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## **Negotiating Group on the Multilateral Agreement on Investment (MAI)**

### **GENERAL EXCEPTIONS**

**(Note by the Chairman)**

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1. General exception provisions were discussed by the Negotiating Group in December, 1995 and a draft article on general exceptions was presented to the Negotiating Group by Drafting Group 2 in March 1996.<sup>1</sup>
2. The question of the interrelationship between a general exceptions provision and the substantive obligations of the MAI was discussed by the Negotiating Group in June, 1996. When considering whether general exceptions should override MAI obligations relating to compensation and protection from strife (paragraph 1 of the present draft article), the Chairman of the Negotiating Group noted that a large majority of delegations felt that general exceptions should not apply to investment protection [DAFFE/MAI/M(96)4].
3. The main outstanding issues relate to the scope of the provision, the nature of measures taken thereunder, and the appropriate procedural mechanisms to ensure transparency, including the role of the Parties Group.
4. This note considers essential security interests and public order exceptions separately and invites the the Negotiating Group to consider the proposed solutions set out herein.

### Essential Security Interests

5. There is no definition of essential security interests. The present draft article (paragraph 2 a(i-iii),b,c) refers to a set of elements often found in international agreements and which assist in determining the kind of measures that are intended to be covered by the term. There are different views whether the list in subparagraph (a) should be an open or closed list.
6. Traditionally, the right of a country to invoke an exception for actions taken in pursuance of its essential security interests is without qualification. The expression "which it considers necessary" is considered to confer a large degree of self-judgement on the party invoking the exception. The commentary to the present draft article indicates that some delegations propose to safeguard against potential abuse by constraining the self-judging nature of the essential security provisions.
7. Recent investment agreements have attempted to limit the possibility of abusive recourse by introducing requirements that measures taken pursuant thereto shall not constitute, or be applied in a manner which would constitute, arbitrary or unjustifiable discrimination or may not serve as disguised restrictions.<sup>2</sup>

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<sup>1</sup> The draft text and accompanying commentary taken from DAFTE/MAI(97)1 are attached to this note for convenience.

<sup>2</sup> ECT (Article 24 (2) and (3) and GATS (Article XIV, chapeau).

8.. The commentary to the present draft article indicates that the introduction of an anti-abuse clause, in whatever form, would be considered to have the effect of allowing a party which had reason to believe that another party had made improper use of this article to challenge such use as contrary to the objectives of the article.

9. The question whether measures pursuant to a general exceptions article should be subject to transparency (i.e. publication) obligations of the agreement has not been fully debated. There is presently no general MAI obligation of notification of new measures or any changes to existing measures which might affect the performance of obligations under the Agreement. This requirement is in brackets in the present draft article.

*Do delegations prefer an essential security provision:*

-- *narrowly drawn with a closed list, which is entirely self-judging and not subject to binding dispute settlement. The provision would not apply to expropriation and compensation and protection from strife. These measures could be subject to the transparency obligations of the agreement and to a notification obligation.*<sup>3</sup>

*or*

-- *with an open list but which is subject to a general anti-abuse clause along the lines proposed in the draft article (paragraph 4).*<sup>4</sup> *The measures would be subject to transparency and notification obligations.*

### **Public Order**

10. As for essential security interests, there is no definition of public order. Some countries believe that a reference to public order is necessary to allow countries to take exceptional measures based on this principle. Other delegations are not convinced that it is necessary to discriminate between foreign and domestic investors in order to protect public order.

11. Unlike "essential security interests", measures taken pursuant to this article are not ordinarily considered to be self-judging.<sup>5</sup> There are often limitations attached such as the principle of proportionality, or restricting the invocation of such measures to a situation where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society. Consequently, a party which feels itself aggrieved by an improper invocation of the article could initiate consultations and/or dispute settlement.

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<sup>3</sup> The GATS (Article XIV bis) contains a notification requirement for these measures.

<sup>4</sup> An interpretative statement could indicate the intended effect of such a provision, e.g. to permit a party that had reason to believe that another party had made improper use of the article to challenge such use as contrary to the objectives of the article.

<sup>5</sup> The ECT is an exception to this general rule (see Article 24(3)).

12. Delegations which were in favour of including a public order exception agreed that its use should be strictly controlled and should be subject to notification requirements and to consultations and dispute settlement.

*Would delegations agree that the MAI should include a public order exception (as a separate article, or sub-article) provided that it is subject to more stringent safeguards than those applying to essential security interests?*

*Could these conditions include:*

- that the public order exception would not apply to articles on expropriation and compensation and protection from strife;*
- an interpretative statement to provide guidance in understanding what is meant by the term.<sup>6</sup>*
- an anti-abuse clause which would include a restriction that such measures could not be invoked unless there was a genuine and sufficiently serious threat to one of the fundamental interests of society;*
- the right to invoke consultations/dispute settlement by an MAI Party;*
- full transparency and notification obligations.*

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<sup>6</sup> The 1991 CIME clarification provides that "measures taken for economic, cultural or other reasons should be identified as such and should not be shielded by an excessively broad interpretation of public order..."

Annex

extract from DAFFE/MAI(97)1

**GENERAL EXCEPTIONS**

- [1. This Article shall not apply to Articles -- (on expropriation and compensation and protection from strife).]
2. Nothing in this Agreement shall be construed:
  - a. to prevent any Contracting Party from taking any action [which it considers] necessary for the protection of its essential security interests [including those:]
    - (i) taken in time of war, [or] armed conflict, [or other emergency in international relations];
    - (ii) relating to the implementation of national policies or international agreements respecting the non-proliferation [inter alia] of nuclear weapons or other nuclear explosive devices;
    - [(iii) relating to the production of arms and ammunition;]
  - b. to require any Contracting Party to furnish or allow access to any information the disclosure of which [it considers] [would be] contrary to its essential security interests;
  - c. to prevent any Contracting Party from taking any action in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.
- [3. Nothing in this Agreement shall be construed to prevent any Contracting Party from taking any action necessary for the maintenance of public order.]
- [4. Paragraphs 2 and 3 may not be invoked by a Contracting Party as a means to evade its obligations under this Agreement.]
- [5. Actions taken pursuant to this Article shall be notified to the Parties Group in accordance with Article-- of this Agreement.]
- [6. If a Contracting Party (the "requesting Party") has reason to believe that actions taken by another Contracting Party (the "other Party") are not in conformity with [Article] [paragraphs --], it may request consultations with that other Party. That other Party shall promptly enter into consultations with the requesting Party and shall provide information to the requesting Party regarding the actions taken and the reasons therefor.]

## COMMENTARY

### **GENERAL EXCEPTIONS**

#### **Paragraph 1**

1. It has been proposed that the general exceptions provisions not be applicable to all of the obligations under the agreement. The ECT (Article 24(1)) is an example of a multilateral agreement that does not allow for general exceptions to be taken with regard to specific obligations concerning compensation for losses or expropriation. Bilateral treaty practice differs on this matter. Some delegations thought that a reference to paragraph 2(c) would be necessary to clarify that actions pursuant to a UN Charter obligation would in any case prevail over the MAI (see paragraph 9, below). One delegation submitted a proposal which would have the same effect by changing the order of the paragraphs.

2. The question is whether certain obligations of the agreement are considered so central to investor protection, for example compensation in case of expropriation, that a provision should limit the right of a Contracting Party to invoke this Article for actions that would be inconsistent with its obligation to pay compensation in the case of an expropriation.

3. The majority view was that the MAI should provide an absolute guarantee that an investor will be compensated for an expropriated investment. This was questioned by one delegation which doubted that in time of war whether a country would be able to pay compensation, in all cases, to an investor of a party with which it is in conflict. In the case that general exceptions would be permitted to override MAI obligations, delegations might further consider whether this should be limited to only essential security interests.

4. One delegation raised the issue of the need to ensure that this provision would not apply retroactively. Delegations pointed to customary international law rules limiting retroactive application of treaties. They agreed this was a valid point, but that it applied more generally to the entire agreement and should be addressed elsewhere.

#### **Paragraph 2**

-- subparagraph a

5. One delegation, supported by other delegations, requested square brackets be put around the phrase "which it considers" in the chapeau, as well as brackets around the phrase "or other emergency in international relations" at the end of (i). In the opinion of these delegations, these proposals would help safeguard against potential abuse by constraining the self-judging nature of the provision and by limiting its scope. One delegation believes that, based on an ICJ decision, such a change would eliminate the self-judging nature of the provision.

6. There were different views on whether to delete the phrase "including those" in the chapeau, which would make the list a closed one. Recent agreements like the NAFTA, the ECT, the GATS, and the Shipbuilding agreement do not define essential security interests but provide elements clarifying the purpose of the provision. One delegation thought that in a closed list it would also be necessary to amend element (ii) (by inserting the phrase "inter alia" after the word "non-proliferation") to cover international non-proliferation agreements, other than those relating to nuclear weapons for example agreements concerning chemical weapons. One delegation, supported by other delegations, proposed the inclusion of an additional element (iii).

-- subparagraph b

7. This provision is found in recent agreements (NAFTA, ECT, GATS, Shipbuilding). One delegation, supported by other delegations, requested that square brackets be put around the phrase "it considers" (to be replaced by "would be") to help safeguard against potential abuse by constraining the self-judging nature of the provision. One delegation believes that, based on an ICJ decision, such a change would eliminate the self-judging nature of the provision.

8. Several delegations noted that this issue also arose in the context of the discussion on transparency in the National Treatment chapter. One country pointed out that in its opinion this paragraph would also apply to concerns relating to public order.

-- subparagraph c

9. Agreements such as the NAFTA, GATS, and the Shipbuilding agreement include a general exception provision relating to obligations for the maintenance of international peace and security. These provisions refer specifically to obligations under the UN Charter. Some delegations thought it unnecessary to refer to this obligation because the supremacy of the UN Charter over international treaties is not disputed, but they agreed not to insist on its deletion if others wanted to make this explicit. Others were of the opinion that this reference was too restrictive because it might not cover actions taken pursuant to regional security arrangements. To address this point, one delegation proposed including, after the words "UN Charter", the phrase "or equivalent arrangements authorised by a competent international organisation". One country saw this as an issue of clarification rather than one of restrictiveness and suggested including, after the word "under", the phrase "or consistent with".

### **Paragraph 3**

10. Some countries believe that a reference to public order is necessary to allow countries to take exceptional measures based on this principle. One country indicated in a written submission [DAFFE/MAI/DG2/RD(96)2] that a public order clause was meant to ensure certain objectives, including the non-discriminatory application of its laws and the prevention of disturbances to the public order that could be posed by certain foreign investments. It thought that given the different circumstances of foreign and domestic investors as concerns the protection of public order, it would not be possible, in all cases, to accord equivalent treatment to these different types of investors. Delegations recognised the interest of a state in ensuring the application of its criminal laws, anti-terrorist measures, and money laundering regulations, for example. But not all delegations were convinced that it is necessary to discriminate between foreign and domestic investors in order to protect public order. One country remarked that if the MAI went beyond national treatment obligations to include the concept of market access, then the broader interpretation of public order would be necessary.

11. Several delegations were of the opinion that provision might need to be made for cases where information requirements or other formalities might be required of foreign investors because they are not in the same situation as domestic investors. This question also arose in the context of the discussion of the transfer provisions in the investment protection chapter where the host state would want to preserve its right to require certain reports without being in contradiction of the absolute right of free transfer otherwise provided by the agreement. Article 1111 of the NAFTA was cited as a possible model to take account of these situations. The question arose whether in fact this was not a matter of "equivalent treatment" which could be included in the context of national treatment.

12. In situations where the state needs to ensure that all investors conform to its laws and regulations which are not in contradiction with the provisions of the agreement, a provision of more general application might also be needed, as in Article 5 of the Capital Movements Code. The Group could consider a provision similar to that in the Code which would apply to the whole of the agreement. If this were the preferred solution, it might obviate the need for a special provision in the transfer article or elsewhere in the agreement where there might be similar concerns.

13. Several proposals were made with the intent to narrow the scope of a public order exception. One delegation proposed limiting the public order concept to exceptions to the national treatment principle and to make the MAI dispute settlement mechanism applicable. One country remarked, however, that if the MAI went beyond national treatment obligations to include the concept of market access, then the broader interpretation of public order would still be necessary. One delegation suggested a reference to the ECJ principles of proportionality and the exclusion of economic purposes as additional limitative qualifications to public order

14. Delegations in favour of including a public order exception agreed that its use should be strictly controlled. These delegations felt that the actions relating to public order would not be self-judging and would be subject to the limitation in paragraph 4 and to the procedures in paragraph 6. One country, supported by another country, stated that these limitations and procedures should apply in the same way to other general exceptions and that all general exceptions should be treated in the same way in relation to the applicability of the dispute settlement mechanism.

#### **Paragraph 4**

15. Paragraph 4 would apply to all exceptions in this article. It is another way of formulating the obligation that parties must be in good faith when invoking this article and cannot avail themselves of it as a pretext for not complying with their obligations under the agreement. A good faith obligation already exists in international law and one country has concerns that by restating it in the agreement, we may create a different standard. Some delegations thought it might be useful to follow the ECT (Article 24) and GATS (Article XIV) provisions that public order or other general exceptions must not constitute a disguised restriction or that they are invoked without proper justification. This paragraph could be considered to have the effect of allowing a party which had reason to believe that another party had made improper use of this article to challenge such use as contrary to the objectives of the article. A decision on paragraph 4, in the opinion of several delegations, would have to wait until such time that consideration of paragraphs 2 and 3 had been completed.

#### **Paragraph 5**

16. The content of this paragraph would need to await a discussion of the role of a "Parties Group". The requirement to notify measures is intended to facilitate transparency and to promote consistency in the manner that MAI Parties might apply the general exceptions provisions. Some delegations thought that the 1991 clarification by the CIME that "measures taken for economic, cultural or other reasons should be identified as such and should not be shielded by an excessively broad interpretation of public order and essential security interests..", might also assist the Parties in applying these provisions.

## Paragraph 6

17. Most delegations were in favour of providing for a mechanism for consultation/dispute settlement. It would be understood that entering into consultations would not prejudice the right of either Party to invoke the other procedures of the agreement to which it might be entitled. The question remains whether paragraph 4 provides an objective standard which, if violated, can give rise to an actionable cause.

18. Paragraph 6 could be adapted depending on how parties wish to proceed. There are several options which can be considered:

a) actions relating to any of the provisions of this article could be subject to consultations (as provided for in the article or by reference to the consultations procedures of the agreement), and to the dispute settlement provisions of the agreement to the extent that the provisions are not entirely self-judging;

b) actions relating to any of the provisions of this article could be subject to consultations (as provided for in this article or by reference to the consultations procedures of the agreement), to the exclusion of recourse to the dispute settlement provisions of the agreement;

c) actions relating to the public order provisions of paragraph 3, could be subject to consultations (as provided for in this article or by reference to the consultations procedures of the agreement), and to the dispute settlement provisions of the agreement.

19. In the view of one country, any dispute settlement mechanism provided in the MAI would be rendered superfluous by the self-judging nature of the general exception provisions. This delegation also questioned whether it would be necessary to provide a specific consultation mechanism in this article separate from the general consultation mechanism of the MAI.

20. Whatever the procedure agreed for general exceptions, it will have to be considered in the context of the MAI provisions on the role of the Parties Group and the dispute settlement procedures.