



Negotiating Group on the Multilateral Agreement on Investment (MAI)

Drafting Group No.3 on Definition, Treatment and Protection of Investors and Investments

DEFINITION OF INVESTOR AND INVESTMENT

(Note by the Chairman)

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The main focus of the December meeting will be the definition of “investors” and “investment”. The Chair proposes to focus on the following items (the paragraph references in parentheses refer to the Commentary section of the “Consolidated Texts and Comments” [DAFFE/MAI(96)16/REV1] reproduced in an attachment to this Note).

Regarding the definition of “investment”, the discussion on the “positive/negative” list issues should take account of the advice of EG5 on Financial Matters which will consider aspects of this issue on 5-6 December.

A. Definition of Investor

1. Nationality of the Investor (para.1)
2. Branches (after advice by EG5) (para. 3)
3. Contracting Party (para. 6).

B. Definition of Investment

4. Negative List (after advice by EG5) (paras. 7-9, 12-13, 25, 27-28).

- | | | |
|------|--------------------------------|----------------|
| i) | Claims to money... | (paras. 32-34) |
| ii) | Traded goods | (para. 33) |
| iii) | Public debt... | (para. 28) |
| iv) | Foreign exchange operations... | (EG5) |
| v) | “Financial operations” | (EG5) |
| vi) | Derivatives | (EG5) |
| vii) | Real estate... | (para. 41). |

“Footer...” to the negative list.

“Header...”, to the negative list.

5. Positive List

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|------|--|----------------|
| iii) | Other forms of debt and rights derived therefrom | (paras. 26-28) |
| iv) | Rights under contracts | (paras. 30-31) |
| v) | Claims to money | (paras. 32-34) |
| vi) | Intellectual Property Rights | (paras. 35-36) |
| vii) | Concessions | (paras 37-40) |

“Footer...” to the positive list.

6. Change in the form of an investment (para. 43)

EXTRACTS FROM DAF/FE/MAI(96)16/REV1

A. CONSOLIDATED TEXTS

I. DEFINITIONS

1. Investor means:

(i) a natural person having the nationality of, or who is permanently residing in, a Contracting Party in accordance with its applicable law; or

(ii) a legal person or any other entity constituted or organised under the applicable law of a Contracting Party, whether or not for profit, and whether private or government owned or controlled, and includes a corporation, trust, partnership, sole proprietorship, [branch], joint venture, association or organisation.

2. Investment means:

(a) Every kind of asset owned or controlled[,] directly [or indirectly,] by an investor, including¹:

(i) an enterprise (being a legal person or any other entity constituted or organised under the applicable law of the Contracting Party, whether or not for profit, and whether private or government owned or controlled, and includes a corporation, trust, partnership, sole proprietorship, branch, joint venture, association or organisation);

(ii) shares, stocks or other forms of equity participation in an enterprise, and rights derived therefrom;

(iii) bonds, debentures, loans to and other form of debt [of an enterprise]; [and rights derived therefrom];

(iv) rights under contracts, including turnkey, construction or management contracts, production or revenue-sharing contracts, [or concession contracts];

(v) claims to money, and claims to performance pursuant to a contract [associated with an investment] [having an economic value];

(vi) intellectual property rights;

(vii) [rights conferred pursuant to law such as concessions, licenses, and permits] **or [any rights conferred by law or contract or by virtue of any concessions, licenses or permits to undertake any economic activity];**

¹ Pending final determination of the scope and content of the agreement, one delegation reserves its position as to whether the positive list should be open or closed.

- (viii) any other tangible and intangible, movable and immovable property, and any related property rights, such as leases, mortgages, liens and pledges,

[unless such assets lack the characteristics of an investment.]

[(b) Except for the purposes of expropriation and compensation and protection from strife [and transfers]] "Investment" does not include [*inter alia*]²

[(i) claims to money that arise solely from commercial transactions[, including the extension of credit,] for the sale of goods or services;]

[(ii) traded goods;]

[(iii) public debt;] [debt securities and loans of a state enterprise or Contracting Party;]

[(iv) foreign exchange operations;]

[(v) "*financial operations*";]

[unless the transactions [to which such [claims, goods, debt, or -----] relate] otherwise have the characteristics of an investment; or]

[unless the respective claims are assets of an enterprise mentioned in paragraph (a) (i); or]

[unless such assets are acquired for the purpose of establishing lasting economic relations with an enterprise; or]

[(vi) derivatives where the underlying asset is not regarded as an investment],

(vii) [real estate or other property, tangible or intangible, not acquired in the expectation or used for the purpose of economic benefit or other business purposes] or [moveable or immovable property, and any related rights, acquired for personal use.]

² One Delegation proposed to include a generic phrase at the head of the negative list.

B. CONSOLIDATED COMMENTS

I. DEFINITIONS OF “INVESTOR” AND “INVESTMENT”

The definitions of “investor” and “investment” need to be carefully reviewed for consistency with text elsewhere in the agreement, and for grammatical precision, including the use of the words “and” and “or”.

Investor

1. One delegation noted that the use of the word “nationality” may require the development of an annex to the MAI in which participants would be able to clarify the meaning of “nationality” in terms of their respective domestic laws.

2. Some delegations expressed concerns relating to the inclusion of permanent residents in the definition of investor. If permanent residents are included, it would be necessary to specify that permanent residents would be those that are recognised as such under the applicable law of each Contracting Party. Concerns relating to their standing for purposes of dispute settlement could be addressed in the MAI provisions dealing with dispute settlement.

3. Some delegations questioned the inclusion of branches in the definition of investor as in their countries branches do not have the legal capacity to make investments. Other delegations expressed concern that including branches in the definition of investor could give rise to a “free-rider” problem. **DG3 identified three options:**

(a) **Include branches in list with an interpretative statement, which might read³:**

“Whether such an entity can be an investor will depend upon its legal capacity to make an investment on its own behalf under the law of the Contracting Party under which it is constituted or organised and the law of the Contracting Party in which the investment is to be made.” or

(b) **Include branches in the definition and permit country specific reservations; or**

(c) **Delete the reference to branches in the list in the definition of investor and add “within the limits of its legal capacity”.**

Options (a) and (b) are of the same nature, with only a difference in method: the conditions under which branches would be included could be expressed in a general interpretative note and/or through country specific reservations. Expert Group N°5 on Financial Services Matters should be asked to look at this.

4. **The issue of sole proprietorship has been raised by one delegation, but not discussed.**

5. **One delegation proposed to add the words “of a Contracting Party” after “legal person” in the definitions of “investor” and “investment” to cover the case of enterprises which may operate,**

³ Work needs to be done on the language of this interpretative statement.

but which are not constituted, in accordance with the applicable law of a Contracting Party. DG3 recognised the point raised by the delegation. Most delegations believed that these enterprises would be covered by the existing texts. If necessary, a possible solution could be found in adding the words “or operating” after “constituted or organised” in the definitions of investor and investment.

6. Some delegations suggested that further consideration be given to the possible need for, or desirability of, including in the definition of investor an additional item to cover a Contracting Party (i.e. a State).

Investment

7. The Drafting Group examined a definition of investment on the assumption that the MAI would contain a single, broad definition covering all forms of assets, including tangible and intangible assets. The consideration of such a definition does not prejudge the scope of its application to the various MAI rights and obligations.

8. While the question of the scope and application of the MAI is still to be resolved, the Drafting Group made the following observations. There was consensus in favour of applying a broad definition with respect to the MAI obligations to protect existing investments; however, several delegations expressed concern over how the MAI obligation concerning national treatment would apply in the pre-establishment phase. Some delegations consider that an unqualified application of this obligation to a broad range of assets could interfere with regulations of financial markets and other operations which are not meant to be covered by the MAI. One delegation also considered that an unqualified application would cause confusion with respect to the precise contents of obligations in the pre-establishment phase.

9. To address this concern while maintaining a broad and single definition under the MAI, specific reservations could be lodged wherever a country is not in a position to fully accord national treatment or other MAI obligations. [...]

10. It was noted that NAFTA and the GATS have special provisions concerning financial services, including provisions relating to prudential matters. [...]

11. The draft definition of investment defines investment in terms of assets and includes an illustrative list of assets so as to cover all recognised and evolving forms of investment. The definition would include the products of an investment.

12. DG3 agreed on the structure of the article on the definition of investment, i.e. a broad positive list and a limited negative list. There was also agreement on the categories to be included in the negative list, i.e. trade-related transactions (i) and (ii), public debt (iii), foreign exchange operations (iv) and derivatives (vi), real estate for personal use or non-business purposes (vii). For these items the drafting needs to be refined.

13. For financial operations (items iv), v) and vi)), advice is requested from Expert Group N° 5 with the aim of better defining the nature of the transactions that must be excluded.

14. Some delegations are concerned that a broad definition of investment might result in a proliferation of dispute settlement claims. If necessary, this concern can be addressed by limiting access to the MAI dispute settlement mechanism, either through a provision in the dispute settlement article or through limitations in the definition itself.

15. Views differ on whether the definition of investment should cover investments indirectly owned or controlled by investors of a Party. Some delegations are of the opinion that covering such investment offers maximum protection to investors, including access to MAI dispute settlement. In addition, those delegations believe that this approach offers the most flexibility to investors in managing their capital flows, and avoids diverting investment flows from developing countries. **The Group considered four cases:**

- (a) **investment by an investor established in another MAI Party, but owned or controlled by a non-MAI investor**

(Example: an investment in Austria by a Belgian subsidiary of a non-MAI parent)

- (b) **investment by an investor established in a non-MAI Party, but owned or controlled by a MAI Party investor**

(Example: an investment in Canada by a non-MAI subsidiary of a Danish parent);

- (c) **investment by an investor established in another MAI Party, but owned or controlled by an investor of a third MAI Party**

(Example: an investment in France by a German subsidiary of a Hungarian parent); and

- (d) **investment in a MAI Party by an investment there covered by the MAI**

(Example: an investment in Italy by an Italian subsidiary of a Japanese parent).

16. There was a broadly shared view that case (a) investments should be covered by the MAI. Most delegations favoured providing for certain exclusions in a denial of benefits clause which would permit, but not require, exclusion. Some delegations were concerned about possible abuse of this provision. It was suggested that the condition for exclusion would be where the MAI investor lacked substantial business activity in the MAI Contracting Party. One delegation suggested limiting this to cases in which the investor was constituted “for no other purpose than obtaining MAI benefits” (exact wording not finalised).

17. There was wide support for covering case (b) investments; however, whether to do so was considered a policy issue to be considered by the Negotiating Group.

18. Related to it was the question of standing for MAI dispute settlement on which the Negotiating Group might provide guidance to Expert Group N°1. Under investor-state proceedings, most delegations considered that only the parent MAI investor would have standing, but some delegations were open to allowing the intermediary entity to have standing as well. Under state-to-state proceedings, all delegations suggested, as a matter of principle, giving no standing to the non-MAI government of the intermediary.

19. There was consensus that case (c) and case (d) investments would be covered by the MAI. There was no further debate on the legal implications.

20. Related to each of these cases was the question of which entities and states have standing for MAI dispute settlement, an issue for consideration by Expert Group N°1. This includes which

tier or tiers of investors have standing in investor-state dispute settlement and which MAI Party (state or states) have standing in state-to-state dispute settlement.

21. One delegation considered that the inclusion of indirectly controlled investments might pose serious problems to the REIO Members states as far as their present level of liberalisation is concerned as this normally also applies to companies established in the REIO, but under control of a non-REIO country. The delegation suggested that such problems could eventually be effectively addressed by a general MAI provision on measures taken within Regional Economic Integration Agreements.

* * *

22. Most delegations would prefer the definition of investment to be an open one, **hence** the word “including” in the chapeau [...].

Item (i)

An enterprise (being a legal person or any entity constituted or organised under the applicable law of a Contracting Party, whether or not for profit, and whether private or government owned or controlled, and includes a corporation, trust, partnership, sole proprietorship, branch, joint venture, association or organisation).

23. The term “enterprise” is defined in parenthesis in the proposed text but could be defined separately. It was agreed that the definition covers, inter alia, scientific research institutes and universities. Most delegations favoured the same definition of enterprise for “investor” and “investment”. It was also proposed to define “enterprise of a Contracting Party”.

24. Some delegations questioned whether “government owned or controlled enterprises” should be considered “investments”. Separately, some delegations thought that the notion “whether private or government owned or controlled” should be deleted given that ownership and control are dealt with in the chapeau.

Item (ii)

Shares, stocks or other forms of equity participation in an enterprise, and rights derived therefrom;

25. This item, as well as item (iii), includes portfolio investment and minority holdings. It is for consideration whether the definition covers strategic alliances and other arrangements involving know-how, intellectual property, or technology or the joint conduct of research and development programmes. This item is also understood to cover an interest in an enterprise that entitles the owner to share in income and profits of an enterprise and its assets. The extent to which the substantive obligations of the agreement will apply to this item and to item (iii), in particular portfolio investment and foreign exchange operations, will need further examination in the light of concerns expressed by some delegations.

Item(iii)

Bonds, debentures, loans to and other forms of debt of an enterprise;

26. This item would cover loans of all maturities and debt securities of a state enterprise.
27. One delegation wishes to exclude loans of less than three years, other than loans between affiliates of an enterprise. Other delegations consider that this issue requires further consideration.
28. Some delegations consider that sovereign debt should not be included, while others believe that including sovereign debt (which includes state-owned enterprise debt) requires further consideration. One element to be considered in this respect would be the sovereign liquidity issue. Some delegations pointed out that confiscatory measures by a debtor state entail international responsibility which should be dealt with in the MAI.

Item (iv)

Rights under contracts, including turnkey, construction or management contracts, production or revenue-sharing contracts, [or concession contracts];

29. Some delegations thought that items (iv) and (v) should be combined. Some delegations proposed deleting “concession contracts” from item (iv) and to address the question of concessions in a revised item (vii).
30. It was also suggested, by several delegations, to add a reference to franchising, licensing and “BOOT” agreements.
31. Some delegations wish to retain, for further consideration, a previous text for item (iv) which would read as follows:

“an interest arising from the commitment of capital or other resources in the territory of a Contracting Party to economic activity in such territory, such as under

-- contracts involving the presence of an investor’s property in the territory of a Party, including turnkey or construction contracts, or concessions, or

-- contracts where remuneration depends substantially on the production, revenues or profits of an enterprise.”

Item (v)

Claims to money, and claims to performance pursuant to a contract [associated with an investment] [having an economic value];

32. “Claims to money” includes bank deposits. Most delegations consider that this item covers derivatives which are not covered elsewhere in the list of assets.
33. Claims to money may also arise as a result of a sale of goods or services. These claims are not generally considered as investments. The NAFTA excludes such claims unless they are associated with

the investment interests which are set out in its definition. The ECT also requires that these claims be associated with an investment. Similar questions arise with respect to “rights under contracts” (item iv).

34. One delegation proposed to address these matters in the MAI by adding the words “associated with an investment” and deleting the words “having an economic value”. Some delegations supported the following alternative text:

“Claims to money and claims to performance pursuant to a contract [associated with an investment] having an economic value, with the exception of :

(a) Commercial contracts for the sale of goods or services by a national or enterprise in the territory of a Contracting Party to an enterprise in the territory of another Contracting Party;

(b) the extension of credit in connection with a commercial transaction, such as trade financing, other than a loan covered by item (iii); or;

(c) any other claims to money that do not involve the kinds of interests set out in items (i) through (ix).”

Delegations felt that these matters merit further consideration.

Item (vi)

Intellectual property rights;

35. All forms of intellectual property are included in the definition of "investment," including copyrights and related rights, patents, industrial designs, rights in semiconductor layout designs, technical processes, trade secrets, including know-how and confidential business information, trade and service marks, and trade names and goodwill. Views differed on whether it is necessary to specifically refer to some of these elements in the definition as part of the illustrative list of assets. Some delegations consider that the question of whether to include “literary and artistic property rights” has not yet been decided. One delegation wishes to cover intellectual property rights under the MAI only when acquired in the expectation of economic benefit or other business purposes.

36. Further work may be needed to clarify the relationship of the MAI to other international agreements that relate to intellectual property, particularly where these conventions might require standards of treatment which differ from the MAI or where these conventions provide for dispute settlement mechanisms.

Item (vii)

[Rights conferred pursuant to law such as concessions, licenses, and permits;] or [**any rights conferred by law or contract or by virtue of any concessions, licenses or permits to undertake any economic activity**]

37. Rights such as concessions, licenses and permits are generally meant to cover rights to search for, cultivate, extract or exploit natural resources. Most bilateral treaties, and the ECT, refer to rights conferred by law or under contract and extend protection to such rights. One delegation considered that this item covers public law contracts.

38. Most delegations preferred to keep concessions in the definitions and to require reservations by any country wishing to discriminate in granting concessions. Some delegations were of the opinion that the issue of the granting of concessions should be kept outside the definition of investments.

39. Some delegations indicated that certain aspects of concessions raised issues related to monopolies in general and to cross-border government procurement, which might require some special provision or clarification in the MAI.

40. Further work will be necessary, bearing in mind that some delegations believe it is necessary to determine whether the rights conferred by virtue of concessions, or the concession as such, are separate elements under the definition of investment.

Item (viii)

any other tangible and intangible, moveable and immovable property, and any related property rights, such as leases, mortgages, liens and pledges.

41. This category includes real estate which is a common form of property protected under BITs, the ECT and NAFTA. There are different views on item (viii) including whether the definition should cover summer residences or second homes. NAFTA, however, excludes real estate or other property which is not acquired in the expectation, or used for the purpose, of economic benefit or other business purposes, and some delegations prefer such an approach.

-- Other Elements

42. Some delegations consider that the MAI should include “returns, or “reinvested returns” as part of the definition of investment as in the ECT.

43. One delegation expressed the view that changes of activities of an investment should also be taken into consideration.

[....]