Inconsistencies in treatment of foreign investment in trade agreements

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December 2008
INCONSISTENCIES IN THE TREATMENT OF FOREIGN
INVESTMENT IN AUSTRALIA’S TRADE AGREEMENTS

INTERNATIONAL REGULATION OF INVESTMENT

Frameworks for international regulation of investment

Regulation of foreign investment is only recently a matter within the domain of international law. While there is currently no comprehensive instrument at the multilateral level that regulates foreign investment or its liberalisation, a legal framework is emerging.

Since the 1950s, international investment was largely regulated through bilateral investment treaties (BITs). Their focus was on enhancing the investment climate and attracting more FDI between signatories by granting strong protection rights against discriminatory or confiscatory state conduct.

This changed significantly with the entry into force of the North American Free Trade Agreement (NAFTA) in 1994 and the establishment of the World Trade Organisation (WTO) in 1995. The WTO General Agreement on Trade in Services (GATS) brought the supply of services into the realm of international trade rules (including that through the establishment of a commercial presence). NAFTA was the first free trade agreement (FTA) to combine BIT-like investment provisions with comprehensive and detailed disciplines for services and investment liberalisation.

Since NAFTA the number of FTAs covering investment in a comprehensive way has increased significantly. The structure and approach to investment in many has been heavily influenced by NAFTA, BITS and the GATS.

It has also been influenced by efforts of the Organisation for Economic Co-operation and Development (OECD) to develop international rules governing capital movements, international investment and trade in services. Beginning in the 1970s, OECD members established ‘rules of the game’ for themselves and for the multinational enterprises that operate within their jurisdictions. This was achieved thorough several codes for liberalisation including for capital movements, financial services, and other current invisible transactions. The Codes of Liberalization are legally binding on all OECD members.

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1 There is no right to invest in a foreign country under customary international law.
6 OECD member countries and eight non-member countries have also subscribed to declarations regulating international investment and multinational enterprises, which incorporate the principles of national treatment. This includes the OECD Declaration and Decisions on International Investment and Multinational Enterprises and The Declaration on International Investment and Multinational Enterprises.
The rise of FTAs

Preferential FTAs have proliferated since the 1990s, particularly in the Asia Pacific region. A new generation of FTAs is emerging with provisions governing foreign investment that are increasingly sophisticated and broad. In contrast to BITs, they are more aptly termed economic integration agreements; commitments to liberalise and to protect or promote investment flows between the parties form an integral part of a wider agreement for liberalisation of trade in goods and services, the movement of people and capital flows.

Since 1994, over 180 agreements combining investment and services rules in the form of FTAs have been negotiated. The pace has picked up markedly since 2000. In 2007, 12 new FTAs with investment provisions were concluded, bringing the total to 254. In contrast, the number of BITs being concluded has declined.

FTAs now occupy an important place in the regulation of international investment and play a key part in the in the creation of (liberal) international law on foreign investment. Countries have increasingly preferred to address investment protection as well as newer investment liberalisation in the context of FTAs, rather than through the conclusion of traditional BITs.

INVESTMENT AND INTERNATIONAL TRADE AGREEMENTS

The role of FTAs

From an economic perspective, nation states include investment in FTAs to derive the benefits from opening the economy to greater participation by foreign investors and investment.

One reason is to extend the effective size of the market for trade and investment. Removal of trade barriers enlarges the market and allows firms to benefit from greater scale. This helps attract market seeking production activities from within and outside the FTA area, for which scale is an important consideration.

A further imperative is to strengthen the overall competitiveness of the economy through restructuring or rationalisation. Relocation of production within partner countries is driven by comparative advantage and helps to increase intra-FTA efficiency seeking investment. It is closely related to the adoption of investment rules that relax market entry restrictions and provide for legal protection. It is accepted that to ensure the combined efficiency effects of scale and comparative advantage, lowering of tariffs alone is not sufficient (although it is a necessary pre condition).

More generally, inclusion of legally binding commitments helps to strengthen the predictability and transparency of the economic climate for investors. It also assists FTA

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7 OECD (2008) p 244.
12 Ibid.
partners to realise the full benefits of trade liberalisation under the agreement, which can be
impeded by barriers to investment flows.13

Investment provisions in FTAs also serve as a means of deepening economic integration
between FTA partners. They can permit parties to move beyond the multilateral level and
take on new policy initiatives in their economic interests in areas that might be too difficult
at the global level.14 External benefits are expected to be generated by the liberalisation of
international trade and investment through closer economic integration.15 Greater levels of
FDI may also drive further benefits arising from stronger commercial relationships.

Investment provisions in FTAs often form part of broader efforts to strengthen political
relations as economic integration increases regulatory political interaction and helps build
trust in other areas.16 One of the core motivations for the negotiation of the Australia/United
States FTA (AUSFTA) for example, was to deepen political as well as economic ties
between Australia and the United States (US).

Core liberalising principles

National treatment

National Treatment is the commitment by a country to treat foreign investors and
investments no less favourably than domestic investors and investments. It is a core
principle through which FTA parties seek to liberalise investment flows. It can apply to
investors pre establishment of their investment and to investments in the post establishment
phase, often with limited exceptions.

The granting of national treatment to investors in the pre establishment phase is key as it
determines the level of liberalisation. Post establishment guarantees do not liberalise
investment flows because they impose no obligation on the host country to permit
investment. They are akin to more traditional rights granted in BITs which reduce or
remove the size and scope of restrictions post establishment and strengthen the protection
of investment vis a vis domestic investors.

Most favoured nation treatment

Most Favoured Nation (MFN) treatment is a commitment to treat a foreign investor or
investment from one jurisdiction no less favourably than an investor or investment from
any other jurisdiction that has been awarded MFN status.

In a bilateral FTA the value of the MFN principle lies in the ability for an FTA partner to
benefit from more liberal treatment in third party agreements. It also has a broader value
where it applies a standard to create a liberalising dynamic.17 This will depend on whether
the extension of MFN treatment is limited or excluded. Many FTAs allow a party to
withhold its most liberalising treatment from other parties. In that case the effectiveness of

Relevance. Emerging Trends and Policy Implications’ in ESCAP, Toward Coherent Policy
Frameworks: Understanding Trade and Investment Linkages, Trade and Investment Studies, No 62,
p 4.
15 These benefits arise from the impacts on third parties from a commercial transaction, which
neither side of the transaction takes into account when they agree on its terms. See Douglas A Irwin,
17 OECD (2008), p 296.
MFN treatment in creating a level playing field between investors from various FTA partners is questionable.\textsuperscript{18}

**Treatment of investment in FTAs**

The degree of liberalisation achieved in an FTA is directly related to its legal structure; the scope and coverage of the definitions provisions, the substantive provisions; the exceptions to this; dispute resolution mechanisms and their interaction.

Treatment of investment in FTAs can generally be classified into two broad categories: those which have been inspired by NAFTA and those which more closely follow the GATS.

**NAFTA style agreements**

NAFTA inspired agreements group provisions on investment for all sectors in one chapter and grant national treatment and MFN across the board in a ‘one shot’ effort at liberalisation. Non conforming measures are specifically excluded in a schedule to the agreement. This is known as a ‘negative list’ approach.

These types of agreements typically provide for broad investment coverage and include strong protection for and non discriminatory treatment of investment. Commitments are often complemented with provisions for investor state dispute settlement (ISDS).

In some cases, non conforming measures are subject to a ‘ratchet mechanism’ which limits changes to non conforming measures to subsequent liberalisation. This has the effect of “locking in” future reforms and preventing expansion of restrictive measures.

**GATS inspired agreements**

Treatment of investment in FTAs which is based on the WTO GATS Agreement combines a ‘positive’ scheduling of sectors (whereby parties list areas where they undertake commitments to liberalise) with a negative list of limitations that they wish to maintain. MFN and transparency tend to be general obligations, with market access and national treatment granted only to the extent liberalisation commitments are scheduled.\textsuperscript{19} GATS style agreements are generally favoured by countries that wish to preserve a certain flexibility and progressiveness in their liberalisation.\textsuperscript{20}

Several factors influence the choice of a GATS or NAFTA inspired approach to investment liberalisation: the openness of each parties regimes; their administrative capacity; past approaches used and the pace at which they wish to liberalise.\textsuperscript{21} Ultimately the type of agreement chosen to regulate investment will be a matter of negotiation.

Generally NAFTA style agreements are considered to be more liberalising than GATS style agreements given their broader coverage and the predictability and the transparency associated with listing of non conforming measures. New investments are automatically granted national treatment and MFN.\textsuperscript{22} A positive list approach can be lacking in

\textsuperscript{18} Ibid, p 243.
\textsuperscript{19} OECD (2008) p 245.
\textsuperscript{21} Ibid, p 243.
\textsuperscript{22} Ibid, p 279.
transparency as there is simply no information on the kind of restrictions that can exist in non committed sectors.\(^{23}\)

However, it is still possible to achieve significant liberalisation following a GATS style approach. Predictability can be improved in a positive list by providing enough information to investors, simplifying the way schedules of commitments are presented and by a clear commitment to future liberalisation.\(^ {24}\) An ambitious level of liberalisation can be achieved by taking on new commitments in new sectors or increasing commitments in existing sectors.

**Best practice regulation**

A legal framework for investment rules which provides for substantive commitments to open the market to foreign investment and which is clear, predictable and consistent is considered to be the “best practice” means for realising the liberalisation benefits under an FTA.

Although the choice of agreement adopted will ultimately be negotiated, the treatment of investment can vary in terms of the structure of commitments, the scope and degree of liberalisation, and the nature of enforcement mechanisms.

Consistency across agreements with respect to these features, in accordance with best practice, is important for realising liberalising objectives.

‘Best practice’ features are summarised in Box 1 below.

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**Box 1 - Best practice treatment of investment in FTAs**

**Scope of liberalisation**
- Broad definitions of investor and investment
- Non discriminatory treatment of investors and investment: National treatment and MFN
- Discretion for employment in investments
- Limitations on performance requirements

**Standard of investment protection:**
- Minimum standards of protection
- Guarantees of free transfers;
- Prohibition on expropriation; provision of compensation

**Degree of liberalisation**
- Comprehensive liberalisation with limited exceptions (WTO plus)
- Central and regional government application

**Enforcement**
- State to state dispute settlement
- Investor state dispute settlement

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\(^{23}\) Ibid, p 275.

\(^{24}\) Ibid, p 250.
Scope of liberalisation

The definition of investor and investment determine the scope of application of rights and obligations under the agreement. Broad definitions which cover both direct and portfolio investment as covered investments and legal persons and natural persons as covered investors are to be preferred.

Inclusion of a commitment to liberalisation, including granting of national treatment to investors in the pre-establishment phase, is crucial. The scope of the right will depend on how investor is defined. Liberalisation commitments can be further expanded through granting of MFN treatment.

A negative list ‘NAFTA style’ approach to liberalisation with inclusion of a ratchet mechanism is generally to be favoured over a ‘GATS style’ approach.

Where possible, provisions which relax nationality and residency requirements for the employment key managerial or professional personnel in investments should be included. This might be complemented with a separate chapter on mobility of business persons.

Performance requirements should be limited or prohibited, preferably beyond those covered by WTO disciplines. Such requirements may interfere with the investors’ prerogative to manage the investment and may impair its value.

Degree of liberalisation

The depth of liberalisation achieved under any FTA is determined by both the substantive scope of the agreement and by the extent and nature of the commitments made, whether under a positive or negative list approach.

A general rule is that commitments to liberalisation using either approach should be comprehensive and WTO plus.

Exceptions to national treatment and MFN should be limited (negative list approach) or commitments should be extensive (positive list approach) across sectors and by type of restriction.

Liberalisation commitments should also extend to measures taken by both central government and regional government where possible.

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25 The former tends to encompass the narrower concept of “commercial presence” upon which liberalisation obligations in services chapter are based. The latter may be subject to with domicile or nationality requirements. OECD (2008) p 9.

26 Usually defined based on NAFTA, to include export requirements, domestic content requirements, requirements to use domestic suppliers, technology transfer requirements, requirements for the value and volume of imports, sales for foreign exchange flows associated with investment.

27 The WTO TRIMS Agreement prohibits certain performance requirements that are consistent with the provisions of the national treatment and quantitative restrictions in the GATT.

28 They also distort trade by preventing the importation or exportation of goods or services and may subject some investments to more burdensome requirements than others. Ibid, p 41.

29 In the case of investment, for which there are no truly specific provisions in the WTO, commitments should expand upon those made for commercial presence undertaken under the GATS.
Standard of protection

The introduction of protection standards furthers the goal of establishing a favourable investment climate. This is achieved through binding commitments to remove or reduce restrictions on the transfers of funds related to foreign investment and restrictions that impede the recovery of profit.

Minimum standards of protection under international customary law, where expressly provided for, may be guaranteed and further defined in FTAs. This includes protection for investors against expropriation of investment by the host economy and for the provision of compensation where it occurs.

Nature of enforcement

In addition to providing for state-to-state dispute settlement, FTAs may include mechanisms authorising arbitration of disputes involving the treaty between investors and the host countries without the involvement of the investor’s home country (investor state dispute settlement).

AUSTRALIA, INVESTMENT AND FTAS

The economic importance of FDI

Traditionally Australia has relied heavily on foreign investment to bridge the gap between domestic savings and domestic investment. In part this reflects the country’s extensive endowment of natural resources and the highly capital intensive nature of the natural resource industries, such as mining. Moreover, Australian businesses are increasingly investing in overseas markets to exploit economies of scale and scope. This tends to reduce further the volume of domestic savings that are available for funding domestic investment.

Australia taps foreign savings through either by borrowing abroad (foreign debt) or by allowing greater foreign ownership of Australian assets (foreign equity). Foreign direct investment (FDI) is one form of foreign ownership. The other principal form of foreign ownership involves portfolio investment in Australian businesses. Expanding foreign investment flows, both inward and outward, has accelerated with recent growth in the Australian economy.

In today’s open global economy, the ability to attract investment is more important than ever. Having achieved open global markets for merchandise trade, the capacity of domestic businesses to attract foreign investment and to invest abroad has become increasingly vital to the technological and business innovation that underpins productivity growth and progressively higher standards of living in a medium-sized economy such as Australia.

Australian regulation of foreign investment

Australian law requires foreign investment proposals in excess of certain monetary thresholds to be screened and approved as being in the ‘national interest’ prior to their execution.

The thresholds vary with the circumstances. They include the acquisition of substantial interests in an Australian business valued at over A$100 million, the establishment of a new business involving an investment of over A$10 million, or any investment by or on behalf of a foreign government. The AUSFTA sets higher thresholds for US entities (see next section).
There are further restrictions on foreign investments in those industry sectors that are considered to be particularly sensitive. They include banking, civil aviation, airports, shipping, the media, telecommunications, and residential real estate.

The screening process is conducted by the Foreign Investment Review Board (FIRB). The Treasurer is responsible for making the decisions on individual investment proposals. Where a foreign investment proposal does not conform to the policy, the Government has the power to block it, or to order the sale of any property that was purchased contrary to government guidelines. Investments by foreign governments and their agencies (such as those by state-owned enterprises and sovereign wealth funds) can raise additional issues.

**Restrictiveness of the regulatory regime**

The overall effect of the regime is to restrict the volume of foreign investment that enters Australia in a given period.\(^{31}\)

The regulatory regime imposes a delay on all inwards foreign investment that is subjected to review. Such delays represent a permanent and ongoing cost to the domestic economy in terms of the return foregone during the screening process.

Over 7 per cent of investment applications to FIRB are withdrawn before the review process is completed. These investment opportunities are likely to be permanently lost to Australia.

Some 30 per cent of the investments approved by the Government have restrictions placed on them. The restrictions vary considerably but generally relate to ensuring or preserving the Australian character of the business being established or acquired.

An unknown number of prospective investment opportunities are never even considered by the Australian Government. These cases do not generate an application to the FIRB due to the subjective assessments by investors of the low probability of success for a given investment application and the significant time and effort in preparing an application to the FIRB.

The restrictiveness of Australia’s regime has been confirmed by the OECD, which indicates\(^{32}\) that Australia is among the most restrictive of the countries it monitors, both within the OECD as well as outside it.\(^{33}\) Were Australia’s screening restrictions to be lifted, the OECD has estimated that Australia’s stock of inwards foreign investment would be increased by nearly 50 per cent over the long run.

**FTA policy and investment**

Australia has pursued bilateral free trade agreements with major trading partners simultaneously with its participation in the multilateral negotiations under the Doha Round. Bilateral liberalisation is generally viewed as complementary or as “building blocks” to

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\(^{30}\) Pursuant to the *Foreign Acquisitions and Takeovers Act 1975.*

\(^{31}\) See *Foreign Direct Investment in Australia – the increasing cost of regulation*, Report by ITS Global, 9 September 2008 at [http://www/itsglobal.net](http://www/itsglobal.net)

\(^{32}\) According to the OECD FDI Regulatory Restrictiveness Index.

\(^{33}\) Of the 43 countries assessed to date, only China, Russia, India and Iceland have regulatory regimes that are more restrictive than Australia’s regime.
multilateral processes; presenting opportunities to pursue liberalisation where multilateral processes move slowly or in the case of investment, are absent.

Bilateral FTAs were concluded first with New Zealand as early as 1983 followed by Singapore (2003), Thailand, the US (both 2005) and Chile (2008). Since 2005, negotiations have been launched with Malaysia, China, Japan, and the Gulf Cooperation Council. Preparatory talks toward negotiations are currently underway with Korea. A regional FTA with ASEAN countries and New Zealand was concluded in August 2008, but is yet to be signed.

Although the Australia/New Zealand Closer Economic Relations FTA (CER) provides for close to completely free trade in goods and services, it does not specially cover investment. This largely reflects its predating of Australia’s first BIT, the WTO and also NAFTA. In 2005, the possibility of adding treaty-level protection for investment through an Investment Protocol was raised. Negotiations have been ongoing since 2006. There is a commitment to conclude the Protocol by 2009, which Australia’s Trade Minister has publicly supported.

The FTA with the United States is the most comprehensive agreement Australia has negotiated since CER. Negotiations presented an opportunity for the government to consider the scope for liberalisation of Australia’s FDI policy regime; a core demand from the US side. The resulting treatment of investment negotiated in the FTA was important in two respects: significant policy liberalisation on the part of Australia (the first relaxation of policy brought about by investment negotiations); and a treaty text that is an important marker in Australia’s investment treaty policy. It was influenced not only by the need to improve bilateral trade and investment flows with a major trading partner, but also the desire to strengthen bilateral political and economic ties more broadly.

TREATMENT OF INVESTMENT IN AUSTRALIA’S FTAS

Inconsistencies in the treatment of investment

Australia’s FTAs are not consistent in the level of investment liberalisation and protection accorded. This applies in terms of Australia’s liberalisation of its own investment policy regime and in the structure of commitments, the scope of non discriminatory treatment, the application of policy restrictions and the nature of enforcement.

Inconsistencies concern:

- Inclusion of specific, preferential and more liberalising disciplines on investment than under domestic law in all FTAs, except for New Zealand in CER;
- Adoption of inherently more liberalising “NAFTA style” agreements for regulation of investment in AUSFTA, SAFTA and CHAFTA, but use of a more limited “GATS style” approach in TAFTA;
- Broad application of non discrimination for liberalisation of foreign investment and its subsequent protection in AUSFTA and CHAFTA - both include national

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34 The Australia and New Zealand Closer Economic Relations Trade Agreement was concluded in 1983 and represents a major expansion of a more limited bilateral agreement, which had been in place since the 1950s.

Inconsistencies in the Treatment of Foreign Investment in Australia’s Trade Agreements

- Commitment to significant policy liberalisation of FIRB screening thresholds under AUSFTA which is withheld from other FTAs and subsequent FTA partners;
- Provision for ISDS in all recent FTAs, but not in AUSFTA, and;
- Inclusion of NAFTA style prohibitions on performance requirements in AUSFTA and CHAFTA but not other FTAs.

Table 1 - Liberalisation of investment under Australia’s FTAs

<table>
<thead>
<tr>
<th>Feature</th>
<th>CER</th>
<th>AUSFTA</th>
<th>CHAFTA</th>
<th>SAFTA</th>
<th>TAFTA</th>
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<tr>
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<td>√</td>
<td>√</td>
<td>√</td>
<td>Positive</td>
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<td>√</td>
<td>√</td>
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<td>√</td>
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<td>limited to covered investments</td>
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<td>Higher thresholds for screening and approval</td>
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<td>√</td>
<td>x</td>
<td>x</td>
<td>x</td>
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<td>√ Senior management only</td>
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<td>√</td>
</tr>
</tbody>
</table>

√ Indicates commitment  X indicates absence of commitment

Structure of commitments

Australia has generally adopted a negative list “NAFTA style” approach in its recent FTAs, with the exception of TAFTA. All include a dedicated chapter on investment, separate from that for trade in services. Positive substantive rights are accorded across the chapter, subject to exclusions listed in Annexes.

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TAFTA adopts a “GATS style” approach, though applies a combined a positive and negative list. Some rights (those with respect to establishment for example) are accorded only to scheduled measures. Others (with respect to post establishment) apply generally unless excluded in schedules.

CER, although also a “negative list” agreement, does not include specific obligations or a dedicated chapter on investment.

**Scope of liberalisation**

**Coverage**

The scope of investment and investors, and thus the application of investment disciplines under the agreement, is broad under AUSFTA and CHAFTA. The definition of investment is broad and asset based. It includes FDI and portfolio investment, as well as intellectual property. Investors include enterprises and nationals.

SAFTA adopts similar definitions. In TAFTA coverage is limited to direct investment as defined by the International Monetary Fund.

CER includes no definition of investment or investor. The Protocol on Trade in Services to CER includes obligations pertaining to the direct investment of service providers, while making these subject to foreign investment policies. New Zealand service investors therefore have rights post establishment.  

**Non discriminatory treatment**

All FTAs (with the exception of CER) provide for liberalisation through rights to non discrimination for investors and covered investments, albeit to differing degrees.

AUSFTA and CHAFTA grant national treatment and MFN rights to investors and investments both pre and post establishment.

SAFTA provides rights only for national treatment in the pre and post establishment phase. There is a weak provision to “give consideration” to subsequent liberalisation in future agreements but no express right of MFN treatment.

TAFTA accords national treatment pre establishment only to scheduled measures. Post establishment national treatment however is applied negatively to covered investments, as is MFN in both the pre and post establishment phase.

Pre establishment is generally defined broadly to include establishment; acquisition; expansion; management; conduct; operation; sale and other disposition of investments in territory of the prospective party. It applies to the central and regional government level where not excluded.

Notably MFN obligations in AUSFTA, SAFTA and CHAFTA do not apply to measures reserved in annexes. FIRB threshold screening requirements for example, are reserved as exceptions to both national treatment and MFN (see below).

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Limiting MFN treatment is significant from a liberalising point of view where the withheld measure is considerably more liberal or the relevant restriction is economically important. This is the case with Australia’s treatment of FIRB screening thresholds under AUSFTA, discussed below.

**Government approval and screening requirements**

The greatest inconsistency in treatment of foreign investment in Australia’s FTAs arises from the differing requirements maintained for foreign investment proposal review and approval in the AUSFTA on the one hand, and other recent FTAs on the other.

In SAFTA, TAFTA and more recently CHAFTA, current FIRB thresholds apply.37 (See Box 2 below). The threshold requirements are reserved in annexes to the agreement (and therefore not subject to non discrimination obligations). Where there is doubt over whether investments are notifiable then they must be screened.

In contrast, under AUSFTA, Australia substantially lifted the thresholds for screening of investments. The following US investments must be screened, as noted in Box 3 below.

This treatment is reserved as an exception to the general non discrimination principles of the agreement. It does not automatically apply to TAFTA and CHAFTA, despite the inclusion of MFN clauses in these agreements.

In the absence of investment provisions in CER, investments from New Zealand are screened according to the FIRB thresholds. While in practice investments may be screened liberally, no preferential legal treatment is guaranteed.

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37 Thresholds were raised unilaterally in 2008 above levels specified in the FTAs.
Inconsistencies in the Treatment of Foreign Investment in Australia's Trade Agreements

Box 3 - FIRB screening thresholds under AUSFTA

- Foreign investments in non sensitive sectors over A$871 million (indexed annually - $913 million 2008);
- Foreign investments in sensitive sectors including telecommunications transport and defence related industries over A$100 million (indexed annually - $105 million 2008);
- Investments in existing business where the value of total assets exceed $50million in various sectors (telecoms, transport, supply of human resources; military goods and technologies, extraction of uranium and nuclear facilities);
- Investments in businesses in all other sectors (excluding financial sector companies) where value of total assets exceed $800million, including acquisitions of developed non residential commercial real estate;
- Direct investment (any size) and portfolio investment of 5 percent or more in the media sector, and;
- All investment in residential real estate and the media and by foreign governments.

Employment and movement of personnel

Australia’s FTAs also include provisions which loosen restrictions on employment of senior management in investments, although to differing degrees. In several agreements, they are complemented with specific provisions for the movement of business personnel. Together these provisions operate to create a more liberal environment for the operation of foreign investments.

AUSFTA prohibits nationality requirements for senior management positions in enterprises, except for a majority or less of boards of directors and committees and provided they do not impair the ability of the investor to control the investment.

This is more liberal than the treatment accorded under SAFTA, TAFTA and CHAFTA in which residency requirements apply for directors and secretaries of companies.

Outside of the investment chapter however, AUSFTA is not supported by specific provisions to permit the temporary movement of business personnel. The US resisted the inclusion of such provisions for domestic political reasons following the conclusion of its FTAs with Chile and Singapore. Instead, a visa scheme was negotiated between Australia and the US outside of the FTA to allow Australian nationals to work in the US temporarily, subject to conditions.

TAFTA and SAFTA both include provisions for the limited movement of business personnel.

CER is the most liberal in this respect, with the Trans Tasman Travel Arrangement permitting free movement of labour between Australia and New Zealand.
**Performance requirements**

Only AUSFTA and CHAFTA specifically regulate performance requirements. Provisions in AUSFTA extend the WTO Trade Related Investment Measures (TRIMS) Agreement to cover measures in the services sector as well as goods. Requirements relating to the transfer of technology, the exclusive supply to specific services markets and domestic sales rates are prohibited. CHAFTA also includes prohibitions on performance requirements which extend beyond the TRIMS Agreement.

**Standard of investment protection**

All recent FTAs provide for some degree of investment protection akin to that traditionally found in BITs. The scope varies however, with AUSFTA and CHAFTA providing for more detailed standards, based closely on that provided for in NAFTA.

Only AUSFTA and CHAFTA for example, include minimum standards of protection in accordance with customary international law. TAFTA includes a general provision for protection of investments and to ensure fair and equitable treatment.

All FTAs, with the exception of CER, guarantee transfers relating to covered investments in a freely convertible currency. All include equivalent prohibitions on expropriation or nationalisation of covered investments and provide for compensation.

**Degree of liberalisation**

The actual degree of liberalisation achieved across all agreements is difficult compare given the differential scope of liberalisation provided. An accurate picture of the degree of ‘market access’ provided to foreign investors requires a detailed examination of the schedules of reservations (AUSFTA, SAFTA, CHAFTA) and positive commitments (TAFTA), all of which are beyond the scope of this paper.

**Nature of enforcement**

A further inconsistency among treatment of investment in Australia’s FTAs arises from rights of enforcement granted. Australia has included ISDS provisions in all of its recent FTAs with the exception of the US. These provisions have their origin in NAFTA and have been included in most US bilateral FTAs. AUSFTA merely includes a provision for the parties to consult where it is considered that a change in circumstances warrants an investor submitting a claim to arbitration directly.

The absence of ISDS reflects the acknowledgement by both governments at the time the agreement was negotiated, of the robustness of their respective domestic legal systems. Australia in particular was of the view that an agreement between two developed countries with advanced legal systems and established rules of law did not require an additional avenue for investors to pursue their rights outside of the domestic legal system. Government at the state level strongly advocated maintaining the status quo. Notwithstanding the evolution of US treaty language to give greater guidance to arbitration panels, there also remains discomfort over NAFTA jurisprudence.

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38 The treatment of ISDS in TAFTA is limited to investment post establishment.
An important implication is that decisions by the Treasurer on foreign investment cases under AUSFTA will not be subject to international arbitration by investors when no similar rights exist under domestic law.

ECONOMIC AND POLICY OUTCOMES OF INVESTMENT IN AUSTRALIA’S FTAs

Inconsistent regulation of investment

The degree of inconsistency among agreements undermines coherent policy toward best practice regulation of investment in FTAs. It also precludes the realisation of the full potential benefits of investment liberalisation to be derived.

Several inconsistencies stand out for their economic and policy implications.

The first is the withholding of higher FIRB screening levels granted to the US from other FTA partners. Granting significantly more liberal treatment to one FTA partner reduces the potential gains from broad liberalisation, undermines policy coherence, creates discrimination and renders the MFN principle largely ineffective.

The decision not to extend the “US treatment” in other FTAs can be explained by the need to give something to an important trading partner and ally. Failure to unilateralise it is partly due to the need to keep some “negotiating coin” in subsequent FTAs. Liberalisation of FIRB screening policy in line with AUSFTA is already emerging as a core issue in the China FTA negotiations. Australia will come under increasing pressure to extend policy liberalisation in future FTAs.

The second is the exclusion of New Zealand from treaty level protection for investment liberalisation. This is despite numerous representations in recent years by New Zealand to request an investment treaty and to seek US treatment under the FIRB thresholds during negotiations for the Investment Protocol.

Given the high degree of Trans Tasman economic integration in trade in goods, services and labour, binding liberalisation of investment regimes would bring greater certainty to the business environment. It would further the process of deep economic integration under CER.

Adopting FTAs which are inconsistent in structure and scope has wider impacts for broader economic integration in the region. Australia’s FTAs negotiated with relatively developed countries (such as Singapore, Chile and the US) adopt a NAFTA style, comprehensive approach to investment liberalisation. Those with developing countries however, (Thailand, ASEAN) tend to adopt a more limited GATS style approach.

While Australia is not alone in its pursuit of differing agreements among FTA partners, consideration should be given as to how the two approaches might be reconciled among each other and as part of regional efforts, as they progress. Australia is thinking of joining the P4 Agreement. The US has indicated it will join, along with Peru and possibly Vietnam. This agreement is a comprehensive NAFTA style FTA, which is being considered as a platform for a wider APEC wide agreement. GATS style FTAs do not necessarily fit neatly within that.

42 The P4 Agreement is the Trans Pacific Strategic Partnership Agreement which currently includes Chile, Singapore, Brunei and New Zealand.
Finally, the lack of investor state dispute settlement in AUSFTA is questionable. Given the importance of US investment to Australia, business may query the economic sense of deliberately denying US investors an avenue for redress that is available to Singaporean, Thai and Chilean investors or Australian investors a similar right in the US. Political considerations partly explain the outcome. The FTA process lacked significant debate on dispute settlement.

**Future regulation of investment in FTAs**

In order to achieve best practice liberalising FTAs on foreign investment, Australia could consider the following:

1. Extending preferential FIRB screening thresholds accorded to the US under AUSFTA to other FTA partners, or unilaterally.

2. Completing the proposed Investment Protocol with New Zealand to support deeper economic integration under CER. Accord New Zealand the most liberalising treatment in recent FTAs, including US FIRB screening thresholds.

3. Adopt comprehensive ‘NAFTA style’ approaches to investment liberalisation and protection in FTAs, including granting of pre establishment national treatment and MFN, and minimal exclusions subject to a “ratchet mechanism” where possible.

4. Open and improve the debate on the inclusion of ISDS as a further avenue for redress or investors to arbitrate disputes over covered investments in FTAs.

Kristen Bondietti, November 2008.
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