinational Enterprises and Host countries (produced by Shigeki Tejima)

- In order to accelerate FDI liberalization and promotion, Good Governance of FDI in host countries shall be established: transparency, predictability, accountability, commitment
- In order to diminish the concern in developing countries, Corporate Governance and Social Corporate Responsibility by Multinational Corporations have to be achieved in host countries.

Request by Japan’s private sector represented “KEIDANREN” (2002, 2004 Keidanren) for foreign investment (produced by Shigeki Tejima)

- Transparency in FDI policy, especially, legal systems and administrative procedures of host countries
- Protection of inward FDI in remittance of profit to home countries and in exploitation of Japanese firms assets etc.
- Intellectual Property Right (IPR) and Portfolio Investment as well as FDI shall be protected in International Investment Agreement led by WTO
- Promoting political stability, trade and FDI liberalization through FTA/EPA with neighboring Asian countries as well as through WTO negotiation
Private Participation in Infrastructure (PPI)

- 15 years from 1990 to 2004, PPI amounted to 868.1 billion US Dollars (2954 cases)
- By industry, 49% of the total to the Energy sector, 32% to the Transportation sector, and 14% to the Telecommunication sector.
- By region, 45% to South and Central America, 23% to Asian Pacific Region and 16% to Europe and Central Asia.

The effects of Regional Integration

- Trade Creation Effects
- Trade Conversion Effects
- Higher Productivity
- Accelerated Accumulation of Capital, Growing Regional Market
- Trade Diversion Effects

Promising countries, for which Japanese firms are planning to implement FDI (Japan Bank for International Cooperation)

<table>
<thead>
<tr>
<th>2005 survey</th>
<th>2004 survey</th>
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<tbody>
<tr>
<td>1. China</td>
<td>397</td>
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<tr>
<td>2. India</td>
<td>174</td>
</tr>
<tr>
<td>3. Thailand</td>
<td>149</td>
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<td>4. Vietnam</td>
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<td>5. USA</td>
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<td>6. Russia</td>
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<td>7. Korea</td>
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<td>8. Indonesia</td>
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<td>9. Brazil</td>
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<td>10. Taiwan</td>
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<td>4. Vietnam</td>
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<td>8. Korea</td>
<td>44</td>
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<td>9. Taiwan</td>
<td>41</td>
</tr>
<tr>
<td>10. Malaysia</td>
<td>28</td>
</tr>
</tbody>
</table>
The effects of Non-discrimination treatment on Japan and Neighboring Asian countries

- More accelerated FDI by Japanese firms in promising countries
- Mutually beneficial relationship between Asian host countries and Japan’s multinational corporations will be strengthened in Asia and other regions
- Transportation Machinery industry will expand more FDI in Asia than before.

Japan’s FDI in transportation

Japan’s FDI in ICT and electronics

September 1-3, 2006  Xiamen, China
Changing Competitiveness of Japanese firms (produced by Shigeki Tejima)

(1) Competitive Transportation Machinery (Automobile) industry and electrical/auto specialty parts and materials
(2) Weakened competitiveness of ICT (information, communication technology) industry
(3) Accelerated “Commoditization” and Globalization through ICT revolution both in supply and demand sides

Japanese firms/industries’ competitiveness, reflecting advantages in supply side and market (demand) side conditions (produced by Shigeki Tejima)

<table>
<thead>
<tr>
<th>Demand</th>
<th>Supply</th>
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<tbody>
<tr>
<td>(I) Large demand for high value added and high priced specialty products</td>
<td></td>
</tr>
<tr>
<td>(II) Large demand for low priced commodity products</td>
<td></td>
</tr>
</tbody>
</table>

(1) Production of specialty parts and final products
   (A) Automobile industry

(2) Production of Specialty parts, Development of innovative products
   (B) Sophisticated parts industry, Cutting edge ICT industries
   (E) Some type of Japanese parts firms

(3) Production of commodity products
   (C) Catching up industries
   (F) Cost competitive East Asian producers

Sales Current profit ratio (%) of Foreign Affiliates in Japan and Japanese firms in Japan

<table>
<thead>
<tr>
<th>Foreign Affiliates in Japan</th>
<th>Japanese firms in Japan</th>
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<tr>
<td></td>
<td>2002</td>
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<td>2002</td>
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</table>
How to reconstruct International Competitiveness of Japanese firms in global/regional dimension (produced by Shigeki Tejima)

- Social and corporate systems, which support "Japanese Preference" vs. Social and corporate systems, which support "Non-Japanese Preference"
- Closely related Networks among well-known firms vs. Open Networks among firms in arms-length
- Non-discriminating National Treatment gives Japanese firms much possibility to solve the above issues and to create new models for accelerating FDI and strengthening mutually beneficial relationship with host countries, in cooperation with local human resources and competitive local firms.
National Treatment: the Economic and Development Implications and Policy Options

Rebecca Fatima Sta. Maria

Outline

• Context
  – Importance of FDI
  – Approach to Investment Agreements
• Definition of National Treatment
• Implication of National Treatment in International Investment Agreements
• Policy Options
APEC Workshop on Non-Discrimination Treatment in Investment Agreements

Malaysia’s Phases of Industrial Growth


Primary commodities/ agriculture

Assembly-type/ Import substitution

Medium-tech/ heavy industries & services

High-tech & services

Knowledge-based/ higher-value added

Ministry of International Trade and Industry, Malaysia, September 2006

Relationship Between FDI and GDP Growth

GDP Growth

FDI

Ministry of International Trade and Industry, Malaysia, September 2006

Importance of FDI to the Manufacturing Sector in Malaysia

• FDI has a positive and statistically significant relationship with economic growth (MITI study, 2004):
  > 1% increase in FDI = 0.02% rise in real GDP;
  > FDI contributed to growth in manufacturing output and transformation of manufacturing sector;

Ministry of International Trade and Industry, Malaysia, September 2006
Importance of FDI to the Manufacturing Sector in Malaysia

• In the context of trade:
  - 1% rise in FDI = 0.04% increase in exports in the short term, and 0.52% increase in the long term;
• Annual Establishment Survey, Dept of Statistics, Malaysia:
  - Foreign-owned firms accounted for 70% of total exports of manufactured products;
  - These companies more export-oriented.

Importance of FDI to the Manufacturing Sector in Malaysia

• Other positive contributions:
  - Employment;
  - Capital formation;
  - R&D;
  - Human capital development;
  - Outsourcing of services;
  - Tax revenue;
  - Technology transfer.

Approach to Investment Agreements

• Malaysia to continue participating in international agreements which can enhance trade and investment flows;
• Approach = Progressive liberalisation;
• Ensure an enabling environment and opportunities for growth;
• Increase access for Malaysian investors.
**DEFINITION**

**National Treatment:**
- ensures that there is **no discrimination** between foreigners and nationals;
- guarantees that foreign investors and their investments are **accorded treatment no less favourable than that it accords, in like circumstances**, to its own investors and their investments.
• The principles of “non-discrimination, MFN and national treatment” created in the context of trade in goods: appropriate for investment?

• Important to consider stage of development of a country;
• Pre-establishment phase: can developing countries control the entry of foreign investors and types of investments?
• Post-establishment phase: would it impede the ability of government to give preferential treatment to local firms, or to channel foreign investment in certain desired directions?

• Host country required to justify differential treatment between the foreign and domestic investor;
• Clarification of “in like circumstances”: does this mean investors in the same “business” or “sectors”.

What matters?
Imperatives for Developing Countries

- Development imperative:
  - when, what and how to liberalize;
  - development-oriented policies, socio-economic development;

- Strengthen domestic industry;

- Must reflect national policies
  - No need to commit to NT if doing so would mean conceding so much of the country’s economic autonomy or limits national policy space.
FAIR AND EQUITABLE TREATMENT IN IIAs

APEC Workshop, Xiamen, 1-3 September 2006
Joachim Karl
Legal Affairs Officer
UNCTAD/DITE

F&E Treatment
Overview of Presentation

- Objective, content and general implications of the F&E treatment standard;
- Drafting options;
- Some specific issues;
- The F&E treatment standard in arbitration practice.

I. Objective, content, and general implications of the F&E Treatment Standard
**F&E Treatment Objectives**

- Provides a general standard of treatment for foreign investors;
- Supplements the more specific protection standards;
- There is uncertainty about the precise meaning of the standard and its implications.

**Origins of the F&E Treatment Principle**

- Draft Havana Charter 1947;
- FCN Treaties of the US in the 1950s;
- Draft Abs Shawcross Convention 1960;
- Draft OECD Convention 1967;
- Vast majority of BITs;
- Regional and sectoral IIAs (e.g. NAFTA, ECT);

**The Content of the F&E Treatment Standard**

**Int. Minimum Standard**

- Pro: Standard refers to established jurisprudence;
- Con: Equation with «IMS» is not obvious and existence of relevant CIL not universally recognized.

**Plain Meaning approach**

- Pro: Provides a flexible "safety net";
- Con: Lacks in precision and is inherently subjective.
**Int. Minimum Standard**

« Neer » case of the ICJ (1926):

IMS prohibits acts that amount to « bad faith, wilful neglect, clear instances of unreasonableness or lack of due diligence ».

**Plain Meaning Approach**

- As compared to the int. minimum standard, the plain meaning approach tends to provide a higher level of protection.
- There is a trend towards a more investor-friendly interpretation of the standard in recent arbitration practice.

**Implications for IIA negotiations**

- It follows from the main purpose of IIAs to create favourable investment conditions that F&E treatment is an integral part of most agreements.
- However, views differ concerning the meaning of the standard. This raises the question of whether its content should be further specified in the IIA. Various options exist.
- The growing jurisprudence on the F&E treatment standard contributes to clarifying its content.
- Importance of the clause also depends on the extent to which the IIA contains other, more specific protection standards.
Implications for development policies

- The F&E treatment standard leaves host country flexibility to pursue their development policies;
- However, the lower the threshold for a violation of the standard, the more the regulatory flexibility of host countries is constrained.
- The concrete wording of the clause might to some extent affect a country’s attractiveness as host to FDI:
  - General language: Might signal openness and strong protection;
  - Specific language: Might signal reservations, but might also reinforce protection.

II. Drafting Options

Main Drafting Options in IIAs

- Option 1: No reference to F&E;
- Option 2: Hortatory approach;
- Option 3: Reference to F&E only;
- Option 4: Reference to F&E combined with one or more additional elements:
  - + Reference to int. minimum standard (CIL);
  - + Reference to discriminatory, arbitrary or unreasonable measures;
  - + Reference to full protection and security.
  - + Reference to national law.
### Option 1: No reference to F&E Treatment

- Is exceptional in IIAs (e.g., BIT Egypt–Japan);
- Might send a negative signal concerning the investment climate in the host country;
- Limits protection to explicit treaty standards and customary international law.

### Option 2: Hortatory Approach

- Intermediary solution between “all-or-nothing” approach;
- Very few examples (ICC Guidelines, Pacific Basin Charter);
- Might send an even more negative signal concerning the investment climate in the host country than having no reference to the standard at all.

### Option 3: F&E Treatment only

- Frequently used approach in IIAs;
- Provides legal assurance about general treatment and thereby contributes to investor confidence;
- Content of standard remains vague – further clarification needed?
- Is in itself not enough for providing sufficient investment protection.
Option 4: F&E Treatment + Other Elements

**International minimum standard (CIL)/International law**
- Examples: US BITs, NAFTA, BIT between France and Mexico;
- May provide more certainty concerning the meaning of the standard;
- Difficulties if CPs disagree on the existence of CIL in this area;
- Possibility to spell out in more detail what CPs mean with the reference to this standard (see, e.g., US model BIT – more general; BIT between France and Uganda – more specific.).

F&E Treatment + Other Elements II

**Prohibition of discriminatory, arbitrary or unreasonable measures**
- Approach taken in numerous IIAs (e.g. German BITs);
- Might further reinforce investment protection;
- Might, however, also be interpreted as a reference to the IMS (at least partially).
- This raises important questions:
  - Relationship between F&E treatment and the other elements;
  - Relationship between prohibition of discriminatory measures and specific NT/MFN clauses.

F&E Treatment + Other Elements III

**Full protection and security**
- Approach taken in numerous IIAs (e.g. NAFTA, ECT);
- Is sometimes combined with prohibition of discriminatory, arbitrary or unreasonable measures;
- Reinforces protection in particular with regard to physical threats to the investor and/or investment.
- Unclear in what other areas this standard might apply.
F&E Treatment + Other Elements IV

Linkage to NT/ MFN Principle
- Approach sometimes taken in IIAs (e.g. BIT between Eritrea and Uganda);
- Combines an absolute protection standard with a relative standard;
- Would change the level of protection only in the unlikely case that host countries have different standards of F&E treatment for foreigners and domestic citizens.

F&E Treatment + Other Elements V

Reference to domestic law of host country
- Rarely used approach in IIAs (e.g. BIT between CARICOM and Cuba);
- Diminishes investment protection (is made subject to domestic law);
- Could send a negative signal concerning the investment climate.

Alternative Wording for F&E Treatment
- Some IIAs use alternative wording, such as « equitable » or « just and equitable » treatment.
- It appears that these variations have no significant legal implications.
Trends in recent treaty practice

Example: BIT between US and Uruguay
- Refers to customary international law as applicable standard;
- Explains that CIL includes F&E treatment and full protection and security;
- Specifies the content of each of these standards.
- Clarifies relationship with other treaty standards.

III. Some specific issues

F&E Treatment and the Specific Non-Discrimination Standards in IIAs

Is F&E Treatment an overriding principle encompassing the NT and MFN standard?
- One might argue that F&E treatment means a general prohibition to discriminate;
- However, there are strong arguments that NT and MFN treatment are separate standards.
F&E Treatment and Exceptions

There is the issue of whether exceptions included in an IIA extend to F&E treatment:
- It could be argued that F&E treatment is a basic protection to be provided in all circumstances.
- Some IIAs allow, however, for exceptions. They relate, in particular, to national security interests, but may also extend to other issues (e.g. taxation).

IV. The F&E treatment standard in arbitration practice

F&E Treatment in Arbitration Awards
- No uniform interpretation of the F&E treatment standard; arbitration practice is still emerging;
- High threshold of the « Neer » case has been lowered in more recent awards (i.e. trend towards a more investor-friendly interpretation of the standard).
- Standard has been interpreted as prohibiting a « wilful disregard of due process of law, an act which shocks, or at least surprises, a sense of judicial propriety ».
- Standard of « improper and discreditable » behaviour has likewise been used.
Discrimination against foreign investors has been regarded as an important indicator;
Some tribunals referred to international or comparative standards.
A failure to effectively implement aspects of domestic law is not necessarily a breach of the standard;
Other criteria employed include arbitrariness, idiosyncrasy, injustice, lack of good faith, lack of due process and proportionality.

Specific applications

- Transparency and the protection of the investor’s legitimate expectations;
- Freedom from coercion and harassment;
- Procedural propriety and due process;
- Good faith.

Transparency and the protection of the investor’s legitimate expectations (e.g. Metalclad, Maffezini, Tecmed, MTD, Occidental, Mondev cases):
Protects the investor against a reversal of decisions or inconsistent action by different government organs and against arbitrary changes of the law.
F&E Treatment in Arbitration Awards

Specific applications III

Freedom from Coercion and Harassment (e.g. Pope & Talbot, Tecmed cases):

Protects the investor against hostile treatment on the part of the government authorities.

Specific applications IV

Procedural propriety and due process of law (e.g. Metalclad, Tecmed, Loewen and Waste Management cases):

This standard includes, in particular, respect of the right to be informed of and to be heard in judicial and administrative proceedings.

Specific applications V

Good Faith (e.g. Tecmed, Waste Management, Mondev cases):

This standard encompasses protection against the use of legal instruments for uses other than their intended purpose and any conspiracy by government authorities to destroy the investment.

Note that action in bad faith is not necessary for a violation of the F&E treatment standard.
Conclusions

- The principle of F&E treatment is common in most IIAs;
- It provides important protection without imposing heavy constraints on host countries;
- It may create different expectations concerning the level of protection;
- Countries have taken different approaches in IIAs concerning the level of specification of the principle.
- Gradual evolution of jurisprudence.

Thank you.
Introduction of China Reciprocal Promotion and Protection of Investment Agreements

Lu Tao

Introduction of China Reciprocal Promotion and Protection of Investment Agreements

Presentation by
Lu Tao
Treaty and Law Department
MOFCOM
P. R. China
September 2006
Xiamen, China

Organization of this presentation

• Introduction: Overview of Chinese reciprocal promotion and protection of investment agreements (RPPIAs)
• Basic elements of China RPPIAs
• New development of China RPPIAs and the positions on some “hot topics”

Introduction: Overview of Chinese reciprocal promotion and protection of investment agreements (RPPIAs)

• First RPPIAs dated from 1982
  - Concluded with Sweden on March 29, 1982, following the opening-up policy
  - Intended to attract foreign direct investments, mainly in the second sector

• Up to now, China has concluded such RPPIAs with 118 countries
Existing RPPIAs

- Asia: 38
- Europe: 36
- Africa: 29
- Latin America: 11
- Oceania: 4

Pending Negotiations

- RPPIAs with Canada, Mexico, Korea (second agreement), Russia (second agreement) are in process of negotiation
- Negotiations of investment chapters in FTA with New Zealand, Australia, ASEAN have been initiated

Basic elements of China RPPIAs

- Two generations of RPPIAs
- The first generation: from 1982-1997
- The second generation: 1997 till now
  - new elements added, such as national treatment, catch-all investor-state dispute settlement mechanism, symbolized by China-Canada RPPIAs negotiation
Basic elements of the first generation RPPIAs

- Likely to be the copy of German style BITs
- Investment definition
- Investment treatment
- MFN
- Compensation for losses
- Expropriation with compensation
- Repatriation of returns
- Dispute resolution between Contracting Parties
- Dispute settlement between investor and state

Investment definition

- China-Sri Lanka RPPIAs (1986): “the term 'investment' means every kind of asset permitted by each Contracting Party in accordance with its laws and regulations…”
- Inference from such definition:
  1. investment already made;
  2. investment approved by host country

Investment treatment

- Fair and equitable treatment approach
- See China-UK RPPIAs (1986) “Investments of nationals or companies of either Contracting Party shall at all times be accorded fair and equitable treatment and shall enjoy the most constant protection and security in the territory of the other Contracting Party.”
MFN

- See China-Thailand RPPIAs (1985)
  "Each Contracting Party shall, in its territory, accord to nationals and companies of the other Contracting Party as regards the management, use, enjoyment or disposal of their investments, treatment which is equitable and not less favourable than that it accords to the nationals and companies of any third State."
- Confirmed that only admitted investments are qualified for such RPPIAs

Expropriation

- Provisions in relevant Chinese laws:
  1. Constitution (Article 11)
     "The State may, in the public interest, expropriate land for its use in accordance with the law."
  2. Law on State Compensation (Article 4):
     "The victim shall have the right to compensation if an administrative organ or its functionaries, in exercising their functions and powers, commit any of the following acts infringing upon property right:
     (1) illegally inflicting administrative sanctions such as imposition of fines, revocation of certificates and licenses, ordering suspension of production and business, or confiscation of property;
     (2) illegally implementing compulsory administrative measures such as sealing up, distracting or freezing property;
     (3) expropriation property or apportioning expenses in violation of the provisions of the State;
     (4) other illegal acts causing damage to property.

Expropriation

- Provisions in relevant Chinese laws:
- Law on Sino-Foreign Equity Joint Ventures (Article 2):
  "The State shall not subject equity joint ventures to nationalization or expropriation. In special circumstances, however, in order to meet public interest requirements, the State may expropriate an equity joint venture in accordance with the legal procedures, but appropriate compensation must be paid."
- The same language revealed in the Law on Wholly Foreign-Owned Enterprises
Expropriation

• See China-Potugal RPPIAs (1992):
  "Neither Contracting Party shall expropriate, nationalize or take similar measures...against investments of investors of the other Contracting Party in its territory, unless the following conditions are met:
  (a) in the public interest;
  (b) under domestic legal procedure;
  (c) without discrimination;
  (d) against compensation."

Expropriation

• Other international alternatives of expropriation conditions:
  • Resolution on Permanent Sovereignty Over Natural Resources (UN General Assembly 1962)- Appropriate compensation
  • Charter of Economic Rights and Duties of States (UN General Assembly 1974)- appropriate compensation
  • Calvo Doctrine – domestic law governs
  • "Hull Formula" – prompt, adequate and effective compensation
  • In accordance with due process of law

Repatriation

• Pre-condition provided for repatriation of profits
• See China-Australia RPPIAs (1988):
  • "A Contracting Party shall...permit, subject to its laws and policies, all funds of a national of the other Contracting party related to an investment or activities associated with an investment in its territory,..."

• With regard to Chinese side, all repatriation shall be approved by competent authority
Investor-State disputes settlement mechanism

- Two approach adopted in the first generation RPPIAs
- Pre-ICSID-accession RPPIAs:
  See China-Sweden, China-UK RPPIAs: ad hoc arbitration. However, both sides agreed, in a exchange of letters, that upon China’s accession to the ICSID Convention, the RPPIA should be supplemented by an additional agreement providing for a mandatory system of settlement of disputes before the ICSID.

Investor-State disputes settlement mechanism

- Post-ICSID-accession RPPIAs,
- China has notified ICSID pursuant to Article 25(4) of the Convention, of the class of disputes it would consider submitting to the jurisdiction of the Center, namely disputes over compensation for expropriation. China’s notification reads as follows:
  “Pursuant to Article 25(4) of the Convention, the Chinese Government would only consider submitting to the jurisdiction of the International Centre for Settlement of Investment Disputes disputes over compensation resulting from expropriation and nationalization.”
- Limited jurisdiction of ICSID arbitration

Investor-State disputes settlement mechanism

  “If a dispute concerning the amount of compensation referred to in the provisions...of Article 5 between a national or company of either Contracting Party and the other Contracting Party..., such dispute shall, at the request of such national or company, be submitted to a conciliation board or an arbitration board, to be established with reference to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States done at Washington on March 18,1965.”
New development of China RPPIAs and positions on some “hot topics”

- New second generation RPPIAs replacing first generation RPPIAs
- Commencing from 2001, amendment to the existing RPPIAs with European countries, such as the Netherlands, Germany, Finland.
- “substantive” progress in investor protection - national treatment and international arbitration

National Treatment

- Not new in the first generation RPPIAs
  "The treatment accorded by either Contracting Party within its territory to nationals and companies of the other Contracting Party with respect to investments, returns and business activities in connection with the investment shall not be less favourable than that accorded to nationals and companies of the former Contracting Party."

- However, in the paragraph 3 of the Protocol to the Agreement, both sides agreed that “for the purpose of the provisions of paragraph 2 of Article 3 of the Agreement, it shall not be deemed ‘treatment less favourable’ for either Contracting Party to accord discriminatory treatment, in accordance with its applicable laws and regulations, to nationals and companies of the other Contracting Party, in case it is really necessary for the reason of public order, national security or sound development of national economy."

National Treatment

- While national treatment committed in the second generation RPPIAs, supplementary provisions provided in protocol
- See China-Finland RPPIA:
  "The provisions (national treatment) do not apply to any existing non-conforming measure maintained within its territory of the People’s Republic of China or any future amendment thereto, provided that the amendment does not increase the non-conforming effect of such a measure from what it was immediately before the amendment took effect.
  Treatment granted to investments once admitted shall in no case be made more restrictive than the treatment granted at the time when the original investment was made.
  The People’s Republic of China will take all appropriate measures to progressively remove all non-conforming measures."

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No limitation for the investor-state disputes submitted to international arbitration

- While China did not withdraw its reservation to the ICSID Convention, recent China’s RPPIAs contained more broadly drafted dispute settlement clauses which do not reproduce the terms of its notification to the Center
- All legal disputes related with investments between an investor and the State could be submitted to international arbitration, either ICSID or UNCITRAL arbitration, with requirement of exhaustion of domestic administrative review procedures

International arbitration

- China’s requirement is based on Article 26 of the ICSID Convention, which reads as:
  "Consent of the parties to arbitration under this Convention shall, unless otherwise stated, be deemed consent to such arbitration to the exclusion of any other remedy. A Contracting State may require the exhaustion of local administrative or judicial remedies as a condition of its consent to arbitration under this Convention."

International arbitration

- See China-Belgium Protocol (2005):
  "It’s mutually understood that the People’s Republic of China requires that the investor concerned exhausts the domestic administrative review procedure specified by the laws and regulations of the People’s Republic of China, before submission of the dispute to international arbitration under Article 8, paragraph 2. The People’s Republic of China declares that such a procedure will take a maximum period of three months."
“Hot Topics” in recent BITs and China’s position

• New style BITs led by the U. S., typically the NAFTA approach
• Pre-establishment national treatment
• Minimum standard of treatment in accordance with customary international law
• Transparency
• Performance requirement
• Intellectual property
• Environment
• Competition policy

“Hot Topics” in recent BITs and China’s position

• Pre-establishment national treatment
  - for the current development stage of China’s economy, it is unacceptable to us to commit obligations which is beyond our capacity

• Minimum standard of treatment in accordance with customary international law
  - there is no uniformed interpretation of such standard and general practice of so-called "customary international law" except certain industrialized countries’ practice

• Transparency and performance requirement
  - China could not go further than WTO Agreements (GATs, TRIMs) for certain period of time and unlikely to include separate articles in its RPPIAs

“Hot Topics” in recent BITs and China’s position

• Intellectual property, Environment and Competition policy
  - these are not directly related with investment, it is appropriate to be addressed in other specific agreements between two States
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Mexico’s Experience and Policy with International Investment Agreements (IIAs)

**MEXICO’S POLICY**

- Mexico continues impelling foreign investment promotion through bilateral investment treaties (BITs) and free trade agreements (FTA’s)
- In 2004 the Mexican executive confirmed this approach with a decree approving the:

**FOREIGN TRADE AND FOREIGN INVESTMENT PROMOTION PROGRAM**

**PROGRAM PRINCIPLES:**

- Foster trade and investment
- Promote balanced economic development
- Impel growth with quality through solid trade and investment instruments
- Strengthen Mexico’s economy through favourable conditions for investment

Seminar “Non-Discrimination in International Investment Agreements”

MEXICO´S EXPERIENCE AND POLICY WITH INTERNATIONAL INVESTMENT AGREEMENTS (IIAs)

Xiamen September 2006, China
APEC Workshop on Non-Discrimination Treatment in Investment Agreements

**Mexico’s Bilateral Investment Treaties (BITs) and Free Trade Agreements (FTAs)**

- **El Salvador**
- **Costa Rica**
- **Nicaragua**
- **Honduras**
- **Guatemala**
- **Israel**
- **Canada**
- **United States**
- **Korea**
- **Chile**
- **Argentina**
- **Bolivia**
- **Venezuela**
- **Colombia**
- **Uruguay**
- **Portugal**
- **Holland**
- **Switzerland**
- **Austria**
- **Spain**
- **France**
- **Italy**
- **Greece**
- **Germany**
- **Belgium**
- **Luxembourg**
- **Finland**
- **Denmark**
- **Ireland**
- **United Kingdom**
- **Sweden**
- **Norway**
- **Iceland**
- **Liechtenstein**

**Mexico’s Experience with FDI**

- **Regional FDI Origin**
  - **Asia**: 41.2%
  - **North America**: 24.7%
  - **Other**: 1.4%

**Mexico’s Major Exporting Power & Major FDI Recipient**

- Imports substitution vs. FDI & Exports Promotion
- Mexico’s Experience with FDI INFLOWS

*Source: Ministry of Economy, National Registry for Foreign Investment*
MEXICO’S EXPERIENCE WITH FDI
IIA’S (BITs & FTAs)
IIA’S HAVE HELPED IN CREATING FAavourABLE CONDITIONS FOR INVESTMENT

- Mexico operates a very liberal screening regime for pre-establishment investment and effectively provides national treatment on post-establishment investment. However, the own nature of Mexico’s foreign investment policy on pre-establishment investment discriminates in rather small number of activities between foreign investors and domestic investors, thereby restricting the provision of national treatment.
- Foreign legal persons authorized by the Ministry of Economy are allowed to establish offices in Mexico if they intend to carry out non-regulated activities.
- Mexico offers national, most favored nation, and fair and equitable treatment in most of its FTAs and BITs.

GENERAL POLICY FRAMEWORK:
NON-DISCRIMINATION

ARBITRAL CASES

Mexico has been involved in several investment arbitration processes

10 NAFTA CASES
2 BITC CASES
(Tecmed; Gemplus & Talsud)
THE NAFTA CASES

24 NAFTA cases to date

- 4 cases against Canada
- 10 cases against Mexico
- 10 cases against the US

- 13 Cases Finally Decided
- 1 Case Settled
- 2 Cases Inactive
- 2 Pending Active Cases

Total Victories for States
- Azinian v. Mexico
- Mondev v. USA
- ADF Group v. USA
- Loewen Group v. USA
- Waste Mgmt. v. Mexico (I & II)
- GAMI v. Mexico
- Methanex v. USA
- Riemann's Fund v Mexico
- Thunderford v. Mexico

Partial Victories for Investors
- Metalclad v. Mexico
- SD Myers v. Canada
- Pope & Talbot v. Canada
- Feldman v. Mexico

NAFTA CASES AGAINST MEXICO (DECIDED CASES)

DAMAGES CLAIMED V. DAMAGES AWARDED
(MILLIONS US DOLLARS)

248.5
18

BIT CASE AGAINST MEXICO (DECIDED CASES)

DAMAGES CLAIMED V. DAMAGES AWARDED
(MILLIONS US DOLLARS)

60
6.8
ISSUES IN DISPUTE

- In most of the cases, investors have claimed violations to:
  1. Minimum Standard of Treatment, and
  2. Expropriation

- In other few cases, the obligations alleged to have been breached were National Treatment (NT) and Most-Favoured-Nation Treatment (MFN).

MINIMUM STANDARD OF TREATMENT

NAFTA Article 1105

(1) Each Party shall accord to investments of investors of another party treatment in accordance with international law, including fair and equitable treatment and full protection and security.
MINIMUM STANDARD OF TREATMENT IN THE NAFTA

**Article 1105**

**First Generation:**

- MST interpretations prior to the Free Trade Commission Interpretation (July 31, 2001)

- Metalclad: A breach of the transparency objectives set forth in the NAFTA establishes a violation of A.1105

- Pope & Talbot: FET & FPS are “additive” to the minimum standard of treatment

- SD Myers: A violation of the NT obligation establishes a violation of A.1105

**Second Generation:**

- More than a simply illegality or lack of authority is required

- CIL demands appropriate evidence

- The conduct of the state has to be arbitrary and grossly unfair

- There has to be an evident lack of due process leading to an outcome that offends judicial propriety

**Free Trade Commission (“FTC”) Interpretation (July 31, 2001)**

1. Article 1105 prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another party.

2. 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 the customary international law minimum standard of treatment of aliens.

3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).
WASTE MANAGEMENT, INC. V. UNITED MEXICAN STATES (FINAL AWARD) (APRIL 30, 2004)

"THE MINIMUM STANDARD OF TREATMENT OF FAIR AND EQUITABLE TREATMENT IS INFRINGED BY CONDUCT ATTRIBUTABLE TO THE STATE AND HARMFUL TO THE CLAIMANT...

IF THE CONDUCT IS ARBITRARY, GROSSLY UNFAIR, UNJUST OR IDIOSYNCRATIC, IS DISCRIMINATORY AND EXPOSES THE CLAIMANT TO SECTIONAL OR RACIAL PREJUDICE, OR INVOLVES A LACK OF DUE PROCESS LEADING TO AN OUTCOME WHICH OFFENDS JUDICIAL PROPRIETY...

AS MIGHT BE THE CASE WITH A MANIFEST FAILURE OF NATURAL JUSTICE IN JUDICIAL PROCEEDINGS OR A COMPLETE LACK OF TRANSPARENCY AND CANDOUR IN AN ADMINISTRATIVE PROCESS."

GAMI INVESTMENTS, INC. V. MEXICO (FINAL AWARD) (NOV. 15, 2004)

"A CLAIM OF MALADMINISTRATION WOULD LIKELY VIOLATE ARTICLE 1105 IF IT AMOUNTED TO AN 'OUTRIGHT AND UNJUSTIFIED REPU DIATION' OF THE RELEVANT REGULATIONS."

NATIONAL TREATMENT (NT) NAFTA Article 1102

"EACH PARTY SHALL ACCORD TO INVESTORS OF ANOTHER PARTY TREATMENT NO LESS FAVORABLE THAN THAT IT ACCORDS IN LIKE CIRCUMSTANCES TO INVESTORS OF ITS OWN WITH RESPECT TO THE ESTABLISHMENT, ACQUISITION, EXPANSION, MANAGEMENT, CONDUCT, OPERATION, AND SALE OR OTHER DISPOSITION OF INVESTMENTS"
APEC Workshop on Non-Discrimination Treatment in Investment Agreements

Purpose: Prevention of discrimination on the basis of the nationality of investors.

The provision protects investors at both the establishment and post-establishment phases.

Applies only “in like circumstances”.

Prohibits both de jure and facto discrimination.

Subject to specific reservations covered in NAFTA Annex I and II.

International Thunderbird Gaming Corp. v. Mexico
(Final Award) (Jan 26, 2006)

The obligation of the Host NAFTA Party under Art. 1102 (NT) is to accord non-discriminatory treatment towards the investment or investor...It must therefore be established that discriminatory treatment was accorded.

There has not been sufficiently established that investments were treated, in like circumstances, worse than those of Mexican nationals.

The Tribunal shall accordingly measure Art. 1105 of NAFTA against the customary international law minimum standard, according to which foreign investors are entitled to a certain level of treatment, failing which the host state’s international responsibility may be engaged.

The content of the minimum standard should not be rigidly interpreted and it should reflect evolving international customary law. Notwithstanding the evolution of customary law, the threshold for finding a violation of the minimum standard of treatment still remains high, as illustrated by recent international jurisprudence.

For the purposes of the present case, the Tribunal views acts that would give rise to a breach of the MST prescribed by NAFTA and CIL as those that, weighed against the given factual context, amount to a gross denial of justice or manifest arbitrariness falling below acceptable international standards.
MEXICO’S FORWARD-LOOKING POSITION:
- CONTINUE NEGOTIATING IIAS
- TAKING INTO ACCOUNT EXPERIENCE
- ASSESSING INVESTMENT TRENDS
- KEEPING TRACK OF GLOBAL INVESTMENT CLIMATE
- LOOKING FOR SOUND AND EQUILIBRATED IIAS

ISSUES TO CONSIDER WHEN NEGOTIATING INVESTMENT INSTRUMENTS:
- FOLLOW A WELL-BACKED STRATEGY
- USE OF LEGAL TECHNIQUE
- CLARITY, CONSISTENCY AND CERTAINTY
- IIAS ARE NOT “ANY-RISK” POLICIES
- BALANCE INVESTOR-STATE

FINAL MESSAGES
- IN THE OVERALL CONTEXT, MEXICO HAS GONE THROUGH A POSITIVE EXPERIENCE WITH IIAS
- AS PART OF OUR POLICY, WE SUPPORT THE NEGOTIATION OF IIAS WITH STRATEGIC COUNTRIES
- HOWEVER, SUCH DECISION ENTAILS RESPONSIBILITY
- MORE THAN EVER, WE ARE CONSCIOUS OF THE NEED TO DESIGN GOOD AND BALANCED IIAS
APEC Workshop on Non-Discrimination Treatment in Investment Agreements

EXPERIENCE IS FUNDAMENTAL
IN ORDER TO LEARN FROM IT AND
CONDUCT BETTER NEGOTIATIONS OF IIAS

FINAL MESSAGES

AT THE END OF THE DAY, ANY INVESTMENT TREATY HAS TO KEEP A RIGHT BALANCE BETWEEN A REASONABLE PROTECTION TO INVESTMENT AND THE LEGITIMATE NEEDS OF THE HOST STATE

THE END

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# APEC Workshop on Non-Discrimination Treatment in Investment Agreements

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