



Negotiating Group on the Multilateral Agreement on Investment (MAI)

Expert Group No.3 on “Special Topics”

MONOPOLIES/STATE ENTERPRISES

(Note by the Chairman)

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I. Introduction

1. The existence of a monopoly is not contrary to National Treatment since both domestic and foreign investors face the same " market access limitation" to the investment opportunities captured by the monopoly.
2. In considering the possible nature and scope of MAI obligations on monopolies and state enterprises, the Expert Group focused on the questions of whether and how the actions taken by government-designated monopolies could interfere with or frustrate the effective application of the National Treatment and MFN Treatment obligations. It also examined the issue of Transparency.
3. Great care was taken in limiting the analysis to the field of investment policy and to avoid undue encroachment in other areas, in particular trade policy, competition policy and government procurement policy.

II. Monopolies

1. Definition

4. The need for a definition on monopolies was considered to be closely related to nature of the MAI obligations in this area. If a specific provision was drafted, a definition would be required for the understanding of the obligations.
5. There was agreement that the focus should be on government-designated monopolies. Some aspects for describing these entities could be found in Article XVII of the GATT on State Trading Enterprises¹, Article VIII of the GATS² and Article 1505 of NAFTA³. Caution should be exercised,

1 Article XVII of the GATT defines a state enterprise as "government and non-government enterprises (...) which have been granted exclusive or special rights or privileges, including legal or constitutional powers (...).

2 Under the GATS, a "monopoly supplier of a service" means "any person, public or private, which in the relevant market of the territory of a Member is authorised or established formally or in effect by that Member as the sole supplier of that service". The GATS also covers the cases of "exclusive service suppliers, where a member formally or in effect, (a) authorises or establishes a small number of suppliers and (b) substantially prevents competition among those suppliers in its territory".

3 Under NAFTA, a monopoly means "an entity, including a consortium or government agency, that in any relevant market in the territory of a Party is designated as the sole provider or purchaser of a good or service". It covers therefore any monopoly permitted or regulated in some manner by the government. NAFTA excludes however from the concept of monopoly " any entity that has been granted an exclusive intellectual property right solely by reason of such grant or monopolies based on "natural advantage".

however, not to take the definitions found in these agreements out of context since they were not drafted with the sole investment perspective in mind and, indeed, embodied trade and competition elements.

6. A number of delegations were attracted by a definition of monopolies that would include "any person, public and private, designated by a government authority as the sole supplier or buyer of a good or service in a given market in the territory of a Contracting Party." This person may be a natural person, an enterprise, a consortium, a state enterprise, or a government agency. There was also some support for including the notion of a "limited" number of suppliers which are substantially prevented from competing amongst each other by a Contracting Party. This again would depend on the question of designation by government authorities.

7. The Expert Group took note of the explanation provided by one NAFTA delegation as to why the NAFTA definition of a monopoly excludes "any entity that has been granted an exclusive intellectual property right solely by reason of such grant". Patents are not granted to transfer regulatory powers, but to protect intellectual property rights. This is a different issue from discrimination that may result from the exercise of delegated powers by government-designated monopolies. The Expert Group also took note that the NAFTA definition excludes monopolies solely based on a "natural advantage".

8. The Expert Group also had a brief discussion on the definition of concessions and whether this subject could be considered to fall in the area of monopolies or private investment. The Expert Group agreed with the position of one delegation [DAFFE/MAI(96)RD(96)11] that this was an important issue and need to be addressed on its own merits. It was noted that concessions is one of the items listed in the proposed definition of "investment" in the MAI.

2. *Possible obligations on Monopolies*

a) To act in a manner not inconsistent with the Agreement

9. There was an emerging consensus that the Contracting Parties of the MAI could not escape their obligations by delegating one or several of their regulatory, administrative or other governmental powers to a government-designated monopoly. **This is a distinct issue from that of the designation of monopolies [see section d) below].** This interpretation would be fully consistent with the MAI objective to discipline discriminatory treatment against foreign investors and their investments. **One delegation stressed that delegated powers should cover sub-national as well as national authorities.**

10. A majority of delegations considered that this understanding could take the form an anti-circumvention clause which could be developed around Article 1502.3a) of NAFTA:

"Each Contracting Party shall ensure, through regulatory control, administrative supervision or the application of other measures, that any monopoly it maintain or designates acts in a manner that is not inconsistent with the Contracting Party's obligations wherever such monopoly exercises any regulatory, administrative or other governmental authority that the Contracting Party has delegated to it in connection of the monopoly good or service".

11. **A few** delegations reserved their position on the grounds that the obligations of the MAI have not all been defined and that it would be more appropriate to discuss this proposal at a later date. A number of delegations noted that the core obligations of the MAI (National Treatment and MFN, in particular) have already been sufficiently defined. **One delegation wondered if the language "not being inconsistent with the Contracting Parties" obligations was precise enough to avoid different**

interpretations. One delegation wondered whether an anti-circumvention clause would be necessary at all given the possible recourse to dispute settlement. It admitted, nevertheless, that this would facilitate the interpretation of the MAI. **It was also pointed out that the desirability of an anti-circumvention clause may not need be limited to monopolies.**

12. The Expert Group also discussed the option of extending the scope of the anti-circumvention clause to every action taken by government-designated monopolies, and not only those resulting from delegated powers. This is the approach of Article VIII of the GATS. A large majority of delegations considered, however, that the GATS language was not directly transferable to an investment agreement such as the MAI because it covers other modes of operation and, more particularly, cross-border trade. If the MAI were to cover the general behaviour of monopolies, it would inevitably enter the field of competition policy. One delegation argued this option could not be entirely discarded at this stage.

b) Purchase and sale practices of monopolies

i) Purchases

13. It was generally recognised that the purchase practices of government-designated monopolies ought to be handled under the GATT Government Procurement and that there would be no value added in reproducing its provisions in the MAI. The procurement policies of monopolies would appear to be of more direct interest to the trade field than to investment field. There was also no interest for discussing the purchase practices of other types of monopolies (natural monopolies, de facto monopolies).

14. One delegation indicated its readiness to go beyond the understandings reached in the WTO through the incorporation into the MAI of a non-discrimination provision for government-designated monopolies, provided other delegations would be prepared to do the same. In its view, the purchase practices of monopolies can also have a major impact on the choice of the investment activities that foreign investors may undertake in a given country.

15. There was wide support to apply the MAI obligations to the monopolistic purchases of certain government-designated monopolies not uncommon in certain sectors (marketing boards in agriculture, energy...). It was noted that this is translated, in NAFTA article 1502.3(c), in the obligation:

"to ensure, through regulatory control, administrative supervision or the application of other measures " that any government-designated monopoly provides "non-discriminatory treatment to investments of investors, to goods and to service providers of a another Contracting Party in its purchase ... of the monopoly good or service in the relevant market".

16. Two delegations reserved their position on this proposal.

17. The Expert Group was not inclined to consider a broader provision along the lines of article 1502.3(b) that would require government-designated monopolies "to act solely in accordance with commercial considerations in its purchase of the monopoly good or service in the relevant market". Some delegations wondered how a government-designated monopoly could be obliged to act according to "commercial" considerations since, by definition, its operations are not subject to market rules.

ii) Sales

18. A majority of delegations thought the MAI should contain a non-discrimination provision covering the sales practices of government-designated monopolies regarding monopoly goods or services. Equal access to raw material (coal, oil...) or infrastructure services (water, electricity transmission, railways, roads services) was mentioned as an essential component to the viability of a business operation.

19. One delegation argued that such an obligation should follow automatically from the application of the anti-circumvention clause discussed in section II.a and that it would be superfluous to create another layer of clarifications. A few delegations argued that, on the contrary, a specific provision was needed since the non-discrimination obligation they had in mind would not be limited to situations where a monopoly acts on behalf of a public authority, but to every sale of the monopoly good or service in the relevant market. One delegation suggested that "*de facto*" or "natural monopoly" goods or services should be covered as well by this obligation.

20. One delegation could not understand why the MAI needed to be concerned with this issue since it was normally covered by national competition rules, at least in OECD countries. One delegation indicated it could not subscribe to a full-fledged non-discrimination provision in this area given the special circumstances (shortage of supply...) that may be encountered in the provision of a monopoly good or service. Two other delegations noted that such concerns might be taken care of by differentiating between private consumers and investors.

21. For the same reasons as those recalled in section i) above, the Expert Group decided not to pursue the idea of including an additional provision along the lines of article 1502.3(b) that would require government-designated monopolies to act solely in accordance with "commercial considerations" with respect to their sales of monopoly good or services.

c) Abuse of dominant position

22. A consensus emerged that the issue of the abuse of dominant position by monopolies could not be adequately tackled within the time available for the MAI negotiations and that it should not be pursued further by the Expert Group. This subject clearly belongs to the competition policy field.

23. It was acknowledged during the discussion that monopolies have the capacity to interfere with an investor's rights and to introduce market distortions, notably by cross-subsidising their business activities in competitive sectors. The impact of these practices may, in fact, be as detrimental to foreign investment as the exercise of delegated regulatory powers. It would be desirable, however, to leave these problems to competition policy.

24. This would not preclude that they be considered at a later stage after the MAI enters into force. They could not, in any case, be dealt with under a single article on abuse of dominant position. Competition policy experts would necessarily need to be involved. One delegation agreed that the proposals it has made on the separation of monopolistic and non-monopolistic activities [DAFFE/MAI/RD(96)11] could be addressed in that context **provided the treatment of monopolies in the MAI is deemed overall to be satisfactory.**

d) Right to designate a monopoly and demonopolisation rules

25. The Expert Group agreed that the right of governments to create, allow or maintain monopolies could not be challenged under the MAI. Governments shall also remain sovereign with respect to "demonopolisation" matters.

26. Using similar arguments as those made during the privatisation discussion [DAFFE/MAI(96)5]), a few delegations expressed a preference for the inclusion of a declaratory provision in the MAI recognising these sovereign rights. It would provide the assurance that they could not be questioned under the dispute settlement provisions of the MAI.

27. One delegation suggested that the need for a specific provision might be more obvious should the MAI contain market access disciplines. Another delegation commented that even in such case, the sovereign rights of governments could not be challenged.

28. The Expert Group also discussed the merits of clarifying the rules pertaining to access to investment opportunities created during a demonopolisation process. A number of delegations considered this to be unnecessary since the National Treatment and MFN obligations would start to apply as soon as a given monopoly is broken down. Some delegations felt that it would be useful to confirm explicitly the application of the National Treatment and MFN provisions to these new situations in view of the fact that market access to demonopolised activities has been traditionally be subject to reciprocity.

29. Other delegations felt this interpretation needed further reflection given the political sensitivity of certain demonopolisation activities. An unqualified application of National Treatment could not be contemplated in the absence of a proper balance between the liberalisation commitments of the Contracting Parties. One delegation reserved its position over a possible abandonment of reciprocity in the context of demonopolisation.

30. It was recognised that some of these concerns could be taken care of in the context of the Contracting Parties's individual reservations to the MAI. One delegation argued that demonopolisation would provide the Contracting Parties with the opportunity to make positive liberalisation commitments during the negotiations. It also was of the view that in the absence of country-specific reservations, the National Treatment and MFN obligations would automatically apply to the new investment opportunities created by demonopolisation. **One delegation recalled that the Drafting Group N°3 had agreed that if MAI obligations were expanded, new reservations would come into play with respect to the new or enlarged obligations⁴.** There was, however, no definite conclusion; delegations agreed to pursue the discussion.

III. State enterprises

31. A large majority of delegations considered that state enterprises would not deserve special attention under the MAI unless they exercise a delegated governmental authority. There is no apparent need for separate provisions on state enterprises since it should prove possible to regroup eventual obligations on delegated governmental authority under a single heading.

4 See DAFTE/MAI(96)16, paragraph 1.3.

32. The issue in this case⁵ is how to ensure that Contracting Parties do not escape their MAI obligations as a result of the powers transferred to state enterprises. The general view was that this problem could be resolved by a general anti-circumvention clause, such as the one envisaged for government-designated monopolies.

33. One delegation reserved its position on the eventual extension of the MAI to state enterprises exercising delegated regulatory, administrative or other governmental authority. **This delegation wanted to make sure that only industrial and commercial activities would be covered.** Another delegation felt that the anti-circumvention clause should also apply to private enterprises exercising a governmental authority since these entities too could be used to circumvent the MAI. The model provided by the Energy Charter would appear to be preferable to the NAFTA model.

34. Delegations did not come to a definite conclusion as whether the MAI should be concerned by the actions taken by the state as a shareholder in a company. It was recognised that these actions could be dictated by genuine business consideration, but they could also provide ground for discrimination against foreign investors. One delegation argued that the state could not escape its MAI obligations when exercising its ownership rights, particularly when holding a controlling interest in the enterprise.

35. A large majority of delegations considered that the MAI should not include a provision applying to the purchases and sales practices of state-owned enterprises. The Agreement should not, in their view, duplicate or attempt to improve upon the GATT Government Procurement Agreement. One delegation felt that the question of overlap with the GATT Agreement needs to be carefully examined before ruling-out any MAI involvement in this area.

IV. Transparency

36. A number of delegations were of the view that the MAI should contain specific transparency rules for monopolies above those already foreseen by the general transparency article of the MAI [section II.2 of DAF/MAI(96)16]. Notification of government-designated monopolies could help assess their economic importance and signal to foreign investors the economic activities excluded from normal competition.

37. Notification requirements could be limited, however, as with OECD instruments, to existing or new government-designated monopolies, but should not extend to state enterprises operating in a competitive environment.

38. It would also appear logical to envisage the same transparency rules for privatisation and demonopolisation. They could eventually be combined into one single provision.

39. Some caution was expressed about not overburdening Contracting Parties with reporting obligations. It would be wise to hold off final judgement on transparency rules for monopolies (and demonopolisation and privatisation) until agreement is reached on the general transparency article and the role of the Parties Group.

5 It should not be confused with the treatment accorded to state enterprises as "investors" of a Contracting Party and the obligations the Contracting Parties have contracted themselves under the MAI. The proposed inclusion of "a legal person or any other entity constituted or organised under the applicable law of a Contracting Party...whether ...government owned or controlled" into the MAI definition of "investor" [Section A.1 of DAF/MAI(96)16] implies that state enterprises would be entitled to all the benefits of the MAI.