



Negotiating Group on the Multilateral Agreement on Investment (MAI)

Expert Group No.3 on “Special Topics”

PERFORMANCE REQUIREMENTS

(Note by the Chairman)

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I. General considerations

1. As a high standards Agreement, the MAI would need to contain obligations on performance requirements (PRs). PRs are obligations imposed by governments on foreign investors to secure certain economic benefits. They are of concern because they interfere with business decisions and produce market distortions detrimental to the efficient use of investment funds.
2. The National Treatment and Most Favoured Nation Treatment obligations of the MAI would not suffice to address this problem. The MAI should attempt to prohibit as many PRs as possible with a view to minimising the distortions or restrictions they impose on investment activities. The MAI should try to go beyond the disciplines found in other agreements, such as the TRIMs Agreement, the ECT and the NAFTA. It would be important, however, to avoid creating conflicting obligations and forum shopping for the settlement of investment disputes (these issues are discussed by the Expert Group N°1).
3. At this stage of the discussion, the Expert Group decided to adopt a functional approach for distinguishing between two categories of PRs: those not associated with the granting of an advantage (for instance PRs attached to an authorisation) and those associated with the granting of an advantage. This should not prejudice, however, the adoption of a single list for both types of PRs, an option supported by some delegations.
4. It also agreed that the MAI obligations in this area should be confined to those PRs that are mandatory or enforceable under domestic law or other administrative rulings. PRs may also be relevant to the issue of investment incentives (IIs) since a prohibition on a PR linked to an II may limit the use of that incentive. This should be kept in mind for the elaboration of disciplines in these two areas. It would also be necessary to keep in mind the provisions of the GATT 1994 Agreement on Subsidies and Countervailing Measures since it also contains disciplines on investment incentives. The Expert Group decided that PRs imposed in the context of privatisation should be taken up in the context of the Group's discussion on the subject of privatisation.

II. Performance Requirements not associated with the granting of an advantage.

5. It was considered that the draft text proposed in the Annex of this report is a good working basis for defining a MAI prohibition on PRs. The PRs covered should be those PRs imposed or enforceable under domestic laws, regulations, procedures and administrative and judicial decisions of general

application or established policies¹. They would relate to investors and investments as defined by the MAI². One delegation felt that it would suffice for the MAI to cover those PRs imposed or enforceable under domestic law.

6. The great majority of delegations expressed a preference for a closed list of prohibited PRs. This would ensure clarity and certainty, for both governments and investors, on the exact nature and scope of the MAI obligations in this area. These are also legitimate policy objectives, particularly those found in labour laws, social security laws or environment laws, that most delegations considered should be taken into account. Two delegations wanted to maintain the open list concept until the shape of the MAI prohibition is better known.

7. The Expert Group agreed that the MAI prohibition should cover those PRs prohibited under the WTO TRIMs Agreement (namely items *b*) to *e*) of paragraph 1 of the Annex). A large majority of delegations considered that it should also cover export performance requirements even though this is not the case under the TRIMs Agreement and apply to both goods and services.

8. The general opinion of the Group is that neither the language of item a) nor that of item e) of the proposed article on PRs would prohibit export restrictions or exports bans. This needs to be discussed further.

9. Most delegations considered the MAI should also cover the two other PRs listed in Article 1106.1 of NAFTA, namely PRs requirements to transfer technology, production processes and other proprietary knowledge, and exclusive supplier arrangements. As to technology transfers (paragraph 1, item *f* of the draft article), some delegations believed it would be desirable to ensure consistency with existing intellectual property agreements since these may allow certain PRs (compulsory licensing for instance) under certain conditions. Other delegations did not necessarily agree with this view. This issue requires further analytical work. The wording of the prohibition on exclusive supplier arrangements (paragraph 1, item *g* of the draft article) may also need to be modified to avoid confusion with MAI obligations on monopolies, an issue being considered separately by the Experts Group. One delegation felt that, as presently described, item *g*) actually could belong to the monopolies issue. It also suggested an alternative wording to capture the comments made by other delegations; this is reproduced in brackets in paragraph 1 of the Annex to the present document.

10. A number of delegations felt, however, that even with these additions the focus of the PRs article would still be too centred on the trade-distorting effects of PRs and that a real attempt should be made to extend the coverage of this provision to those PRs more directly related to the capital and labour markets. One possibility would be to prohibit, in paragraph 1, item *e*) of the draft article, all PRs on local sales and not only those linked to exports or foreign exchange earnings. Manufacturing requirements and local hiring requirements could also be added to the list. A few delegations thought it would be more transparent to list as well local equity requirements or joint venture requirements even though these measures should, in principle, be captured by the National Treatment and MFN treatment articles.

11. One delegation suggested exploring whether the MAI could include some of the PRs explicitly excluded under Article 1106.4 of NAFTA and, more particularly, PRs to locate production, train or

1 This closely follows the language of the draft transparency article of the MAI which suggests that its obligations may apply to “laws, regulations, procedures and administrative rulings and judicial decisions of general application” as well as “established policies” not expressed in laws or regulations by other means. See consolidated text DAFFE/MAI(96)16, page 5.

2 The proposals that have been made by the Drafting Group 2 are found in DAFFE/MAI(96)16, section A.1.

employ workers, construct or expand particular facilities. Local funding requirements were also mentioned in this context. Several delegations were attracted to this more ambitious approach, but it was also recognised that the broader the list, the greater the number of qualifications or limitations there are likely to be to preserve the ability of Contracting Parties to determine their own policies in these areas. This consideration should be kept in mind in future discussions.

12. There was a general consensus that no Contracting Party should be prevented from adopting or maintaining measures necessary to protect public health, safety and the environment provided that National Treatment and MFN treatment obligations are respected. However, it was noted there is no compelling reason that these concerns be addressed in the context of PRs. Thus a great majority of delegations felt that it would not be necessary to retain the clarification found in Article 1106.2 of NAFTA concerning technical specification requirements imposed by domestic health, safety and environmental legislation or regulation which may be relevant to technology transfers. One delegation reserved its position at this point.

13. The Expert Group agreed that the MAI prohibition obligation on PRs should apply to any investor of a Contracting Party and its investments, but remained divided as to whether this obligation should also apply to an investor of a non-Contracting Party and its investments in a Contracting Party (i.e. on an *erga omnes* basis). (The same question arises with PRs associated with the granting of an advantage.) Many delegations took the view that such an extension could create a serious problem since non-Contracting Parties would remain free to impose PRs on MAI investors and their investments; these are the countries which make the more extensive use of PRs. Other delegations advocated a prohibition covering investors of both Contracting and non-Contracting Parties.

14. NAFTA Delegations explained that the *erga omnes* option had been chosen under NAFTA to ensure that NAFTA investors are not put at a disadvantage vis-à-vis non-NAFTA investors because of their inability to offer special undertakings to secure a government authorisation or advantage. If PR prohibitions were extended to non-Contracting Parties in the MAI, their potential effect on MAI investors could also be avoided. Unless all investments were treated in a similar way, a conflict could also arise with the MFN treatment obligation (which requires that a NAFTA investor always be treated no less favourably than a non-NAFTA investor). These Delegations also argued that the *erga omnes* approach would be more consistent with the objective of reducing economic distortions and creating the best conditions possible for investment by domestic MAI and non-MAI investors.

III. Performance Requirements associated with the granting of an advantage.

15. While a large majority of delegations reserved their judgement as to how PRs associated with the granting of an advantage might be disciplined under the MAI, it nonetheless recognised that the circumstances which condition their existence are not entirely the same as for other PRs. There may be legitimate political and economic reasons for seeking concrete returns from government assistance programmes such as a good return for tax payers money. Subtracting an investor from the benefits of an incentive, even if linked to a PR, has different implications than the removal of PRs imposed by domestic law or regulation. Because of these differences, the list of prohibited PRs might be shorter for PRs associated with the granting of an advantage than for other PRs. Some delegations considered, however, that the list should be identical for the two categories of PRs.

16. Several delegations underlined the need for consistent and harmonious relations between MAI disciplines on PRs and those on Investment Incentives. Due account should also be taken of the WTO disciplines, notably the TRIMs Agreement and the 1994 GATT Agreement on Subsidies and

Countervailing Measures. One delegation considered that these new agreements have yet to be tested and it would not be wise for the MAI to try to go beyond these instruments.

17. A number of delegations underlined, however, that the WTO Subsidies Agreement covers only the fiscal side of an investment incentive but not any related PRs. This leaves the MAI free to develop obligations on PRs associated with the granting of an advantage. The MAI would in any case need to cover those captured by the TRIMs agreement, namely those listed in items b) to e) of paragraph 1 of the Annex. As with the first category of PRs examined, a majority of delegations were in favour of prohibiting export PRs linked to the granting of an investment incentive.

18. A number of delegations were in favour of covering services as well as goods. This would also constitute an important step beyond the TRIMs Agreement. The Expert Group concurred, however, with the comments of a NAFTA delegation that the dividing line between contracted services (such as book-keeping, accountants and advertising) and employment requirements is not always easy to draw. It would therefore be necessary to reflect further on how employment-related PRs could be brought under the MAI umbrella.

19. There were greater doubts that PRs linked to R&D incentives could be prohibited under the MAI given the nature of the incentives programmes currently in place in this area in OECD countries.

20. No other PR was singled out as a possible candidate for a prohibition obligation, but delegations were invited to reflect on how the list³ in Article 1106.4 of NAFTA could be shortened. It was also decided to come back to the exceptions listed in Article 1108.8 of NAFTA as a house keeping matter after the list of prohibited PRs is firmed up. There was no general inclination to attempt to define the term "advantage", although a few delegations noted that it could not be limited to an opportunity to invest or to the granting of an operating license.

IV. Implementation

21. The Expert Group felt it premature to discuss whether any prohibition obligation under the MAI should be made applicable upon the entry into force of the Agreement (or after a transition period as under the TRIMs Agreement) or whether the Contracting Parties would be entitled to lodge reservations for non-conforming measures in accordance with the proposals that have been made in this connection⁴. The connection with excluded PRs was also noted. This issue also raises important questions for accession of non-OECD countries to the MAI. It would be desirable to come back to implementation of the MAI obligations on PRs at a later stage.

3 It includes performance to locate production, to provide a service, train or employ workers, construct or expand particular facilities, or carry out research and development.

4 See Standstill, Rollback and the Listing of Country Specific Reservations in DAFPE/MAI(96)16, section C.

Annex

Draft Article on Performance Requirements

Paragraph 1¹

No Contracting Party may impose, enforce or [maintain]², any of the following requirements³, or enforce any commitment or undertaking, in connection with the establishment, acquisition, expansion, management, operation, management, maintenance, use, enjoyment and sale or other disposition of an investment⁴ of an investor of a Contracting Party [or of a Non-Contracting Party] in its territory⁵:

- (a) to export a given level or percentage of goods or services;
- (b) to achieve a given level or percentage of domestic content;
- (c) to purchase, use or accord a preference to goods produced or services provided in its territory, or to purchase goods or services from persons in its territory;
- (d) to relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment;
- (e) to restrict sales of goods or services in its territory that such investment produces or provides [by relating such sales in any way to the volume or value of its exports or foreign exchange earnings];⁶
- (f) [to transfer technology, a production process or other proprietary knowledge to a person in its territory]⁷;
- (g) [to act as the exclusive supplier of the goods it produces or services it provides to a specific region or world market] [to locate its headquarters for a specific region or the world market in

1 It is yet to be decided whether paragraph 1 and 2 can be combined into one.

2 One delegation has proposed the inclusion of this term.

3 One delegation considers that this obligation should be limited to PRs found in laws, regulations, procedures, administrative rulings and judicial decisions of general application as well as established policies and should exclude contractual obligations between the investor and the state.

4 This list of investment activities reproduces the list proposed for the National Treatment and Most Favoured Nation obligations [See DAFFE/MAI(96)16, A.II.1.].

5 The place of this term is still to be determined in the National Treatment and Most Favoured Nation Treatment provisions [See DAFFE/MAI(96)16, A.II.1.].

6 One delegation supports the elimination of the brackets.

7 This obligation does not apply under NAFTA when the requirement is imposed or the commitment or undertaking is enforced by a court, administrative tribunal or competition authority to remedy an alleged violation of competition laws or to act in a manner not inconsistent with other provisions of the Agreement.

a Contracting Party concerning one or several goods the investor produces or services it provides to this specific region or the world market⁸].

(h) [to achieve a given level or value of production, investment manufacturing, employment, research and development in its territory];

(i) [to hire a given level or type of local personnel]; or

[(j) (Others to be defined)⁹].

Paragraph 2

No Contracting Party may condition the receipt or continued receipt of an advantage, in connection with an investment in its territory¹⁰ of an investor of a Contracting Party or of non-Contracting Party, on compliance with any of the following requirements:

(a) [to export a given level or percentage of goods or services];

(b) to achieve a given level or percentage of domestic content;

(c) to purchase, use or accord a preference to goods [and services]¹¹ produced in its territory;

(d) to relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such an investment; or

(e) to restrict sales of goods or services in its territory that such investment produces or provides by relating such sales in any way to the volume or value of its exports or foreign exchange earnings.

8 Alternative wording proposed by one delegation.

9 It was left undecided whether local equity requirements and joint venture requirements should be listed for transparency purposes in view of the fact they should be prohibited under the National Treatment and MFN provisions.

10 See note 5.

11 It is yet to be determined how this provision would exclude contracted services.