



## POLICY FRAMEWORK FOR INVESTMENT USER'S TOOLKIT

## Chapter 1. Investment Policy

**Introductory note**

The PFI User's Toolkit responds to a need for specific and practical implementation guidance revealed from the experience of the countries that have already undertaken a PFI assessment.

Development of the Toolkit has involved government users, co-operation with other organisations, OECD Committees with specialised expertise in the policy areas covered by the PFI and interested stakeholders.

This document offers guidance relating to the PFI chapter on Investment Policy.

The PFI User's Toolkit is purposely structured in a way that is amenable to producing a web-based publication. A web-based format allows: a flexible approach to providing updates and additions; PFI users to download the guidance only relevant to the specific PFI application being implemented; and a portal offering users more detailed resources and guidance on each PFI question. The website is accessible at [www.oecd.org/investment/pfitoolkit](http://www.oecd.org/investment/pfitoolkit).



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## ***Investment Policy***

Investment policy in the PFI relates to a country's laws, regulations and practices that directly enable or discourage investment and that enhance the public benefit from investment. It covers, for instance, policies for transparent and non-discriminatory treatment of investors, expropriation and compensation laws and dispute settlement practices.

The quality of a country's investment policies directly influences the decisions of investors, be they small or large, domestic or foreign. Transparency, property protection and non-discrimination are core investment policy principles that underpin efforts to create a quality investment environment for all.

Investors are also concerned with the way that investment policy is formulated and changed. They will avoid circumstances where policies are modified at short notice, where governments do not consult with industry on proposed changes and where laws, regulations and procedures are not clear, readily available and predictable.

The PFI Investment Policy chapter identifies through eight questions the most important issues relevant for judging the effectiveness of a country's investment policies and practices. The issues are often directly relevant to the specific needs of foreign investors, but they apply in most instances to domestic investors as well. This section of the Toolkit offers additional detail on why these investment policy questions are important, and specific guidance on the topics to scrutinise in order to form an opinion on how well a country's investment policies perform vis-à-vis good practices.

The eight PFI questions on Investment Policy relate to:

- Laws and regulations
- Effective ownership registration
- Intellectual property rights
- Contract enforcement and dispute resolution
- Expropriation laws and review processes
- Non-discriminatory treatment for national and international investors
- International co-operation and periodic review
- International arbitration instruments

## **Laws and Regulations**

1.1 *What steps has the government taken to ensure that the laws and regulations dealing with investments and investors, including small- and medium-sized enterprises, and their implementation and enforcement are clear, transparent, readily accessible and do not impose unnecessary burdens?*

### **Rationale for the question**

Policy uncertainty encompasses both predictability and transparency and is one of the greatest obstacles to investment. Firms need to know what the rules of the game are and require some assurance that those rules will not change once they have invested. Their views, along with other stakeholders, should also be solicited when policies are being developed or revised. Going beyond the rules and regulations themselves, their implementation and enforcement should be clear and transparent. Investors need to understand the practical implications of rules governing their investment, in terms of the conditions to fulfil, the procedures for a public review and the appeals process in the event of a dispute. This process can help to institutionalise procedural transparency by systematically ensuring that changes in implementing regulations and administrative decisions are subject to public review and appeals.

Rules and procedures should be designed in a way which achieves stated policy goals while imposing the least cost on investors in terms of red tape. Unnecessary administrative burdens can be a significant cost for potential investors, especially for small and medium-sized enterprises (SMEs), and can help to account for both a low level of investment and a high share of SMEs in the informal sector where rules can more easily be circumvented.

### **Key considerations**

To promote investment, governments can consult with interested parties, simplify and codify legislation, use plain language drafting, develop registers of existing and proposed regulations, disseminate regulatory material electronically, and publish and review administrative decisions.

#### **Availability of relevant information to investors**

Information is the lifeblood of well-functioning markets. Meaningful information on all measures materially affecting a firm's investments should be readily available, and to reassure all market participants that business operates on a level playing field, investment laws and regulations and their enforcement should be codified and clear to all.

This requires a consistent, predictable system of laws, policies, regulations and administrative practices, as well as information on rulings and judicial decisions.

While the sheer number and complexity of laws and regulations may not always make it possible to provide comprehensive information on all matters that might influence investor decisions, governments have an interest in providing essential information on how to start a business and inform investors, *i.a.* about ownership and exchange control restrictions, administrative requirements, taxation, investment incentives, monopolies and concessions, intellectual property protection and competition policy, as well as environmental and social requirements and corporate responsibilities.

*Prior notification and consultation*

Involving investors and other stakeholders in the process of legal and regulatory changes contributes to their legitimacy and effectiveness. It also reflects a commitment to professionalism and contributes to building trust between investors and relevant stakeholders. Moreover, policy is more likely to be sound and not produce unintended side effects if it is structured and transparent and permits input from all interested parties. Prior notification and consultation is a process that begins with public hearings, policy papers outlining the reasons why changes are needed, circulation of draft regulatory changes to all concerned stakeholders, and processes for revision and recirculation based on these public inputs.

*Public appeals processes*

Public appeals processes increase procedural transparency, thereby helping both to avoid regulations that impose undue burdens and to limit the discretionary power of officials. Procedural transparency can be institutionalised by systematically ensuring that changes in implementing regulations and administrative decisions are subject to an open, prompt and impartial public review and appeals process.

## **Policy practices to scrutinise**

The [OECD Framework for Investment Policy Transparency](#) assists governments to enhance transparency of their investment policy frameworks and serves as a basis for conducting self-evaluation and sharing experiences among public officials. While the focus is on the information gaps and special needs of foreign investors, the Framework applies, in most instances, to domestic investors as well. It asks 15 questions that support a level playing field for all investors.

- *Are the economic benefits of transparency for international investment adequately recognised by public authorities? How is this being achieved?*
- *What information pertaining to investment measures is made readily available, or available upon request, to foreign investors?*
- *What are the legal requirements for making this information public? Do these requirements apply to primary and secondary legislation? Do they apply to both the national and sub-national levels? Is this information also made available to foreign investors in their countries of origin?*
- *Are exceptions/qualifications to making information available clearly defined and delimited?*
- *What are the main vehicles of information on investment measures of interest to foreign investors? What may determine the choice of publication avenues? What efforts are made to simplify the dissemination of this information?*
- *Is this information centralised? Is it couched in layman's terms? Is it in English or another language? What is the role of Internet in disseminating essential/relevant information to foreign investors?*
- *Have special enquiry points been created? Can investment promotion agencies fulfil this role?*
- *How much transparency is achieved via international agreements or by international organisations?*
- *Are foreign investors normally notified and consulted in advance of the purpose and nature of regulatory changes of interest to them? What are the main avenues? Are these avenues available to all stakeholders?*
- *Are the notice and comment procedures codified? Do they provide for timely opportunities for comment by foreign investors and accountability on how their comments are to be handled?*
- *Are exceptions to openness and accessibility to procedures clearly defined and delimited?*
- *What are the available means for informing and assisting foreign investors in obtaining the necessary licensing, permits, registration or other*

*formalities? What recourse is made to “silence is consent” clauses or a posteriori verification procedures?*

- What are foreign investors’ legal rights in regard to administrative decisions?*
- To what extent do one-stop shops assist foreign investors in fulfilling administrative requirements?*
- What efforts are being made to address capacity building bottlenecks?*

### **Further resources and case studies**

- The full publication on the OECD [Framework for Investment Policy Transparency](#) provides further information on the elements behind each question. A related OECD report on [Public Sector Transparency and the International Investor](#) offers principles of good practice for enhancing public sector transparency.
- The World Bank Doing Business project ([www.doingbusiness.org](http://www.doingbusiness.org)) studies the cost, length and complexity of various aspects of the investment climate and provides a score of how long it takes in each country for business to complete key regulatory tasks. Longer and more complex processes are one measure of unpredictability and often indicate a lack of transparency.
- The World Bank [Doing Business Law Library](#) is the largest free online collection of business laws and regulations. It offers links to official government sources covering areas such as banking and credit law, labour law, tax law, trade law and bankruptcy and collateral laws.
- The World Bank [Business License Reform Toolkit](#) offers practical advice on how to reform business-licensing regimes at the national level.

## Effective Ownership Registration

1.2 What steps has the government taken towards the progressive establishment of timely, secure and effective methods of ownership registration for land and other forms of property?

### Rationale for the question

Investors need to be confident that their ownership of, or right to use, property is legally recognised and protected. Secure, verifiable and transferable rights to agricultural and other types of land and forms of property give an incentive for investors and entrepreneurs to shift into the formal economy, entitle the investor to participate in the eventual profits that derive from an investment and reduce the risk of fraud in transactions.

An essential part of any system designed to protect property rights is the creation and maintenance of a registry of property ownership. A secure and verifiable system of property ownership rights carries an intrinsic economic value by encouraging new investment and the upkeep of existing investments. Land titles, for example, give an incentive to owners to promote productivity-enhancing investments. Reliable land titling and property registrars also help individuals and businesses to seek legal redress in case of property rights violations and offer a source of collateral, thus facilitating access to credit and on better terms. This is particularly important in rural areas where barriers to credit are more pronounced.

### Key considerations

The question focuses on tangible forms of property, like land, buildings and manufacturing plants. (Protection of intangible assets is covered in Question 1.3, since it is often governed by separate laws.)

#### *Access to the property-ownership registration system*

How well does the property registration system perform? If a formal system is not in place, how could one be designed? What obstacles deter the formal recognition of ownership of certain classes of asset (e.g. small-sized or low-valued property) or types of investor from using the registry system?

Accessibility also depends on the ease with which information on the identity of the owner and the status of the ownership interest can be retrieved from the property registry. This is useful for lenders who wish to establish if a property has already been offered as collateral and for property owners who wish to pledge their property as collateral for credit.

### *Integrity of the property registration system*

Governments have a responsibility to build and maintain confidence in the security and accuracy of the property registration system. How secure is the property registry? How well does it avoid competing and fraudulent claims to ownership? Are users confident in the accuracy of the property registry. (See also Questions 1.4 and 1.5 in this regard.)

In some countries, there is an interplay between formal and traditional processes of recognising property ownership, especially for immovable property like land. The choice of system depends on culture, history and geography. How vulnerable is the system in place to conflicts between property titling methods that harm the overall integrity of the system.

### **Policy practices to scrutinise**

Key issues when assessing the effectiveness of a country's property ownership registration systems are whether the property registration system is open to all and how well it performs.

The following policy practices and criteria ought to be considered:

- The **share of property formally registered in a country or region**. A low rate of property registration is a *prima facie* sign that the system in place to register property is not functioning well but this needs to be interpreted with care, especially in countries where property ownership is asserted and held through informal processes.
- To establish the reasons why property ownership titling is low, or limited to certain types of assets, the details of the processes involved need to be examined, including:
  - The **fees charged and taxes levied** to register or transfer a title to land and other forms of property, as well as the structure of these costs. For example, are they proportional to the value of the property or fixed in absolute terms? Do they vary according to the type and planned use of the property being registered? How do they compare with those in other countries at a similar level of economic development?
  - The **time taken** officially to register new property titles or transfer existing ones. This will depend on the number and types of procedures required, on the number of agencies (e.g. are registries limited in scope by geographic area, by type of property, by type of filing entity, by legal jurisdiction or along supervising ministries?) involved in the property registration process and when multiple agencies exist, whether they are

- linked by computer or feed into a central database. It also depends on whether the operational practices of the registrar office are capable of accepting and working with time-saving technologies, such as digitised records and online internet-based property registration; and
- The **compliance costs** of registering or transferring the title of property. This depends on the documentation requirements (e.g. providing proof of property surveys or tax payments), the number and complexity of regulatory requirements stipulated, taxes that are levied on property registration and transfer, how easily the documentation and information on all the property registration requirements is obtainable (e.g. via the internet) and whether electronic lodging is allowed. The time taken by a business or individual to register or transfer title is also a part of the cost of compliance.
  - Do **foreign individuals or corporations** have the same rights as nationals to own and register land, and, if not, do the restrictions depend on the type of land (e.g. rural, residential property or industrial real estate) or its intended use? Are the administrative and compliance procedures for foreigners more burdensome or costly than for nationals?
- When examining the practices of property registration offices it is important to obtain the views of their staff and management and users of their services. This helps to pinpoint potential organisational and management problems (e.g. human resource capacity, information technology limitations).
  - No single indicator sheds light on the integrity of the property registration system, but insights can be gained by examining the details of the dispute resolution process and their outcomes. Confidence in the system will depend on:
    - Whether entries in the registrar are open to public inspection and may be relied upon by third parties.
    - The ability to challenge the validity of an entry by filing an administrative appeal with the registrar itself or by bringing a court action against the registrar. In this case, whether the registrar office and, when called for, the judicial system provides an equitable, inexpensive and timely system for resolving property ownership disputes;
    - The incidence of fraudulent or duplicate claims to assets;
    - The number of disputes and the efficiency and speed with which they are resolved; and

- Analysis of the causes of dispute from court cases may also help to bring to light systemic weaknesses in the registrar system.
- Where traditional and formal property ownership systems co-exist, are there clear boundaries and rules that delineate between the two systems? For instance, is each system responsible for distinct, well-defined classes of property or delineated on a geographic basis?

### ***Further resources and case studies***

- One dimension of the World Bank Doing Business project ([www.doingbusiness.org](http://www.doingbusiness.org)) covers the cost, relative to the value of the property, the number of procedures involved and the average time, measured in days, it takes to register property. The information is updated yearly and is available for a large number of countries.
- Even if property ownership rights are secure and verifiable, collateral laws may act to prevent banks from accepting business assets as collateral. The World Bank has produced a toolkit on [Reforming Collateral Laws to Expand Access to Finance](#).

## Intellectual Property Rights

1.3 Has the government implemented laws and regulations for the protection of intellectual property rights and effective enforcement mechanisms? Does the level of protection encourage innovation and investment by domestic and foreign firms? What steps has the government taken to develop strategies, policies and programmes to meet the intellectual property needs of SMEs?

### Rationale for the question

Intellectual property (IP) rights give businesses an incentive to invest in research and development, fostering the creation of innovative products and processes. They also give their holders the confidence to share new technologies through, *i.a.* joint ventures and licensing agreements. In this way, successful innovations are in time diffused within and across economies, bringing higher productivity and growth.

Intellectual property has significant value and thus deserves the same types of registration and protection systems as other forms of property (see Question 1.2). But intellectual property right regimes need to strike a balance between society's interests in fostering innovation, in keeping markets competitive and, especially in the case of essential medicines, in sufficient supply.

The intellectual property rights regime is of concern not only to large firms and multinational enterprises but also to SMEs. Although SMEs are a driving force behind innovation, their potential to invest in innovation activities is not always fully exploited. They tend to under-utilise the intellectual property system. Measures to make the system more accessible may thus help to attract investment in research and development (R&D) and to transmit the positive spillovers to society that such investment embodies.

### Key considerations

The question focuses on the laws, regulations and instruments that give value to intangible forms of property. (The protection of tangible assets is covered in Question 1.2.) The main formal IP instruments cover patents, trademarks, copyright, new varieties of plants, industrial designs and geographic indications.

#### *Access to, and use of, the IP rights system*

What laws and regulations are in place to protect ownership rights to intellectual assets? How much protection and coverage do these laws provide? How efficient is the registration process in terms of costs involved and time required? Is it reliable and secure? What are the procedures for handling intellectual property that is registered in other jurisdictions?

SMEs require specific consideration: they are a major source of innovation yet they tend to under-utilise the formal IP protection system. The diversity of SMEs (*e.g.*

sectors, size, age) means that the obstacles they face using the IP system are likely to differ (e.g. high costs, limited knowledge of the system and lack of legal and technical IP expertise), as well as their needs (e.g. use of certification and collective marks). Strategies to meet the IP needs of SMEs must, therefore, take into account their specific features and characteristics.

#### *Enforcement and dispute settlement mechanisms*

As with tangible assets, for a market to function effectively, property rights must be secure, *i.e.* protected against fraud, theft and crime. Government has a responsibility to protect owners from violations of their IP rights and their citizens from abuses of IP rights. This depends on how IP rights are enforced and the mechanisms (e.g. special unit of the IP office, courts, special tribunals) to adjudicate disputes. The ability to protect IP rights is related to contract enforcement and dispute resolution, points that are also taken up in Question 1.4.

#### *An innovation policy framework*

An incentive to invest in R&D does not guarantee success in innovation. How effective the incentive that IP protection gives to innovation depends on the country's broader innovation policy framework. How do IP laws and regulations fit within the country's overall innovation strategy? What are the links between businesses and universities, especially the rules on IP ownership, royalty sharing and commercialisation of IP rights? What programmes are in place to improve access to existing knowledge, especially among SMEs?

### ***Policy practices to scrutinise***

Key issues when assessing a country's laws and regulations for the protection of intellectual property rights include: how laws and regulations define IP rights and balance these rights with society's wider interests; how well the IP filing process performs; how accessible the IP system is for SMEs and how much use they make of it; and how effective are IP enforcement and dispute settlement mechanisms.

The following issues ought to be considered:

- The extent that businesses and entrepreneurs are using the IP system and their filing success rate. When usage is restricted to larger firms or low in comparison to other similar economies, it is a sign that businesses have poor confidence in the IP protection system. The filing success rate provides a summary measure of how well businesses are informed about IP filing requirements.

- A low utilisation rate of the IP system needs to be interpreted with care, however. It may reflect the use alternative strategies by businesses to appropriate the value of their intangible assets, such as secrecy, exploitation of lead-time advantages and technical complexity. These less formal instruments can be supported through legislation on trade secrets and unfair competition (see Chapter 4). Trade secrets, for example, are recognised as intellectual property by the TRIPS Agreement.
- Establishing why usage of the IP system is low or limited predominantly to large enterprises requires an examination of the following policies, practices and constraints that may limit access:
  - Availability of legally-recognised instruments and laws to protect ownership of all types of intellectual property. In countries that are signatories to the WTO TRIPs Agreement, whether national legislation has been enacted to comply with this Agreement.
  - The costs of filing and obtaining IP (e.g. application, publication and maintenance fees, translation costs when applying for protection in other markets), as well as those incurred to maintain and enforce IP rights;
  - The time required and the complexity of the filing system. This depends on the number and types of procedures needed, how easily information on the filing requirement is obtainable, the processes used by the IP office to examine, register and grant IP, physical accessibility, in terms of distance to the IP office and whether electronic filing is allowed.
  - The geographic coverage of IP protection afforded to a business can be expanded cost effectively if the home country of the business signs onto international IP agreements administered by WIPO. Is the country a party to the Patent Co-operation Treaty for inventions, the Madrid system for trademarks and the Hague system for industrial designs? If not, then what deters the country from doing so?
- Use of the IP system by business depends also on the mechanisms and practices that are employed to raise awareness and understanding of all elements of the IP system. Areas that need to be considered include whether the IP office or its equivalent:
  - Organises information seminars and campaigns on IP and provides capacity building programmes on how to file for IP protection;
  - Produces practical IP guides and other information materials targeted to specific customer groups (e.g. start-up companies,

- inventors, researchers, government institutions, universities and businesses in specific sectors like bio-technology or agriculture);
  - Collects and disseminates case studies illustrating good practices in applying for and enforcing IP protection;
  - Facilitates procedural and administrative issues relating to the application process (e.g. help desks within IP offices, information kits, web sites and simplified procedures for granting IP protection to SMEs).
- The effective use of the IP protection system in promoting investment in innovation and its subsequent diffusion depends on policy practices that flank IP laws and regulations, e.g. collateral laws that allow IP owners to pledge their IP as collateral. Care needs to be taken, however, not to enter domains that are being filled by commercial providers of business services. Publicly-funded activities should address a market failure or serve to awaken a latent demand. Practices to examine include whether the IP office or its equivalent:
  - Regularly transforms information available in patent databases into more workable knowledge, e.g. by compiling and disseminating technical information on recent patent filings in given technical fields and translating information in patent data bases into other languages;
  - Provides easy access to patent information, e.g. through free on-line consultation of patent records, with functional search and analytical tools, holding information sessions on how to use and benefit from the public disclosure of patent information and by linking patent databases into patent libraries;
  - Promotes close ties and collaboration between universities and businesses to commercialise inventions and new technologies, e.g. by laws that enable universities to share royalties from jointly-produced innovations.
- The goal of fostering innovation and investment in R&D needs to be balanced against the public interest in terms of access to goods and services and knowledge, and each government will seek to achieve an appropriate balance. How well do provisions in place meet the government's policy objectives? Practices include IP laws that limit the period of protection granted (normally 20 years for a patent); the use of special provisions defining circumstances when the state can use patents outside of normal patent protection rules on the grounds of the wider public interest; and provisions that require the inventor publicly to disclose how to make and use the invention.
- What mechanisms are in place to enforce a country's IP system and to resolve disputes? Mechanisms that limit the cost to business of enforcing

and monitoring the use of their IP rights make the IP system more accessible.

- Procedures exist for quickly settling IP disputes out of court. Examples that appeal to inventors/businesses with limited financial resources include expedited arbitration and pre- and post-grant opposition or review procedures at IP offices. Greater use of arbitration and mediation and developing a market for IP insurance would also help reduce the costs of litigation.
- Fast and efficient procedures for hearing disputes in courts are also necessary (see also Question 1.4). Jurisdiction for hearing IP disputes needs to be clearly defined in law, with each agency involved having well-delineated responsibilities.
- Penalties for transgressions of IP laws and processes for enforcement of penalties or legal judgments exist. Whether these take into account aggravating and mitigating factors, such as the severity of violation, the resulting harm to the IP owner, the benefits that the offender derived from the violation, prior violations, early admission of the violation, co-operation or refusal to co-operate with the investigation, and the economic and financial situation of the offender.
- Mechanisms might be available in principle to enforce IP rights, but experience often shows that the process of enforcement can militate against overall effectiveness. What is the track record of enforcing IP rights and the outcomes of disputes?. A proxy measure of performance is whether the country features on watch-lists for not adequately enforcing IP rights (e.g. US Trade Representative Special 301 reports). What steps are being taken to address concerns raised by the international community or revealed by a poor enforcement track record (e.g. educational campaigns, specialised training for law enforcement officials and creation of specialised courts to deal with IP issues)?

### ***Further resources and case studies***

#### **The World Intellectual Property Organization ([www.wipo.org](http://www.wipo.org))**

- WIPO is responsible for administering 24 international treaties covering intellectual property protection. These treaties ensure that one international registration or filing will have effect in any of the relevant signatory States.
- WIPO has 189 country and 10 regional copyright and industrial property offices with information relating to the registration of intellectual property.
- It also maintains a comprehensive source of information on intellectual property issues for SMEs, which takes into account their time and resource

constraints. It brings together practical information and case studies on best practices for making IP rights more accessible and relevant to SMEs.

- The WIPO Arbitration and Mediation Center offers alternative dispute resolution options, in particular arbitration and mediation, for the resolution of international commercial disputes between private parties. The procedures offered by the Center are particularly appropriate for technology, entertainment and other disputes involving IP. The Center provides information on how it works, case examples, fees and background resources.

#### **The World Trade Organization ([www.wto.org](http://www.wto.org))**

- The WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), covers five broad issues: i) how basic principles of the trading system and other international IP agreements should be applied ii) how to give adequate protection to intellectual property rights; iii) how countries should enforce those rights adequately in their own territories; iv) how to settle IP disputes between members of the WTO; and v) special transitional arrangements during the period when the new system is being introduced.

#### **Others**

- The African Intellectual Property Organisation ([www.oapi.wipo.net](http://www.oapi.wipo.net)) aims to foster the conditions which allow national firms to profit from the results of research and exploit technological innovations, encourages the transfer of technology and makes the IP legal framework attractive to private investors. They offer training courses, and their website provides tools, including guides to filing for IP and model applications and access to a patent database.
- The European Patent Office ([www.epo.org](http://www.epo.org)) has produced a series of case studies that provide practical information on how SMEs manage their intellectual property.
- The European Commission maintains a [website](#) on intellectual property which includes surveys of IP enforcement worldwide and extensive links to other resources.
- The Australian government has developed an [IP toolbox](#) offering practical information to businesses on the use and management of IP. While parts of the Toolbox are specific to Australia, the guide is a useful resource to all IP owners and managers.

## **Contract Enforcement and Dispute Resolution**

1.4 *Is the system of contract enforcement effective and widely accessible to all investors? What alternative systems of dispute settlement has the government established to ensure the widest possible scope of protection at a reasonable cost?*

### **Rationale for the question**

The ability to make and enforce contracts and resolve disputes is fundamental if markets are to function properly. Good enforcement procedures enhance predictability in commercial relationships and reduce uncertainty by assuring investors that their contractual rights will be upheld promptly by local courts. When procedures for enforcing commercial transactions are bureaucratic and cumbersome or when contractual disputes cannot be resolved in a timely and cost effective manner, economies rely on less efficient commercial practices. Traders depend more heavily on personal and family contacts; banks reduce the amount of lending because they cannot be assured of the ability to collect on debts or obtain control of property pledged as collateral to secure loans; and transactions tend to be conducted on a cash-only basis. This limits the funding available for business expansion and slows down trade, investment, economic growth and development.

### **Key considerations**

Contract law includes the rules set and administered by the state that determine when an agreement is enforceable, the grounds on which a breach of the agreement will be found and the consequences. Contract enforcement is one of the pillars of the rule of law.

#### **Effective contract enforcement**

When two parties strike a bargain, there must be some mechanism to ensure that each party will stick to the terms. The main contract enforcement mechanisms are self-enforcement (e.g. posting bonds, ending a commercial relationship), reputation (e.g. risking a future commercial relationship), organisational (e.g. third party audits), technology (e.g. to monitor sales) and of course contract law. The issue is not whether a contract can be enforced but rather the cost of the various enforcement mechanisms and their efficacy in improving confidence between contracting parties. To be effective, the costs of enforcement must not outweigh the gains achieved from increased contractual commitment.

*Institutional requirements to support contract enforcement*

Having a contract law on the books is not sufficient. What matters equally are the role and practices of the legal institutions that support the effective implementation of contract law. The legal institutions relate to the organisation of courts, an independent and competent judiciary, the legal profession, the enforcement services and the process of law making itself. Their design is a crucial factor influencing equality of treatment between actors (e.g. small- and large-sized enterprises) and also bears on the cost of enforcement and thus the reliance and confidence that investors have in the system of contract enforcement.

*Alternative dispute settlement processes*

Exclusive reliance on formal systems of contract enforcement (*i.e.* litigation through the judiciary system) can be costly and slow. Alternative dispute resolution systems seek to resolve differences between parties in a timely and fair manner. The main examples are arbitration, mediation and conciliation hearings, often by industry bodies, specialised agencies or third party evaluators, conducted at the national or international level. Alternative dispute settlement processes often complement and sometimes supplement judicial contract enforcement procedures and can strengthen contractual commitment at lower cost. How well do these alternative dispute resolution mechanisms function? What are the relative costs and efficacy of the alternatives available and the methods of involvement by the official sector to enforce settlement agreements?

***Policy practices to scrutinise***

Key issues in assessing the effectiveness of a country's contract enforcement and dispute resolution system are how the contract enforcement system (*i.e.* contract law and supporting legal institutions) performs in terms of securing committal between transacting parties and enforcing contracts at a reasonable cost; as well as the accessibility to all investors and the options for, and cost effectiveness of, alternative dispute settlement mechanisms.

The following policy practices and criteria ought to be considered:

- The **role of the rule of the law** in the development and protection of contractual rights. Areas that need to be considered include whether:

- The jurisdiction for hearing contractual disputes is clearly defined in law (e.g. for contracts involving foreign entities, government and state-owned enterprises) and in which courts (e.g. local, specialised, small-claim courts); each agency involved in contract enforcement has well-defined responsibilities and powers to order particular remedies to parties and if there are limitations on these powers (e.g. prohibition on seizing state property to satisfy court judgements) they are transparent; national laws define the validity and enforcement of foreign judgments; and clear rules exist on who can invoke the work of the court (e.g. government agencies, like the competition authority or third party beneficiaries of the contract).
- The existence of distinct laws that underpin and support self-enforcement mechanisms. For instance, laws enabling and governing transactions secured by collateral, deposits, bonds and so on. These increase the effectiveness of a contractual promise by reducing the cost of enforcement and the risk of unsatisfactory court adjudication and orders. Is the institutional environment able to recognise and enforce these practices? Is it, for example, legally possible to establish escrow accounts or liens?
- **The implementation of contract enforcement laws.** While mechanisms might be available in principle to enforce contractual agreements, experience often shows that the process can be limiting, because it is expensive, slow or partial. What policy practices and constraints compromise the effective implementation and enforcement of contract laws? The factors to consider are:
  - *The performance of the supporting legal institutions* This will involve assessing judicial expertise (e.g. technical capacity of judges to hear complex business disputes), the impartiality and independence of the courts and the integrity of the judiciary (e.g. adhering to codes of judicial ethics, evidence or strong perceptions of corruption); the court system (e.g. case load of judges, backlog of cases, level of funding, staff training); case management practices of the court system (e.g. time limits and sanctions on delaying tactics, use of information technology for filing and tracking cases, for implementing procedural and jurisdictional rules, and for recording and disseminating reasoned case histories); the ability of the courts to contribute to jurisprudence in the area of contract enforcement (e.g. mandatory publication of decisions); and the track record of the legal system enforcing contractual agreements and settlements (e.g. do all types of parties duly obey court orders?).

- *The costs involved by a plaintiff to enforce a contract* This will depend on court fees including taxes, expert fees, enforcement fees, costs of discovery and geographic accessibility to courts. Enforcement costs will also depend on the average length of time required to enforce a contract through the court system. This in turn is determined by the number and complexity of pre-trial and trial procedures mandated by law (e.g. evidentiary standards, cooling-off periods) or court regulation (e.g. time limits for court actions and on the parties to present evidence) and procedural rules between the parties needed to file a case, during the trial and judgment period and to enforce the judgment. Also relevant for determining enforcement costs is whether procedural rules depend on the nature of the dispute and the court that is hearing the dispute (e.g. small-claim courts often have simplified procedures).
- When examining the practices of a country’s contract enforcement and dispute settlement system, the point is not to choose between one judicial system and another but rather to evaluate the cost and effectiveness of different contractual enforcement mechanisms in the reviewed country’s specific institutional context. In doing this, it is important to obtain the views of all the players. Since businesses are often the parties involved in disputes they can help pinpoint the possible practices which deter accessibility, raise the cost and slow down the resolution of commercial disputes. Similarly seeking the views of judges, lawyers etc. can help to identify reform needs (e.g. conflicts of law) and possible solutions that improve the efficiency of the courts in the enforcement of contractual rights and obligations.
- Alternative dispute settlement systems. What measures have been taken to encourage the use of other dispute resolution channels (e.g. ICC, UNCITRAL, ICSID arbitration) and to examine the cost effectiveness of alternative options for hearing and settling disputes? The factors to consider are: whether all investors have the right to choose an alternative dispute settlement method (e.g. international commercial arbitration); and if not, the rules that determine access; the processes used by local courts to enforce arbitration awards and how well they function (e.g. no significant additional cost to the plaintiff and prompt settlement); and the rules that determine final authority (e.g. consider no new evidence, time to appeal period) and whether they succeed in limiting the practice of “forum shopping”: i.e. tactics used by a party to unduly delay the process of settlement by trying to have their case re-heard before the formal court system.

### **Further resources and case studies**

- The International Development Law Organisation ([www.idlo.int](http://www.idlo.int)) provides developing countries with resources, tools and professional skills for establishing or strengthening the rule of law. They offer programmes specifically designed to improve legal frameworks and build capacity in commercial law, including contract enforcement.
- One dimension of the World Bank Doing Business ([www.doingbusiness.org](http://www.doingbusiness.org)) project covers contract enforcement. The indicators measure the efficiency of the judicial system in resolving a commercial dispute. The data are based on a payment dispute before local courts and relate to: i) the number of procedures involved; ii) the average time, measured in days it takes to enforce a contract from the moment a plaintiff files the lawsuit until payment and; iii) the cost entailed, relative to the value of the debt (assumed to be 200 per cent of the country's per capita income). The information is updated yearly and is available for most countries, facilitating cross-country comparisons.
- The [Judicial Reform Index](#) is a tool developed by the American Bar Association to assess how judicial institutions implement the rule of law. The JRI is based on comparative legal traditions as well as international standards, such as the U.N. Basic Principles on the Independence of the Judiciary. It has been used to assess judiciaries in more than 15 countries in Europe and Eurasia through a prism of 30 indicators related to: quality, education and diversity of judges; judicial powers; financial resources; structural safeguards; transparency; and judicial efficiency. The tool could usefully be applied in other countries.
- The United Nations Commission on International Trade Law ([www.uncitral.org](http://www.uncitral.org)) has a general mandate to further the progressive harmonisation and unification of the law of international trade. One area of the Commission's work is International Commercial Arbitration and Conciliation. Their website offers UNCITRAL Model Laws on International Commercial Conciliation and International Commercial Arbitration, guidelines and procedural rules on their use, as well as a set of useful on-line resources.
- [International Centre for Settlement of Investment Disputes](#) (ICSID) (see Question 1.8).
- A World Bank [Alternative Dispute Resolution Manual](#) provides practical advice and an overview of good practices when introducing commercial mediation to any legal system. Using case studies, diagnostic and assessment tools and stakeholder-specific marketing approaches, the manual provides strategies to overcome the challenges of building alternative dispute resolution programmes.

## **Expropriation Laws and Review Processes**

1.5 Does the government maintain a policy of timely, adequate, and effective compensation for expropriation also consistent with its obligations under international law? What explicit and well-defined limits on the ability to expropriate has the government established? What independent channels exist for reviewing the exercise of this power or for contesting it?

### **Rationale for the question**

Governments have the right to take private property for public purposes in certain circumstances. To develop infrastructure, such as roads and power stations, governments may need to acquire land. In environmental emergencies, people whose property is located in irreparably contaminated areas may need to be resettled in the interest of public health.

When a government expropriates property, compensation should be timely, adequate and effective. The right to fair compensation and due process is uncontested and is reflected in all international investment agreements. At the same time, some recent agreements provide that, except in rare circumstances, non-discriminatory regulatory actions to protect legitimate public welfare objectives, such as public health, safety and the environment, are not considered to constitute expropriation. Uncertainty about the enforceability of lawful rights and obligations raises the cost of capital, thereby weakening firms' competitiveness and reducing investment. Investment promotion and protection agreements can add to predictability and legal enforceability of property rights against arbitrary expropriation.

### **Key considerations**

Key issues in assessing a country's expropriation laws and review processes include: the clarity and transparency of expropriation laws and modalities in terms of their ability to provide timely, adequate and effective compensation; their consistency with international norms; and whether independent channels exist to review or contest expropriation decisions.

#### **Defining the power to expropriate property**

Government expropriation of land or other property ought to be for public purposes, observe due process of law, not discriminate among investors and be guided by transparent rules defining when expropriations are justified and how compensation is to be determined. When deciding whether to expropriate, governments should ask whether the public interest can be served by using public policy means other than expropriation, such as, for example, giving government the right of first refusal on land transactions?

### *Management of expropriation cases*

If actual practices for handling the expropriation of private property differ from those built into the statute books, what practices may be acting to compromise the due process of law, including the implementation of timely, adequate and effective compensation for expropriation? In some expropriation cases, the modalities go beyond financial compensation, and these also need to be considered. Land taken to build a hydroelectric project, for example, will typically involve resettlement issues.

### *Contesting expropriation decisions*

In countries governed by the rule of law, the government is itself subject to the law. When an expropriation is contested, the final say on the legitimacy of the expropriation or the terms on which compensation is made should be handled by a court or other tribunal. Does this court or tribunal, whether domestic or supranational, have the authority to review decisions regarding expropriation of property and to give effect to its decisions? What restrictions, if any, exist on who has the right to contest an expropriation event? What are the modalities for filing an appeal or contesting an expropriation decision? What is the technical capacity of the court or tribunal to hear contested expropriation cases?

## **Policy practices to scrutinise**

The following policy practices and criteria ought to be considered.

- *Defining the ability to expropriate private property.* Areas to be considered include:
  - The laws that permit the confiscation of property and whether they expressly limit the conditions under which the government may expropriate private property for public purposes (e.g. nationalisation) and whether legal standards exist for determining when an expropriation event has occurred. Specific features of the laws permitting expropriation to examine include whether: *i*) they are non-discriminatory (e.g. in terms of nationality); *ii*) they establish the right to adequate compensation; *iii*) they allow for an appeals process; and *iv*) procedures exist for calculating compensation (e.g. specifying the factors and methods that can be used, such as purchase price, resale value, depreciation, goodwill etc.).

- It is not feasible to list every circumstance in which the State may take private property in the public interest, but have the authorities made efforts to define the concept and to place boundaries on the scope of the public interest? Expropriation on political grounds, for example, is not in the public interest.
- Regulations that result in the *de facto* expropriation of property. Regulatory actions may constitute expropriation by denying an owner the ability to use or sell property or otherwise heavily encumber its use, thus reducing its economic value. Many government decisions can affect the value of private property, and judgments will differ on whether the government is exercising its regulatory powers or acting to seize indirectly property. Governments can help to alleviate this uncertainty by providing guidance to its agencies on how to distinguish practices that may constitute indirect expropriation. Does the government, for instance, collect, synthesise and communicate the reasoned decisions of case histories from conciliation commissions and arbitral tribunals? For events that were determined to be cases of indirect expropriation, was the property owner compensated, following the same modalities as for direct expropriation?
- *Implementing expropriation laws and practices* Are there practices and constraints that may compromise the implementation of timely, adequate and effective compensation for expropriation? The factors and criteria to consider are:
  - The median time taken to effect compensation following an expropriation event. There is no golden rule on the length of time taken, as it depends on many factors (e.g. complexity of the case). Comparisons with countries with similar cases can provide a benchmark.
  - The techniques used to calculate the level of compensation. One way to assess whether compensation is adequate is to ask how close the amount paid is to the current market value of the expropriated property. This involves examining the methods used to determine market value. In straightforward cases, such as land, there are usually prevailing market prices, but for unique or rarely traded assets, there is no readily available market price. In these cases what efforts does the government make to avoid arbitrary procedures? What valuation techniques are used (e.g. book value)? Which factors are taken into consideration (e.g. the value of intangible assets, depreciation, damage to property)? What legal standards are applied and what practices are adopted (e.g. use of third-party expert valuations, payment of interest)?

- The modalities of compensation. Beyond the issue of prompt payment of compensation is the question of how compensation is paid. Are payments fully realisable (e.g. paid in cash) and freely transferable (e.g. convertible into another currency, or payable in a hard currency)? When non-pecuniary settlements are offered (e.g. resettling displaced persons), does the government dialogue with those directly concerned? Are such persons resettled near to the previous location? And does the new location offer a similar amenity value and a comparable quality?
- Analyses of case histories of expropriation events brought to commissions or arbitral tribunals and consultation with stakeholders to gain their insights and experiences with the process. Are there signs of potential problems (e.g. disproportionate number of cases in a specific sector, or involving foreign enterprises)? How long does it take to effect compensation? What are the actual methods used to calculate compensation? And what is the manner of expropriation (e.g. arbitrary or guided by due process)?
- *Independent channels to review or contest expropriation decisions* What are the mechanisms available and processes for contesting expropriation decisions. The factors to consider are:
  - Whether the appeals body is independent from the agency ordering the expropriation and has the power to review and if necessary overturn government agency decisions regarding expropriation and compensation to owners of expropriated property; the grounds on which a decision can be contested are clear and transparent (e.g. documented procedural rules); whether national laws recognise alternative dispute resolution systems (e.g. foreign-based conciliation commissions and arbitral tribunals) and honour and enforce their decisions.
  - The technical capacity of the court or tribunal to review expropriation events. On this point, the policy practices to scrutinise are discussed in detail in Question 1.4.

### **Further resources and case studies**

- [International Centre for Settlement of Investment Disputes](#) (ICSID) (see Question 1.8).
- The [UN Commission on International Trade Law](#) (UNCITRAL) (see Question 1.4).
- Lex Mercatoria ([www.lexmercatoria.org](http://www.lexmercatoria.org)) (see Question 1.8).
- The [International Chamber of Commerce \(ICC\) Commission on Arbitration](#) is a forum for pooling ideas on issues relating to international arbitration and

other forms of dispute resolution. The website offers information on their work, arbitration rules and guidelines on the ways in which the ICC Rules of Arbitration can most effectively be used.

- An OECD paper on [“Indirect Expropriation” and the “Right to Regulate” in International Investment Law](#) surveys jurisprudence, state practice and related literature. It presents the issues at stake and describes the basic concepts of the obligation to compensate for indirect expropriation; reviews whether and how legal instruments and other texts articulate the difference between indirect expropriation and the right of the governments to regulate without compensation; and attempts to identify criteria which emerge from jurisprudence and state practice for determining whether an indirect expropriation has occurred.
- The [Investment Treaty Forum](#) at the British Institute of International and Comparative Law is a centre for discussion and research in public international law and international commercial arbitration. The Forum facilitates debate among lawyers, senior business managers, policy advisers, academics, government officials and other specialist practitioners. It also encourages dialogue with state representatives. Part of this work involves reviewing each of the arbitral awards where the issue of damages was discussed. The thrust of each case summary is on issues related to the award of monetary compensation. These case study summaries are available to Members of the Forum.
- The [Political Risk Insurance Center](#) at the Multilateral Investment Guarantee Agency provides a searchable database of Web-based documents on political risk environments; on legal issues related to arbitration, mediation and other investment dispute resolution and prevention mechanisms; research findings and analyses of political risk issues and their relationship to foreign direct investment.

## **Non-Discriminatory Treatment for National and International Investors**

*1.6 Has the government taken steps to establish non-discrimination as a general principle underpinning laws and regulations governing investment? In the exercise of its right to regulate and to deliver public services, does the government have mechanisms in place to ensure transparency of remaining discriminatory restrictions on international investment and to periodically review their costs against their intended public purpose? Has the government reviewed restrictions affecting the free transfer of capital and profits and their effect on attracting international investment?*

### **Rationale for the question**

Non-discrimination concerns the notion of "national treatment", which provides that a government treat enterprises controlled by the nationals or residents of another country no less favourably than domestic enterprises in like situations. National treatment requires equivalent, not identical, treatment. Equivalent treatment is when a different regime applies to non-residents as compared to residents to place them on an equal footing (e.g. for prudential purposes). Non-discrimination also means that an investor or investment from one country is treated by the host country no less favourably than an investor or investment from any third country (referred to as Most Favoured Nation or MFN in international agreements) in like situations. Reciprocally, non-discriminatory treatment does not call for providing advantages to foreign investors.

The application of these principles towards investment varies considerably across countries, partly because a state's right to regulate sometimes involves discriminating against foreign investors. Policies that favour some firms over others (i.e. any policies that derogate from national treatment or MFN) involve a cost, however. They may result in less competition (see also the chapter on Competition Policy), distort resource allocation, impede linkages between MNEs and local suppliers and slow the diffusion of technological innovations. These effects discourage all investors and give a negative perception about a country's receptiveness towards investment. This is why exceptions to non-discrimination, especially in sectors that play a central role in the development of an economy (e.g. financial and telecommunication sectors), need to be periodically re-evaluated to determine whether the original motivation and national benefits behind an exception remain valid and outweigh the costs borne by consumers, suppliers and investors.

The ability to transfer investment-related capital, including repatriating earnings and liquidated capital, is important for any firm to be able to make, operate, and maintain investments in another country. At the same time, governments sometimes need to limit these economic freedoms in order to address serious balance of payment difficulties. Since measures that restrict the free transfer of capital may adversely affect inflows of international investment, deter domestic

companies from accessing international capital markets to fund investment and encourage inefficient and non-transparent practices such as transfer pricing, restrictions on the transfer of funds also need to be reviewed periodically. Governments have authority to take any measure required to prevent evasion of their laws and regulations.

### **Key considerations**

#### *Establishing equivalent treatment*

Do national laws and regulations discriminate among investors and investments? What are the number and scope of exceptions from national treatment, the quality of implementation and enforcement, and the interactions with the concepts of MFN and fair and equitable treatment?

#### *Transparency and periodic review of discriminatory restrictions on international investment*

Does discrimination in investment policy - either inadvertent or intended - represent the best option for meeting particular policy objectives? There is a trade-off between offering national treatment as a means of increasing investment and qualifying national treatment as a means of promoting local enterprise development. While peer practices can offer insights on how to evaluate the trade-offs, the actual balance will depend on country specific conditions, levels of development and the goals of each host country. The basic consideration is to evaluate whether the present level and form of exceptions to national treatment contribute to promoting these goals and economic development more generally; whether alternative policy instruments could achieve the same goals more effectively; and how exceptions to national treatment discourage investment.

#### *Free transfer of funds*

Do restrictions on the transfers of investment-related capital exist? And if so, how do they operate? If restrictions exist, what is their likely impact on international investment? International investment is influenced by many factors, of which capital restrictions form only one part, but there may be some evidence of underperformance in attracting investment compared to similar countries without such restrictions.

### **Policy practices to scrutinise**

Key issues in assessing equivalent treatment for national and international investors are whether national laws and regulations treat foreign investors operating in the host country comparably to domestic or other foreign investors and whether discriminatory practices between domestic and foreign and among foreign investors are transparent. It also requires identifying any restrictions impeding the free transfer of capital and profit and assessing whether they deter investment.

The following policy practices and criteria ought to be considered:

- The legal framework establishing non-discrimination as a general principle governing investment. Areas that need to be considered include:
  - Whether a country’s constitution, laws governing commercial activity, including the investment law if one exists, other relevant laws and regulatory practices enshrine the principle of non-discrimination; their scope and application (e.g. sub-national authorities apply national treatment); if discrimination can be exercised through discretionary powers, and if so are there safeguards in place to avoid abuse of discretionary power; at what phase national treatment is embodied in international investment agreements that the country is a party to (i.e. pre- or post-establishment); whether these agreements grant most-favoured-nation treatment to investors and investments; how strictly treatment is compared to national investors (e.g. “same as”, “as favourable as” or “no less favourable”); and whether national treatment is dependent on a reciprocal commitment to the standard or deferred to a later date (as is done, e.g. in the Energy Charter Treaty).
- No country unequivocally applies national treatment. Laws and regulations and international agreements rightly allow a country to make qualifications. Where exceptions exist and when the scope of national treatment is limited, any exception should be transparent and clearly defined in law. This requires identifying:
  - **General exceptions** (e.g. to maintain public health, the protection of national security); subject specific exceptions (e.g. intellectual property, taxation provisions in bilateral tax treaties); and country-specific exceptions (e.g. specific industries, such as financial services and transport). It is also important to understand whether exceptions are based on an explicit and clearly defined rationale (e.g. public order, economic development, such as infant industries); and if exceptions are notified to international organisations or in the context of investment or trade agreements (e.g. OECD National Treatment Instrument, or Article 6 TRIMS agreement); and the key features of their design (e.g. indefinite duration or for a defined time

- period). Alternatively in some international agreements, national treatment extends only to those areas and industries identified in a 'positive' list (e.g. TRIMs and GATS agreements).
- **The nature of the exceptions.** For instance: across-the-board screening procedures for FDI entry, more burdensome licensing requirements for foreign investors than for domestic investors, sectoral foreign equity ownership ceilings, denial of access for foreign control-established enterprises to local finance and incentives (e.g. tax concessions), legal establishment (e.g. subsidiaries or branches), denial of access to specific markets (e.g. public procurement, privatisations), performance requirements (e.g. local content rules) and other discriminatory practices (e.g. nationality based restrictions on boards, limits on key personnel).
  - **How the country compares with other countries** in the region or at a similar level of economic development in terms of its discriminatory measures. The factors to consider are whether the country benchmarks the scope of national treatment in its laws and in practice with other similar economies; periodically reviews the list of exceptions based on an analysis of their costs and benefits, or a narrower regulatory impact analysis (see Question 10.3); and canvasses the views of foreign and domestic investors and other relevant stakeholders.
- The free and full repatriation of capital and profits from investments. What are a country's practices and restrictions on the transfer of investment-related capital, their key features and their impacts on investment decisions? This requires identifying:
    - **The scope of provisions allowing for the free transfer of funds.** For instance, rules apply both to inward and outward investment, or whether different rules are in force depending on the direction of the investment flow; whether rules apply to both existing and new investments; the types of investment-related capital and their coverage (e.g. profits, dividends, interest and royalty receipts, original capital, capital appreciation, proceeds from liquidation, payments received as compensation for property expropriation, settlement of disputes etc., and earnings of personnel engaged from abroad in connection with an investment); and the conditions that are attached to the transfer of investment-related capital (e.g. convertibility requirements)
    - **The principle exceptions and qualifications attached to the transfer of funds.** Which provisions effectively excuse a country from fulfilling obligations on the free transfer of capital that it has committed itself to? Under which conditions may new restrictions be imposed (e.g. a balance of payments crisis)? What

- is the form of these qualifications on the free transfer of capital (e.g. for a fixed duration in length, formal notification procedures, imposed on a discriminatory basis)? To which types of transfer do they apply?
- **The impact of restrictions on investment decisions.** Factors to consider are: whether the country’s policies on the transfer of funds result in unreasonably high costs (e.g. because of excessive exchange transaction charges); unreasonable delays (e.g. because of numerous and complex verification procedures); and the scope for arbitrary and discretionary decisions regarding the transfer of investment-related capital (e.g. on the choice of exchange rate values).

### **Further resources and case studies**

- OECD member countries have committed themselves to maintaining and expanding the freedom for international capital movements and current invisible operations under the legally-binding [OECD Codes of Liberalisation of Capital Movements and of Current Invisible Operations](#). The Codes are applicable to all OECD member states, which collectively represent the majority of foreign investors. A [User’s Guide](#) contributes to a better understanding of the principles, procedures and coverage of the OECD Codes.
- The OECD [Declaration on International Investment and Multinational Enterprises](#) includes an instrument on National Treatment. It consists of a declaration of principle and a procedural OECD Council Decision, which obliges adhering countries to notify their exceptions to National Treatment, and established follow-up procedures to deal with such exceptions. All 30 OECD members and 12 non-members have adhered to the Declaration. The website offers information on the National Treatment Instrument, how it works, a list of exceptions to National Treatment by each adhering country and a list of other measures having a bearing on the investment climate.
- The [OECD FDI regulatory restrictiveness index](#) captures statutory deviations from "national treatment" by calculating a summary measure of restrictiveness for OECD countries and an increasing number of non-member countries. The methodology covers four broad categories of restrictions: limitations on foreign ownership, screening or notification procedures, and management and operational restrictions.
- An OECD paper on “[Fair and Equitable Treatment Standard in International Investment Law](#)” surveys information on jurisprudence and practice related to the fair and equitable treatment standard. It examines the origins of the standard and its use in international agreements and state practice, its relationship with the minimum standard of international customary law and normative elements identified by arbitral tribunals

- An OECD paper on “[Most-Favoured-Nation Treatment in International Investment Law](#)” surveys jurisprudence and related literature on MFN treaty clauses in investment agreements. It defines the MFN clause, traces its origins and provides some examples of such provisions in the two major types of model investment agreements in existence (the “North American model” and the “European model”). It then summarises relevant aspects of the extensive work carried out by the International Law Commission between 1968 and 1978 on MFN clauses and describes recent arbitral awards on the scope of application of MFN treatment clauses resulting from disputes under investment treaties.
- A WTO website deals with the [General Agreement in Trade in Services \(GATS\)](#). The GATS agreement covers all internationally-traded services and defines four ways of trading, including “mode 3” when a foreign company sets up a subsidiary or branch to provide services in another country. The website provides information about the GATS agreement, including the application of the MFN and National Treatment Principles.
- The IMF compiles, in close consultation with national authorities, the [Annual Report on Exchange Arrangements and Exchange Restrictions](#). It tracks for each country exchange measures in place, the structure and setting of the exchange rate, arrangements for payments and receipts, procedures for resident and non-resident accounts, mechanisms for import and export payments and receipts, controls on capital transactions and provisions specific to the financial sector.

## **International Co-operation and Periodic Review**

1.7 Are investment policy authorities working with their counterparts in other economies to expand international treaties on the promotion and protection of investment? Has the government reviewed existing international treaties and commitments periodically to determine whether their provisions create a more attractive environment for investment? What measures exist to ensure effective compliance with the country's commitments under its international investment agreements?

### **Rationale for the question**

International investment agreements promote cross-border investment. They can reduce restrictions on sectors closed to international investment, offer investors minimum levels of protection based on international legal standards (e.g. against expropriation), and make the rights and obligations of the parties more stable and predictable. Although the government loses some policy flexibility, risks and uncertainties faced by investors are reduced, helping to mobilise additional investment. Wider country coverage of international investment agreements is thus one of the elements underpinning an attractive investment environment.

A country's investment climate is not static. Terms of trade, technologies and policies in other countries change continuously. As a result, a country's competitiveness can change even when a government has made no changes in its own rules, and its policy practices and regulations (e.g. performance requirements) can quickly become outdated vis-à-vis prevailing best practices. Both points underscore the need for a country periodically to review provisions under their international investment agreements to ensure they play fully their role in promoting investment, and to ascertain their effective implementation.

### **Key considerations**

*The international legal framework for attracting FDI* Some of the topics covered in other questions in this chapter (e.g. Questions 1.5, 1.6 and 1.8) and in other chapters (e.g. trade-related investment measures, Question 3.5) relate to provisions of international investment agreements (IIA). The main consideration here is not to revisit these issues, but to make an overall assessment of how well they and other IIA provisions in existing agreements perform in terms of providing an environment conducive to cross-border investment. It also involves reviewing efforts made by the authorities to expand the coverage of a country's IIA agreements and their compliance with them. The related area of international tax co-operation is covered in Question 5.9.

### **Policy practices to scrutinise**

Key issues in assessing international co-operation and periodic review are to take stock of the international legal framework for attracting FDI and to assess the

efforts being made to review and further develop international investment co-operation and their effective implementation.

The following policy practices and criteria ought to be considered:

- **Coverage of international investment agreements.** What bilateral investment treaties (BITs) have been signed by the government and have they been ratified? If they have not been ratified, what has prevented the country from doing so? It also involves taking stock of other international agreements that facilitate cross-border investment (e.g. regional investment agreements, concession agreements, the Energy Charter Treaty, TRIMs and GATS: see also the Trade Policy Chapter, bilateral tax treaties: see also the Tax Policy chapter and treaties covering intellectual property: see also Question 1.3). Calculating the proportion of FDI inflows that are protected by IIAs offers a summary measure of the coverage of a country's IIAs. Cross-country comparisons need to be interpreted with care, however, since the scope of IIAs can vary widely (e.g. because of the definition of investment used or the extent of sectoral exceptions).
- **Expanding IIAs.** Examining the institutional arrangements in place helps in understanding the strategic approach of the country towards international investment co-operation. For example, who has authority and responsibility for initiating negotiations? Is there a dedicated unit responsible for evaluating the performance of existing agreements and how do new agreements incorporate the lessons drawn from existing international co-operation? The latter might involve, for instance, countries developing and modifying a model BIT in light of emerging best practices. Review processes should also involve regular interaction with relevant stakeholders and the partners to international investment agreements. These parties are often well-placed to provide rapid feedback on emerging trends or problematic areas, as well as giving their perceptions about the investment climate. There is no golden rule on the frequency with which a country should review its international treaties and commitments. It will depend, inter alia, on the number of treaties, their average age and the specific issues that have emerged between the parties (e.g. in arbitration).
- **Effective compliance with IIAs.** Are there any gaps between commitments made and actual compliance under IIAs? In some agreements (e.g. TRIMs), there are transitional periods and notification requirements. It also involves assessing whether the authorities responsible for implementation have the expertise and capacity to ensure commitments are enforced and examining efforts to communicate to government agencies the implications of IIAs for their areas of responsibility (e.g. implementation guides).

### ***Further resources and case studies***

- UNCTAD's programme on [International Investment Agreements](#) helps developing countries to participate more effectively in international discussions or negotiations on investment at the bilateral, regional, plurilateral and multilateral levels. Resources include databases on [bilateral investment treaties](#) and a collection of treaty-based investor-State dispute settlement cases which were disclosed by the parties or arbitral institutions, articles on key concepts and issues relevant to international investment agreements and recent trends and developments in international investment rule-making.
- An [ICSID database of bilateral investment treaties](#) lists BITs notified to ICSID by governments but is not complete.
- A [WTO website on trade and investment](#) provides technical and non-technical information about trade and investment at the WTO, including reports from the WTO Working Group on the relationship between trade and investment, notification of TRIMs that have been eliminated, documents on dispute settlement involving the TRIMs agreement and a handbook on TRIMs notification requirements.
- The UN Commission on International Trade Law ([www.uncitral.org](http://www.uncitral.org)) (see Question 1.4).
- The [OECD Model Tax Convention on Income and Capital](#) is widely used by countries when negotiating bilateral tax agreements which clarify the situation when a taxpayer might find himself subject to taxation in more than one country.

## **International Arbitration Instruments**

1.8 *Has the government ratified and implemented binding international arbitration instruments for the settlement of investment disputes?*

### **Rationale for the question**

International arbitration instruments provide a binding mechanism for resolving disputes between a host country government and an investor, typically relating to commitments made in international investment agreements (see Question 1.7). Most international investment agreements contain provisions for international arbitration (in limited instances contingent upon having exhausted local remedies). They afford recourse to a usually cost-effective, prompt, flexible, impartial and confidential channel for settling disputes for domestic businesses collaborating in cross-border joint ventures and international investors doing business with the government. While international arbitration should normally be perceived as a last resort, its existence as an option provides a credible form of reassurance to investors and signals a government's commitment to the rule of law and to observe its investment treaty obligations. They thereby bolster the confidence of investors that their property is secure (see also Questions 1.2 and 1.4) and contribute to establishing a reliable and stable environment for investment.

### **Key considerations**

*Making international arbitration instruments operational*

The preferred instrument for resolving disputes specified in investment treaties is the 1966 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention, also known as the Washington Convention). In order for a dispute to be brought before it, there must be a written agreement to arbitrate, most often in the form of an investment treaty. When a dispute is based on a contract and not an investment treaty (*i.e.* non-ICSID arbitral awards), the 1958 New York Convention on Recognition and Enforcement of Arbitral Awards makes, with certain exceptions, arbitral awards rendered in one party to the Convention enforceable in any other party to the Convention. For these Conventions to function properly and credibly, a country must sign and ratify them, as well as introducing national legislation and procedural rules so that foreign arbitral awards are recognised and enforced by local courts.

### *Improving how treaty arbitration functions*

International arbitration improves the effectiveness of dispute settlement and can also help in some cases to make recourse to such arbitration less likely in the first place. Publishing arbitral awards can help develop a public body of jurisprudence and promote public acceptance of international investment arbitration. Higher visibility, more generally, can demonstrate a national commitment to honouring international arbitration instruments. How can transparency be promoted in international investment arbitration and what steps are the authorities taking to develop expertise in handling cases before international arbitration?

### **Policy practices to scrutinise**

Key issues in assessing international arbitration instruments are to examine whether the state is a signatory to international arbitration instruments, whether local laws and practices recognise and enforce foreign arbitral awards, and what efforts are being made to improve how treaty arbitration functions. Among policy practices and criteria to be considered are:

- The implementation of international arbitration instruments.
  - Has the government signed and ratified the major international arbitration conventions (e.g. Washington and New York Conventions) and regional arbitration conventions (e.g. the Olivos Protocol for the Settlement of Disputes in Mercosur, the ASEAN Protocol on the Dispute Settlement Mechanism)? If the country is not a party to ICSID, is the ICSID Additional Facility used?
  - Has the government made operational its commitments under the international and regional arbitration conventions? Are national legislation, regulations and enforcement systems in place so that parties can choose to commit themselves irrevocably to arbitrate disputes internationally and so that foreign arbitral awards are recognised and enforced by local courts and without undue delay?
  - Do practices or restrictions on agreements to arbitrate disputes hinder the use and effectiveness of international arbitration instruments (e.g. mandatory procedures for the conduct of arbitration proceedings, regulations that limit who can serve as an arbitrator)? Do national courts interfere with valid arbitrations (e.g. accepting to hear a dispute or an appeal to an award that the parties had agreed to submit to international arbitration)?

How clear is supporting national legislation (e.g. ambiguities which may affect arbitral efficiency)?

- How treaty arbitration functions.
  - What efforts has the government made to promote the transparency of international arbitration without compromising confidential business and government information? When the parties agree, are the outcomes of awards involving the country communicated widely (e.g. posted on relevant government websites)? Does the government participate in intergovernmental organisations that facilitate arbitration and other forms of dispute settlement between states (e.g. the Permanent Court of Arbitration)?
  - What has the government done to strengthen its expertise in handling international dispute settlement instruments and managing the cases brought before international forums?
  - What are the lessons for both the government and business organisations from the public body of jurisprudence aimed at enhancing the effectiveness of international investment arbitration? What are the views and practical experiences of the parties involved?

### ***Further resources and case studies***

The following resources provide additional information on international arbitration instruments:

- The [International Centre for Settlement of Investment Disputes \(ICSID\)](#) is an autonomous international institution established under the Washington Convention on the Settlement of Investment Disputes to provide facilities for conciliation and arbitration of international investment disputes. Its website provides information on its services, how it functions, its rules and regulations, a list of signatory countries and the text of the Convention.
- Lex Mercatoria ([www.lexmercatoria.org](http://www.lexmercatoria.org)), an online law site dedicated to the provision of information on international commercial law, has compiled a comprehensive set of resources on [International Commercial Arbitration and other Dispute Settlement](#).
- An OECD paper on “[Transparency and Third Party Participation in Investor-State Dispute Settlement Procedures](#)” surveys issues related to transparency and third party participation in investor-state dispute settlement procedures. It examines the way in which the current rules apply to these issues, describes the steps taken to improve the transparency of the system at the governmental level, by the arbitral Tribunals and the ICSID and examines the perceived advantages as well as the challenges of additional transparency.

- The UN held a conference on the status of the New York agreement and prepared a useful set of papers entitled “[Enforcing Arbitration Awards under the New York Convention: Experience and Prospects](#)” that outlines the purpose and the experiences of various countries using the international system for enforcing foreign arbitral awards.
- The [International Treaty Arbitration \(ITA\)](#) website provides access to all publicly available investment treaty awards; information and resources relating to investment treaties and investment treaty arbitration; and links to further resources.
- UNCTAD provides a [database of Treaty-based investor-state dispute settlement cases](#) that are pending or which have been concluded. Only those claims that were disclosed by the parties or arbitral institutions are included.
- The [International Council for Commercial Arbitration \(ICCA\)](#) website includes a comprehensive set of on-line resources relating to international treaties and conventions on arbitration, national arbitration law and national, regional and international institutions involved in arbitration.