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NON-DISCRIMINATION AND MODALITIES FOR PRE-ESTABLISHMENT COMMITMENTS BASED ON A GATS-TYPE, POSITIVE LIST APPROACH

EXECUTIVE SUMMARY

Canada continues to believe in the benefit of agreeing to a *general approach* to issues in the WGTI with a view to clarifying options for Ministers in the run-up to Cancun. Any prospective international investment agreement (IIA) in the WTO must be consistent with the Doha mandate, including balancing the interests of home and host countries, and taking due account of the development policies and objectives of host governments as well as their right to regulate in the public interest.

With respect to the fundamental concept of non-discrimination, as well as modalities for commitments in this regard, architectural considerations remain paramount. An IIA in the WTO will also have to be thoughtfully integrated into the existing family of WTO agreements, including the GATS as well as agreements affecting trade in goods. Many of these agreements already have provisions affecting the investment behaviour of foreign investors, particularly in so far is it is trade related.

Two of the cornerstones of a non-discriminatory trading system, national treatment and most-favoured-nation (MFN) treatment, are complementary and closely related. This is not strictly true of the GATS partly because it deals with the supply of services from outside the territory of a Party. IIAs, however, generally include similar provisions on national treatment and MFN. This is usually because such treatment is deemed necessary to reassure foreign investors concerning their commitment of capital in the territory of a Party for the long term.

In order to be of interest to governments, investors, and the interested public, an IIA in the WTO should seek to minimise differences in treatment of investors in goods industries vs. investors in services industries, as well as between foreign and domestic investors seeking to make investments in the first place – subject to agreed upon exceptions and reservations.

Both "selective liberalization" (GATS-type) and "MFN/national treatment" (negative list) agreements tend to embody pre-establishment commitments with respect to non-discrimination provisions. Indeed, drawing a distinction between pre- and post-establishment may undermine the concepts of non-discrimination and market access. However both selective liberalization and

MFN/national treatment agreements do facilitate limitations to the scope of non-discrimination provisions in a number of ways. This attribute should be retained in any prospective IIA in the WTO.

An MFN/national treatment agreement is predicated on general applicability with defined exceptions or reservations to certain provisions. This is inherently a more transparent approach than an agreement predicated on commitments undertaken with respect to selected obligations only.

Whatever the approach taken in the WTO, developing countries and LDCs may require more focused technical assistance and capacity building from developed countries in order to compile commitments, exceptions, and/or reservations. This would be a constructive means of fulfilling the Doha mandate with respect to productive and meaningful further integration of non-developed countries in the world economy.

I. INTRODUCTION

1. This paper is based on the same premise as Canada's previous submission [WT/WGTI/W/113] on scope and definition: we believe that our work in the WGTI would benefit from focussing on a *general approach* to issues that Ministers asked us to consider at Doha. In turn, this can help us to continue clarifying specific concepts with a view to providing a basis for a decision on the modalities of negotiations, without pre-judging outcomes. It is understood that our work must also be consistent with the Doha mandate, particularly with respect to the importance of balancing "the interests of home and host countries, and to take due account of the development policies and objectives of host governments as well as their right to regulate in the public interest" as indicated in para. 22 of the Doha Declaration.

2. It also bears repeating that in order for our work to be effectively anchored and as relevant as possible to the rapidly evolving international economy, Canada believes that important considerations in determining our approach to non-discrimination and related modalities for commitments include: (a) supporting the principles and objectives of the WTO as outlined in the Doha Declaration and at Marrakesh; (b) reflecting business realities and assisting in the development of a multilateral rules-based framework for evolving relationships between the state on the one hand and investors and investments on the other; and (c) providing for "flexibility" in the scope of any prospective agreement, including with respect to the development needs of members.

3. Finally, the submission is also based on a belief in the utility of a prospective investment agreement in the WTO. Ultimately, such an agreement must be consistent with a legally and administratively enhanced trade and investment framework, and thereby be a positive contribution to the activities of investors and governments, and be seen to be so by the interested public.

II. THE IMPORTANCE OF ARCHITECTURAL CONSIDERATIONS TO ANY PROSPECTIVE INVESTMENT AGREEMENT IN THE WTO

4. In order to attain all of the objectives outlined above, architectural considerations, namely the way in which any provisions in a prospective investment agreement will interact with each other, as well as the way they will interact with other agreements of the WTO system, loom large in WGTI work. This is particularly true for any provisions on non-discrimination and the way in which any reservations or commitments, including "pre-establishment" ones, are set out with respect to this fundamentally important concept. The Secretariat paper on modalities for pre-establishment commitments [WT/WGTI/W/120] sets out a useful taxonomy of three types of agreements

("investment control", "MFN/national treatment", and "selective liberalization" (or GATS) approach) in this regard.

5. "Non-discrimination" and "modalities for pre-establishment commitments" with respect to these provisions are addressed together in this submission. These subjects are inextricably linked. As the Secretariat paper on non-discrimination [WT/WGTI/W/118] points out in a number of places, the extent of non-discriminatory treatment of foreign investors and their investments is in many respects determined by how exceptions to this treatment are determined.[1] In addition, linkages between the two issues are explicitly noted in section IV.B.1 on pre-establishment and post-establishment treatment (paras. 47-52) of the Secretariat paper, where it is correctly pointed out that pre-establishment market access is increasingly important for countries wishing to attract FDI.[2]

6. Following from this, our approach to these issues should also be consistent with the other conceptual consideration that underlies the agreements of the WTO, namely transparency, which Ministers at Doha also emphasized. This issue was partly addressed at the previous WGTI meeting (see paras. 118-155 of WT/WGTI/M/17), where it became apparent that the primary objective of transparency could be considerably furthered through the way in which a prospective agreement is structured. Architectural considerations are therefore fundamentally important to the scope and coverage of any prospective provisions, including reservations and/or commitments, in any agreement, as well as how any prospective investment agreement would interact within the WTO family of agreements.

III. NON-DISCRIMINATION AND TRANSPARENCY: FUNDAMENTAL PROVISIONS IN INTERNATIONAL INVESTMENT AGREEMENTS

A. NON-DISCRIMINATION: MFN AND NATIONAL TREATMENT

7. Two of the cornerstones of non-discrimination provisions in both the WTO system and in international investment agreements are national treatment and most-favoured-nation (MFN) treatment.

8. Provisions on these powerful principles underlying a non-discriminatory trading system reinforce each other, and there are several considerations with respect to investment behaviour that suggest that they should remain complementary and closely related. Where market access is unclear, for instance, or not as transparent as it could be (which itself can depend on the approach to exceptions or scheduling commitments – see below) investors will seek in the first instance to be treated at least as well as other foreign investors (i.e. enjoy MFN treatment). Where market access conditions are more clear-cut, it becomes important for investors to seek national treatment, i.e. to be treated in the same way as domestic investors. Parties seeking to offer an optimal investment environment with a view to maximizing investment flows will also seek to provide this sort of treatment.

9. MFN and national treatment are treated differently in the GATS of course. The MFN article (Article II) is a general obligation, i.e. it applies to all sectors and measures, unless otherwise specified through exemptions. A negative list approach is thus adopted in the GATS with respect to this obligations. The concept of MFN would make little sense under a positive list approach, which would allow unlimited and unspecified discrimination between and among WTO members in sectors where no commitments are made.

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[1] See 5th and 9th paras to the Executive Summary of WT/WGTI/W/118, as well as paras. 5-9, sections III.C (paras. 25-32), IV.B.2 (paras. 53-56), and V.C (paras. 84-86).

[2] Para. 51 of WT/WGTI/W/118; as noted by UNCTAD in the International Investment Agreement Series booklet on Most-Favoured-Nation Treatment – UN Publications Sales no. E.99.II.D.11.

10. The positive list aspects of the GATS concern national treatment and market access (Articles XVI and XVII), whereby these disciplines are only relevant with respect to listed (scheduled) commitments. Even here, however, a partly negative list approach is taken, since limitations with respect to these commitments in each of four modes of service delivery are listed, as the Secretariat paper points out.

11. The possible applicability of the GATS for investment activity in both goods and services industries may be problematic however. Under the GATS national treatment, and indeed market access in general, are concepts that arguably had to be treated with a degree of circumspection with respect to trade in services through modes 1 (cross-border supply) and 2 (consumption abroad) of service delivery, whereby services are supplied from outside the territory of a Party (see also para. 39 of WT/WGTI/W/120).

12. However the GATS has attributes of clear interest to investors, as well as Parties seeking to encourage investment consistent with broader societal goals. One of these is the implicit recognition that *pre-establishment* restrictions on foreign investments (not only in terms of equity, but also with respect to licensing, numerical quotas and other restrictions) are encompassed within the agreement. Thus any Party outlining limitations with respect to market access commitments (or indeed MFN exemptions) should include pre-establishment restrictions among them. Importantly, then, even under a selective liberalization agreement such as the GATS, pre-establishment commitments are not "off the table", and Canada believes that this understanding should be retained in any IIA in the WTO.

13. This is increasingly the case in international investment agreements. There is indeed little conceptual justification for discriminatory treatment of foreign investors pre- or post- establishment.[3] Non-discrimination with respect to post-establishment is, in addition, already provided for in many IIAs, often through a negative list approach.

14. In dealing with discrimination against foreign investors, to draw an *a priori* distinction between pre- and post-establishment national treatment, could be seen to undermine the meaning of national treatment and market access. To foreign investors, the right of establishment (or pre-establishment market access) effectively determines whether in fact non-discriminatory market access exists. In an era of declining tariffs, this is an increasingly important consideration for international investors. In increasingly competitive markets, investors are less inclined to make investments for reasons attached to import substitution only, but rather to respond to market conditions extending beyond the host (or home) market. Thus there is an increasing dynamic established between investment conditions in the host market and trade possibilities, which militates against pre-establishment discrimination against foreign investment in the same way that such discrimination is addressed in the trading system.

15. It would therefore be a missed opportunity to consider designing an IIA in the WTO agreement whereby MFN and national treatment would be treated differently *ab initio*.

16. Of course it also must be acknowledged that pre-establishment market access will not be permitted by the host country in all cases in all sectors. For political or other reasons it will not always be possible, or even desirable, to do so, and even where it may make economic sense to expose domestic investors to competition from more efficient foreign investors, vested interests may make it difficult to do so. This realization is implicitly embodied in MFN/national treatment (or negative list-type) agreements, and is an important illustration of "flexibility" that is often overlooked in these sorts of agreements. Indeed MFN exemptions for bilateral and regional agreements are also a feature of investment agreements to which Canada is a party – and of the GATS itself (Article V).

[3] Indeed "post-establishment discrimination" can sometimes effectively amount to expropriation, and dealt with through investment protection provisions or agreements.

And in the NAFTA an annex also exists for Mexico which exempts several broad sectors such as petroleum, electricity, railroads, and others, from MFN, national treatment, and other provisions in the agreement.

17. Thus, from the perspective of both foreign investors and Parties to an agreement in the WTO, it could be a less than optimal approach to seek to finesse non-discrimination to allow Parties to maintain discriminatory treatment of foreign investors without taking the opportunity of describing it. Again, it must be stressed that flexibility for development or other purposes under an MFN/national treatment agreement permits discrimination under specified circumstances. Subject to negotiations, the "right to discriminate" is retained – even, in some case, for horizontal measures such as investment screening or review; what is required, however, is for Parties to state how or in which sectors or sub-sectors this discrimination occurs.

B. TRANSPARENCY

18. As noted at the last WGTI meeting, transparency is a crucially important principle that underlies and open and non-discriminatory multilateral trading system. It thus follows that commitments and/or exceptions or reservations to non-discrimination should be transparent. The GATS includes comprehensive transparency obligations, both with respect to informational requirements (publication, notification, enquiry and counter notification in Article III - Transparency) and procedural transparency (Article VI – Domestic Regulations). The possible applicability of these types of obligations to a comprehensive investment agreement was discussed at the last WGTI meeting. Another approach to transparency, raised by Canada, was the possibility that the goal of transparency can also be furthered in the way in which an investment agreement could be structured, including with respect to the way in which reservations and/or commitments to obligations are delineated.

19. From Canada's perspective, it remains evident that without transparency, it is difficult to speak of – let alone achieve – stable and predictable conditions for long-term cross-border investment. Architectural considerations furthering the transparency inherent in MFN/national treatment type agreements thus become important. An MFN/national treatment approach, predicated on general applicability, with defined exceptions or reservations, is inherently more transparent than an agreement predicated on commitments undertaken only with respect to selected obligations. It tends to be the latter approach that necessitated an additional complex transparency obligations, coupled with other obligations and ongoing negotiations as well. Another possible problem with a selective liberalization approach in the investment domain could be a tendency to "freeze" non-discriminatory treatment at relatively low levels of commitments, taking no account of further liberalization in the host country. An MFN/national treatment type agreement, however, simply lists exceptions and reservations, whether they be horizontal, broad, or specific. In this context, it should also be noted that developing countries tend to enjoy broader exemptions to non-discrimination provision than developed countries in these kinds of agreements.

IV. MODALITIES FOR SCHEDULING IN A PROSPECTIVE INTERNATIONAL INVESTMENT AGREEMENT: FURTHER IMPLICATIONS FOR THE WTO

20. Differences between MFN/national treatment vs. GATS-type modalities for pre-establishment commitments *can be* more apparent than real. Canada, which has experience of both types of agreements in, for example, the Canada-Chile Free Trade Agreement (CCFTA) and the GATS, includes comprehensive lists in both.[4] The first lists those sectors and/or subsectors – including

[4] The text and annexes to this agreement are available on the Canadian Department of Foreign Affairs and International Trade (DFAIT) website at: http://www.dfait-maeci.gc.ca/tna-nac/cda-chile/menu.asp.

horizontal measures – to which non-discrimination and other specified provisions in the agreement do not apply. This can also extend to future measures (Annex II): in specified negotiated sectors, some of which are relatively broad (in Canada, with respect to any measure affecting aboriginal affairs, for example, or to the foreign ownership of ocean front land), Parties are free to retain or indeed adopt more restrictive measures in the future. Nonetheless, they are listed, and both investors and governments can tell at a glance where discriminatory treatment is still extant and permitted. And it must also be noted that horizontal exceptions for all Parties with respect to national security, taxation, balance of payments, as well as environmental measures and transfers can also feature in these sorts of agreements.

21. Adopting an approach to scheduling commitments which may not sufficiently encourage transparency does not facilitate the Doha mandate. On the other hand, with a commitment on the part of developed countries for technical assistance in the drafting of reservations and schedules, as well as a recognition, again consistent with Doha (para. 22), that developing country obligations and commitments will be commensurate with their individual needs and circumstances, we would maintain that it is premature to close the door to pro-transparency scheduling mechanisms.

V. CONCLUSION

22. As it is in most IIAs and the WTO system already, non-discrimination must remain the cornerstone of any prospective investment agreement in the WTO. There is a strong case for treating national treatment and MFN in tandem. Exceptions to this treatment in specified sectors for development or other purposes would be permitted.

23. Canada is flexible with respect to how exceptions and commitments to non-discrimination are structured. In this paper we have sought to illustrate some of the practical advantages of an MFN/national treatment-type list approach, particularly with respect to non-discrimination, transparency, and the approach to reservations and exceptions. Nonetheless, whatever option is ultimately chosen, we must do so fully cognisant of its implications for the WTO system. The architecture embodied in an MFN/national treatment type agreement offers a number of advantages and can assist in the development of a WTO agreement on investment, as well as the integration of developing countries more fully into the international trade and investment framework in the WTO.

24. Finally, it is acknowledged that scheduling commitments and exceptions for developing countries under an MFN/national treatment type agreement will require technical assistance from developed countries. This would be a highly productive means of assisting developing countries in becoming more integrated participants in the world economy as envisioned at Doha. Ultimately, such an approach could also assist in the development of an investment agreement fully consistent with existing WTO disciplines, including those agreements within it with a direct bearing on investment behaviour already.

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