Expert Paper # 2

TPPA: CHAPTER 9 ON INVESTMENT

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Key points: Coverage; Sovereign right to regulate; Specific policy issues; Investor-state dispute settlement

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Negotiations for a Trans-Pacific Partnership Agreement (TPPA) were concluded in Atlanta, USA on 5 October 2015, and the text was released on 5 November 2015. There are twelve negotiating countries: Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States and Vietnam. The TPPA has 30 chapters and many annexes, with parties also adopting bilateral side-letters. They are expected to sign the agreement on 4 February 2016 in New Zealand, which is the formal depositary for the TPPA. Each party to the negotiations must complete its own constitutional processes and requirements before it can take steps to adopt the agreement. The TPPA will come into force within two years if all original signatories notify that they have completed their domestic processes, or after 2 years and 3 months if at least six of them, including the US and Japan, have done so. This research paper is part of a series of expert peer-reviewed analyses of different aspects of the text.

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Summary

- The investment chapter provides an overall greater level of protection for foreign investors and their investments as compared with New Zealand's existing trade and investment treaties.
- The protections include rules relating to non-discrimination, a minimum standard of treatment, and expropriation.
- The text includes novel safeguards which are aimed at clarifying the purpose of the rules and preserving policy space. Nonetheless, some issues are not addressed, and the scope of the rules and the exceptions (and therefore the government's right to regulate in the public interest) remains uncertain.
- While complete textual clarity is an unrealistic goal, alternative approaches to dealing with the uncertainty inherent in some investor protections include taking a more cautious approach to the rules, and providing stronger safeguards.
- The chapter also includes specific limits on policy making in areas such as investment screening, fiscal policy and economic development (through so-called "performance requirements").
- There are some exceptions to these obligations, but generally speaking, the exceptions are narrowly drawn. For example, the government can adjust the factors for screening investments into New Zealand under the Overseas Investment Act 2005, but cannot add new categories of investment into the screening regime.
- The screening threshold is raised from $100m to $200m.
- The commitments in the investment chapter are directly enforceable by TPPA investors through investor state arbitration.
- Investors can also take claims to arbitration on the basis of alleged breaches of certain types of government contracts, something that New Zealand has never agreed to before.
- There is a carve out for disputes relating to consent decisions under the Overseas Investment Act 2005.
- For other disputes, there is no requirement that investors to seek remedies in New Zealand courts first, before initiating a claim under the TPPA.

Introduction

The objectives of the investment chapter are to facilitate access for cross border investment between the TPPA countries and to protect TPPA investors both in terms of the process of investing and their investments once made.[1] This is achieved by conferring rights on investors that are directly enforceable by them through the dispute settlement provisions of the chapter. Early on in the negotiations, the TPPA negotiators also recognized the sensitivity of regulatory autonomy issues, in the sense that investor protections can constrain the regulatory powers of states. According to the Ministry of Foreign Affairs and Trade (MFAT), the investment chapter provides a "high quality yet balanced" framework of obligations, with "[n]umerous safeguards" that protect the Government's ability to regulate for legitimate policy reasons without the threat of legal proceedings initiated by foreign investors.[2] The question is whether the safeguards are sufficient to achieve this purpose.

The template for the investment negotiations was the model bilateral investment treaty (BIT) of the United States, the basic aim of which is the protection of United States investment abroad.[3] All countries, including the United States, have become increasingly protective of sovereign prerogatives in their investment treaty negotiations in recent years. Even so, the United States' approach is still considerably more pro-investor when compared to many others. It seems apparent from leaked texts that, during the negotiations, at least some of the other TPPA countries were pushing back in relation to the typical United States standards on a wide range of matters.[4] Nonetheless, the final text is still reflective of United States' preferences and the push-back was only partly successful.

Since the launch of the TPPA talks, New Zealand's negotiators have had to pursue the country's interests in promoting both outbound and inbound investment while also keeping a protective eye on domestic policy space. This note comments on some of the main features of the outcome of the investment negotiations with an emphasis on regulatory autonomy, including new ways of safeguarding the public interest.[5] I do not deal with the expected economic gains from either increased New Zealand investment into TPPA countries or increased investment from those countries into New Zealand.

1 A number of fact sheets were issued by TPPA trade officials after the negotiations were concluded to explain what the investment chapter aims to achieve. See for example "Summary of the Trans-Pacific Partnership Agreement" Office of the United States Trade Representative, <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2015/october/summary-trans-pacific-partnership>.

2 Ministry of Foreign Affairs and Trade (New Zealand) "Investment and ISDS" available <http://www.tpp.mfat.govt.nz/> ("MFAT Fact Sheet").

3 See Lee M Caplan and Jeremy K Sharpe "United States" in Chester Brown (ed) Commentaries on Selected Model Investment Treaties (Oxford, 2013) 755. The current 2012 model treaty is available <http://www.state.gov/e/eb/ifd/bit/>.

4 Other TPPA countries share many of the United States' preferences regarding investment, particularly Canada. Canada's model investment treaty is available <http://www.italaw.com/investment-treaties>.

5 Available http://tpp.mfat.govt.nz/text. The chapter is subject to legal review and authentication.

Coverage: who benefits?

(i) Relevant definitions

The investment chapter has wide application as a result of broad definitions, subject to standard but possibly ineffective provisions for excluding treaty shopping free-riders. In terms of the relevant definitions, an "investor of a Party" is defined as an investor that "attempts to make, is making, or has made" an investment; an investor will only be regarded as attempting to invest within the definition when it has taken "concrete action" to make its investment (art 9.1). The application of the definition to the whole life-cycle of an investment is consistent with the extensive nature of the non-discrimination obligations discussed below, as those obligations commence from the pre-establishment phase.

The definition of "investment" applies an asset-based test that has become standard in investment treaty practice. It covers both foreign portfolio and direct investment, including investment in intellectual property, rights under construction, concession and other contracts, and portfolio assets which are financial in nature (such as futures, options and derivatives). There is a requirement that the asset have the characteristics of an investment – for example, debt may not have the required characteristics if it relates to payments immediately due from the sale of goods.[6] That said, the scope of investments protected by the investment chapter is very wide. By way of comparison, in New Zealand's recent free trade agreement (FTA) with Korea, economic interests such as expected gains and opportunities for profit-making are expressly excluded.[7]

Some of New Zealand's trade and investment treaties provide, in the definition of "covered investment", that only investments which are admitted according to each host state's laws are entitled to benefit from the investor protections.[8] The underlying principle is that protection should be withheld from foreign investors that do not respect a host state's laws when making an investment.[9] There was a proposal to include text along these lines in a draft investment chapter that was leaked in 2012, but that proposal was dropped at least by January 2015, according to the second text that was leaked in March 2015. The omission may be significant for countries with relatively weak regulatory systems where compliance with legal requirements can be an issue. For this reason, it seems unlikely that it will have much practical significance for New Zealand. It is a further illustration though of investor interests being given priority over those of the host state's regulatory environment, especially since the requirement to comply with host state law when investing is one of the few instances where expectations are imposed on investors.

6 See e.g. Global Trading Corp and Globex International Inc v Ukraine ICSID Case No ARB/09/11 (Award (1 December 2010) (sale and purchase contracts were not investments for the purposes of the ICSID Convention)

7 New Zealand Korea FTA, art 10.2.

8 See ASEAN-Australia-New Zealand FTA, art 2 of ch 11; New Zealand-Malaysia FTA, art 10.1.

9 See Planet Mining Pty Ltd v. Republic of Indonesia, ICSID Case No. ARB/12/14 and 12/40, Jurisdiction, 24 February 2015 at [274].

(ii) Provisions to address treaty shopping

Treaty shopping in this context is the phenomenon where "free-rider" investors establish a legal presence in a state to take advantage of the benefits of a particular treaty. For states facing claims by such free-riders, this is objectionable for the simple reason that the investor's true home state is not a party to the treaty. As with most modern investment treaties, the TPPA includes a denial of benefits clause to address the problem (art 9.14). It provides that a state party may deny the benefits of the chapter to an investor that has no substantial business operations in any other state party. The denial of benefits clause also has a limited foreign policy carve out that allows TPPA countries to maintain sanctions regimes with respect to non-TPPA countries.

As is typical with these clauses, it does not say when the denial of benefits must take place. This is despite recent cases suggesting that states must exercise the right to deny the protections proactively and at least before the commencement of any arbitral proceedings.[10] Although there may be good reasons for interpreting the standard provisions this way, in reality, most states do not keep a watch on who is investing within their territories in order to make a decision on their eligibility to treaty protections. To ensure their effectiveness, denial of benefits provisions need to be more unequivocal about the matter, for example, by proclaiming that investors lacking the requisite connection with a state party do not benefit from the treaty; the onus is then on claimant investors to prove that connection.

(iii) Government contract claims and investment authorizations

One of the most controversial issues in the investment negotiations was whether the dispute settlement provisions would enable investors to bring claims based on alleged breaches of their rights under contracts with TPPA governments, as distinct from alleged breaches of the investment chapter.[11] The United States was reportedly alone in seeking the enforceability of contract claims in respect of contracts entered into before the TPPA comes into effect, and most TPPA countries opposed the inclusion of contract claims altogether.[12] Despite the opposition, the final agreement allows these kinds of claims to be made. This is a first for New Zealand, which has never agreed to arbitration of contract claims in its treaty practice to date.[13]

10 See e.g. Plama Consortium v Bulgaria, ICSID Case No. ARB/03/24, Jurisdiction, 8 February 2005; Yukos Universal Limited (Isle of Man) v the Russian Federation, PCA Case No. 227, Interim Award on Jurisdiction and Admissibility, 30 November 2009; Khan Resources Inc and others v Mongolia PCA Case No 2011-09, Jurisdiction, 25 July 2012. Contrast Pac Rim Cayman LLC v El Salvador, ICSID Case No. ARB/09/12, Jurisdiction, 1 June 2012, [4.84]-[4.91].

11 The enforcement of contract rights by investors against host states through investment treaty arbitration has developed from the umbrella clause obligation found in some investment treaties (see Anthony Sinclair "The Origins of the Umbrella Clause in the International Law of Investment Protection" (2004) 20(4) Arbitration International 411).

12 See Lori Wallach and Ben Beachy "Analysis of Leaked Trans-Pacific Partnership Investment Text" (Public Citizen, 25 March 2015) < citizen.org/documents/tpp-investment-leak-2015.pdf>.

13 See further David Williams QC and Amokura Kawharu Williams & Kawharu on Arbitration (LexisNexis, 2011) at [28.8] (observing that New Zealand has not agreed to the umbrella clause type of protection covering contract claims).

In the final text, "investment agreement" is defined to mean a contract between a TPPA state and an investor of another TPPA state in relation to some forms of exploitation of natural resources, the operation of public utilities, or government procurement (art 9.1).[14] Only contracts that are concluded and take effect after the TPPA enters into force are covered. In the dispute settlement part of the chapter, investors are conferred standing to bring proceedings for breaches of investment agreements (art 9.18.1). As a result, they do not need to enforce their contractual rights in the forum provided by the contract, such as a national court, unless that forum is one of a select group of arbitration institutions or rules.[15] Instead, investors can bypass that aspect of their agreement and seek resolution under the TPPA process instead.[16] If sued, the New Zealand Government could counterclaim (see art 9.18.2). In my view this is not a safeguard (although described as such by MFAT[17]), but completes the transfer of the litigation to the investment treaty arbitration process.

The TPPA also enables investors to bring proceedings alleging that the respondent state has "breached" an "investment authorization" granted by the applicable foreign investment authority. As with contract claims, the government may bring a counterclaim (see arts 9.1 and 9.18.1-2). In New Zealand, the relevant authority would be the Overseas Investment Office exercising the delegated functions of the responsible Ministers under the Overseas Investment Act 2005. Again, New Zealand has never agreed to this before. At the same time, is unclear how this right would apply in the New Zealand context. This is because the most obvious kind of alleged "breach" would involve government action to enforce the conditions of a consent (for example, relating to the employment of locals). While the need for such action might be disputed by the investor, through an exclusion, the enforcement of consent conditions by itself is not capable of founding a claim. A relevant breach might include revocation or amendment of a consent other than in accordance with the Act (such conduct could also lay the basis for an expropriation claim). Consent decisions themselves are not able to be submitted to the investor state dispute settlement process, as explained below.

A footnote to the definition of "investment authorization" provides that actions taken by a state to enforce laws of general application, such as competition, environmental, health or other regulatory laws, are not encompassed within the definition. This seems unusual, since the definition relates to what an investment authorization is, rather than to the grounds on which a claim for breach of an authorization may be made.

14 See definition in art 1, and fns 8 and 9.

15 See annex 9-L. The institutions and rules are the same as those provided for disputes concerning alleged breaches of Section A of the investment chapter, as well as the London-based LCIA and the Paris-based ICC. None of the regional arbitration centres are included in the list.

16 The governing law will be either the law specified in the agreement, or if there is none, the law of the respondent state party and any applicable international law. See art 9.24.2.

17 MFAT Fact Sheet at 4.

The sovereign right to regulate

(i) Express recognition

The Preamble to the TPPA includes the following general statement on the right to regulate:

> [The Parties recognize] their inherent right to regulate and resolve to preserve the flexibility of the Parties to set legislative and regulatory priorities, safeguard public welfare, and protect legitimate public welfare objectives, such as public health, safety, the environment, the conservation of living or non-living exhaustible natural resources, the integrity and stability of the financial system and public morals.

The right to regulate is not recognised in the preamble of the United States model BIT, although it is referred to in the preambles New Zealand's FTAs with China, Korea, Malaysia, Singapore and Thailand.[18] Tribunals have often relied on preambles to justify expansive interpretations of investor protections and / or their jurisdiction, where the preambles clearly indicated that the overriding objective of the treaty was investment promotion and protection. Preambular statements affirming the right to regulate are a more recent innovation, and at this stage their impact remains to be seen.

In the investment chapter itself, there is a more forthright statement that nothing in the chapter shall be construed as preventing a party from adopting any measure to ensure that investments are undertaken in a manner sensitive to environmental, health or other regulatory objectives (art 9.15). At present, there is a lack of caselaw to indicate the extent to which these kinds of clauses may lead a tribunal to prefer an interpretation that is more deferential to regulatory autonomy. The TPPA clause has circular language, because it states that regulatory measures must still be consistent with the chapter. In a recent case, *Tamimi v Oman*, the tribunal rejected an investor's claim for breach of the minimum standard in part in reliance on a very similar clause appearing in the United States-Oman FTA.[19] However, it remains the case that on its face, the TPPA provision appears to provide no additional protection, and only affirms the right to regulate in a manner consistent with the other terms of the investment chapter.

(ii) Non-discrimination

The investment chapter includes two provisions that are commonly found in most investment treaties and require non-discriminatory treatment of TPPA investors: national treatment, and most favoured nation treatment (MFN). National treatment requires foreign investors to be treated no less favourably in like circumstances to domestic investors. MFN requires foreign investors to be treated no less favourably in like circumstances to investors from third countries. MFN works as a ratchet, so that each successive treaty, to the extent that it is more favourable to investors than

18 As a matter of general international law regarding the interpretation of treaties, the preamble may be taken as evidence of relevant intent and context for the interpretation of commitments in the investment chapter. See Vienna Convention on the Law of Treaties (in force 27 January 1980) art 31(1)-(2).

19 Tamimi v Oman ICSID Case No ARB/11/33 Award, 3 November 2015 at [387]. The preamble, which contains a statement on sustainable development, reinforced the tribunal's view (at [389] note 777).

previous treaties, broadens the scope of the substantive protections available to investors covered by those previous treaties.[20] For New Zealand though, the significance of MFN is in the application of the rule under previous treaties rather than the TPPA. That is, the standard of protection under New Zealand's existing treaties will ratchet up to the level of protection established by the TPPA, to the extent the TPPA is more favourable. In general terms, the TPPA is more favourable to investors on many fronts, including those noted specifically below.

The text introduces new language about "like circumstances", recognizing both that the concept has been difficult to apply in practice and also that differential treatment of participants in a business or economic sector is not necessarily the outcome of protectionist discrimination. A footnote explains that it is relevant to consider whether the treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives. Unlike the reference to public welfare objectives in the annex on expropriation (below), public welfare objectives are not further defined. However, an interpretive "drafter's note" has also been issued by the parties to explain their shared intentions further, with references to cases decided under the North American Free Trade Agreement (NAFTA). In terms of regulatory autonomy, as the drafter's note explains, these cases emphasize the point that different treatment (as between foreign and domestic investors) may be justified by legitimate policy goals.[21]

(iii) The minimum standard of treatment

The TPPA includes two core investor protections that find their origins in customary international law, the so-called "minimum standard of treatment" (art 9.6), and rules regarding the expropriation of covered investments (including the obligation to compensate, art 9.7). The scope of both these protections warrant close scrutiny because of their potentially limiting impact on the ability of host governments to regulate in the public interest. That impact, and in particular the realization that expansive interpretations of these protections may undermine regulatory autonomy, has prompted states to be more directive about how they are expressed in their treaties. Different formulations have emerged reflecting differing levels of comfort regarding the balance between regulatory interests and investor protections.

In relation to the minimum standard of treatment, the TPPA obliges each state party to accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security (that is, the minimum standard of treatment, art 9.6). What is required by customary international law is then detailed in an interpretive annex (annex 9-A). In that annex, the standard of treatment is stated to refer to all customary principles

20 New Zealand's Annex II of non-conforming measures makes it clear that MFN under the TPPA applies to future treaties, not past ones.

21 One of the cases cited in the drafter's note is GAMI Investments Inc v Mexico NAFTA / UNCITRAL Award 15 November 2004. In this case, Mexico determined that several sugar mills operating in effective insolvency should be nationalized in the public interest. The investor's national treatment claim failed because its mill was nationalized not because of the foreign ownership, but in the interests of the Mexican economy in the broad sense. Also, public investment in an ailing strategic asset that is locally owned should not necessarily be seen as favourable treatment of a domestic investor, if the purpose of the investment is to ensure its ongoing operation in the public interest. This could be relevant in a New Zealand setting, given past issues with entities like Air New Zealand.

that protect the "investments of aliens". An earlier and more liberal proposal, which referred loosely to the "economic rights and interests of aliens", did not make the final cut.[22] Linking the standard to customary international law is intended to limit the scope of the protection in a way that is more deferential to host state regulatory autonomy. While this is an improvement on past practice, views remain divided as to whether this is effective or sufficient,[23] because its application to particular facts continues to produce controversial results.[24]

In view of the ongoing problems, the TPPA parties have introduced two new clauses to clarify the content of the minimum standard. According to these clauses, actions that may be inconsistent with an investor's expectations, and the withdrawal or amendment of a subsidy or grant, are deemed insufficient by themselves to constitute a breach of the minimum standard (arts 9.6.4 and 9.6.5). It has been suggested that the provision on expectations is aimed at foreclosing the possibility of a claim based on the investor's subjective expectations, rather than its legitimate (or reasonable and investment-backed) expectations.[25] If so, an expectations-based claim may still be possible, where a state arbitrarily departs from reasonable expectations.[26] This is despite recent state practice suggesting that investor expectations should not form the basis of a customary law

22 New Zealand has previously agreed to the "economic rights and interests" language – see annex 10-A New Zealand-Korea FTA.

23 The position of the United States Government is that tribunals are now more respectful of regulatory authority as a result of the refinements to the treaty language: M Kantor "Little Has Changed in the New US Model Bilateral BIT" (2012) 27(2) ICSID Rev 335, 352. New Zealand's Foreign Affairs, Defence and Trade Committee took a similar view in its report on the New Zealand-Korea FTA: Foreign Affairs, Defence and Trade Committee International treaty examination of the Free Trade Agreement between New Zealand and the Republic of Korea (May 2015) at 7. Compare Matthew C Porterfield "A Distinction Without a Difference? The Interpretation of Fair and Equitable Treatment Under Customary International Law by Investment Tribunals" (Investment Treaty News, 22 March 2013).

24 See, recently, Clayton / Bilcon of Delaware, Inc v Government of Canada (Bilcon v Canada), NAFTA / PCA Case No 2009-04, Award on Jurisdiction and Liability, 17 March 2015. One arbitrator, Professor Donald McRae, dissented from the majority's decision to uphold the investor's minimum standard of treatment claim against Canada. He cautioned that the decision could "chill" environmental regulation, to the extent that regulation giving weight to community values over scientific assessment is seen as unfair treatment. See Bilcon v Canada, Dissenting Opinion of Professor Donald McRae, 10 March 2015 at [51]. Part of the problem for Canada was that local officials made positive representations to the investor about its proposed investment. As explained above, the language around investor expectations does not adequately deal with how expectations can be factored into the assessment of the host government's conduct.

25 See Luke Eric Peterson "A first glance at the Investment Chapter of the TPP agreement: a familiar US-style structure with a few novel twists" (Investment Arbitration Reporter, 6 November 2015). Expectations are relevant to the assessment of expropriation claims (annex 9-B at 3(a)(ii)) and claims based on investment agreements (art 9.18.1).

26 Wording along these lines is included in the concluded FTA between Canada and the EU (CETA) and the EU's proposed text for its FTA with the United States (TTIP).

minimum standard claim at all.[27] In other words, the TPPA text could have been more emphatic about the issue.

The chapter also states that the investor has the burden of proving all the elements of its claim (art 9.22.7). At first this seems unusual, as claimants have always had the burden to establish their claims. The intent may be to clarify that the burden includes proving the content of customary law, and to emphasize that the standard should be understood in a holistic way. In practice, one of the problems with the minimum standard of treatment is that investors are allowed to discharge their burden easily by referring to past tribunal awards rather than state practice. If addressing this problem was the intent of the provision on burden of proof, it could have been made clearer.

(iv) Expropriation

Covered investments may be expropriated for a public purpose and on payment of compensation (see art 9.7). The meaning of expropriation has been elaborated in an annex (annex 9-B). As under most modern treaties, but unlike New Zealand domestic law, the TPPA encompasses indirect and therefore regulatory expropriation, where regulation has an adverse economic impact on an investment but the investment is not seized outright. The amount of compensation payable for the expropriation of an investment is prescribed by the treaty and not by national laws such as New Zealand's Public Works Act 1981.

Unlike fair and equitable treatment, the scope of the expropriation claim under the TPPA is not tethered to customary international law. This follows the rejection of an earlier proposal to align the obligations regarding expropriation with their origins in the beliefs and practices of states. Instead, the approach taken in the TPPA is closely modeled on United States practice, uses broad and sometimes vague language, and of the various iterations of text dealing with the matter, provides the least safeguarding of legitimate state regulation.

In particular, the text accepts that regulation in the public interest may, in "rare circumstances", constitute an indirect expropriation. Read against the other parts of the annex, "rare circumstances" will likely be construed narrowly. While this may be so, the text could have required the tribunal to adopt a narrow approach. For example, in an earlier draft, "rare circumstances" were expressly limited to the situations in which the state either discriminated against the investor, or breached a prior, binding written commitment to the investor. Another version from an earlier draft rejected outright the notion that non-discriminatory law making in pursuit of legitimate public welfare objectives could amount to compensable expropriation.

In each case, the tribunal has to conduct a fact specific enquiry to determine whether a measure amounts to indirect expropriation. The annex lists three non-exhaustive factors that a tribunal will need to consider in the enquiry for a given case. These are the economic impact of the challenged measure, the extent to which it interfered with the investor's reasonable expectations, and the character of the government action.

27 See e.g. submission of the United States in *Spence International Investments v Costa Rica* ICSID Case No ARB/10/23 17 April 2015 at [17]: "Neither the concepts of "good faith" nor "legitimate expectations" are component elements of "fair and equitable treatment" under customary international law that give rise to an independent host State obligation".

An attempt has been made to qualify what expectations are relevant through a footnote (note 36). The footnote provides that whether expectations are reasonable depends, for example, on whether they are backed by written and binding assurances by the host state. Unlike a version rejected from an earlier draft, the final text does not require the deprivation caused by the allegedly expropriatory measure to be severe and disproportionate to the public purpose, although it must have an effect "equivalent to direct expropriation" (annex 9-B, at para 3).

To a degree, New Zealand took a similar approach to the issue of expropriation in the investment protocol with Australia,[28] but it has otherwise been more cautious. The higher level of protection under the TPPA will now override that caution through the operation of the MFN rule in the earlier treaties. That is, the TPPA standard will have to be extended to non-TPPA investors who are entitled to MFN treatment under New Zealand's earlier treaties.

(v) General exceptions

Chapter 29 of the TPPA sets out several general exceptions that apply to the agreement as a whole. However, those modeled on the general exceptions in the World Trade Organization's (WTO) agreements relating to trade in goods and services do not apply to the investment chapter (art 29.1). This is consistent with standard United States FTA practice. Looking at the text, the negotiators' preferred approach seems to have been to integrate the public interest into the investor protections themselves, as in the elaboration of "like circumstances" and "expropriation" in annex 9-B discussed above. From the perspective of governments defending claims, this has the advantage of including the public interest in the substance of the claim that needs to be established by the investor. Exceptions, on the other hand, must be raised and proved by the party seeking to rely on them, that is, governments. On the other hand, it is not all that clear whether the added text will be effective in protecting the right to regulate in pursuit of the general public interest, and WTO-style general exceptions could have been useful as a fallback option.

Exceptions of general application include those dealing with security, balance of payments, taxation, the much talked-about issue of tobacco control measures (through a denial of benefits style provision), as well as the Treaty of Waitangi. The adequacy of the Treaty of Waitangi exception is the subject of a claim before the Waitangi Tribunal.

Specific policy issues

(i) Investment screening – Overseas Investment Act 2005

The national treatment obligation (art 9.4) requires foreign investors to be treated no less favourably in like circumstances to domestic investors. While readily acceptable at a basic level, national treatment is not just about non-discrimination in the usual sense of fairness and equality before the law. It is also used to facilitate access for foreign investment into countries where that access might not otherwise be allowed or might be subjected to conditions in relation to the establishment of a given investment.

28 New Zealand-Australia investment protocol (signed 16 February 2011, in force 1 March 2013) art 14. There is no interpretive annex. The protocol does not include an investor – state dispute settlement mechanism.

The TPPA promotes access for foreign investors, by defining "investor of a Party" to include an investor who attempts to make or is making an investment (as above), and by applying the national treatment rule from the pre-establishment phase. The policy implications of this for New Zealand relate to the fact that since 1968,[29] New Zealand has subjected foreign investment to a screening process to ensure that significant foreign investments in New Zealand are in the national interest. Currently, screening takes place under the Overseas Investment Act 2005 and associated regulations.

New Zealand's consistent treaty practice has been to exempt the Act from its national treatment obligations, and to reserve to itself the flexibility to amend the criteria for screening in the existing categories of screened investments, that is, fishing quota, sensitive land and significant business assets. Under the TPPA, the usual practice has been followed, and the Act is listed in New Zealand's two annexes of non-conforming measures (art 9.11 and associated annexes I and II).[30] The result is that the current operation of the Act can continue, and the screening criteria for existing categories can be changed. However, there is no flexibility to add new categories.[31]

This lack of future-proofing already seems to have raised the ire of the Labour Party in view of its policy proposal to restrict foreign investment in residential housing.[32] The National Government has responded that a concession has been allowed so that discriminatory taxes may be introduced to deal with the housing problem.[33] Both political parties should be concerned about the inability to use the Act to deal with other problems that might arise in the future and which are not currently foreseen. This is especially so since the Act does not deal with sensitive strategic investments other than through the blunt tool of a financial threshold and the wide definition of sensitive land.

To prevent the government from being harassed by investor-state arbitral proceedings in respect of the screening process, a decision to grant or refuse consent cannot be the subject of a claim under the dispute settlement provisions of the chapter (annex 9-H). In other words, disgruntled prospective TPPA investors will need to take their complaints through the normal judicial review process. Apart from actual decisions to grant or refuse consents, claims may be possible with respect to the administration of the Act. That is, annex 9-H does not provide a complete carve out for all types of possible claim relating to the Act from the investor-state dispute settlement process.

The screening threshold for investments in significant business assets has doubled from $100 million to $200 million, although for investments by "government sources" the threshold remains at $100 million. Given that the National Government described this as an easy concession to

29 Land Settlement Promotion and Land Acquisition Amendment Act 1968. Consent was also required for certain investments under regulations made under the Reserve Bank of New Zealand Act 1964.

30 The exemptions apply to art 9.9 (performance requirements) and art 9.10 (senior management), in addition to national treatment. Other exemptions for non-conforming measures also apply to art 9.5 (MFN).

31 See further Amokura Kawharu "The Admission of Foreign Investment under the TPP and RCEP: Regulatory Implications for New Zealand" (2015) 16 Journal of World Investment and Trade 1050.

32 "Little won't say if Labour supports TPP" (New Zealand Herald, 7 November 2015).

33 Audrey Young "Minister challenges Labour's objections to TPP" New Zealand Herald, 7 November 2015).

make,[34] it is not clear why it could not have been disclosed and debated before the text was finalized without compromising New Zealand's negotiating position. The change attracted some criticism, but will now be fixed once the TPPA enters into force.

The raised thresholds for screening will apply not only to TPPA investors, but also to investors that are entitled to MFN treatment under New Zealand's other FTAs (who would not be subject to the dispute settlement carve out). It will become important that the Overseas Investment Office has the expertise available to determine whether a prospective investor is a bona fide TPPA / other FTA investor and not a treaty shopping free-rider.

(ii) Financial policy

The investment chapter affects the ability to frame financial policy in several ways. This is an area of some complexity however, since the chapter also needs to be read alongside commitments regarding financial services and the general exceptions.

First, the chapter includes rules that oblige the TPPA parties to permit the free transfer of funds relating to covered investments into and out of their territories without delay (art 9.8). The rules are drafted widely to cover contributions to capital, as well as (for example) profits, interest, capital gains, dividends, and proceeds from the sale of an investment. As with prohibitions on performance requirements (below), the rules on free transfers are not derived from customary international law. Instead, they have been included in treaties because the ability to liquidate investments and convert investment-related funds into freely useable currency is regarded by many states as an important right of foreign investors, and / or on the basis of the neoclassical economic theory that capital account liberalization will help to promote a country's integration with the global economy.

The obligation to allow free transfers is subject to exceptions of an administrative and law enforcement nature, and to the general balance of payments exception for measures to prevent or mitigate threats to financial stability in chapter 29 (art 29.3). The scope for adopting such safeguard measures is severely constrained by the conditions in the exception. New Zealand has agreed to tight restrictions on balance of payments measures in past treaties, but the TPPA goes further, reflecting the fact that the practice of the United States is not to allow exceptions for such measures at all.[35] Policies involving capital controls and other macro financial measures that regulate transfers of funds such as financial transaction taxes are all but eliminated from the policy toolkit.

Secondly, because the chapter applies to financial services and services suppliers, any regulation of the financial sector will potentially be subject to review against the substantive commitments to investors in the financial services sector. While New Zealand's retail banking sector is almost entirely Australian-owned (and covered by the TPPA), the Australian banks already benefit from

34 Isaac Davison "Fewer investor checks under TPP" (New Zealand Herald, 9 October 2015).

35 Despite increased acceptance of the use of capital controls since the recent global financial crisis (see e.g. International Monetary Fund The Liberalization and Management of Capital Flows: An Institutional View (14 November 2012)). On United States policy, see further Kevin P Gallagher "Regaining Control? Capital Controls and the Global Financial Crisis" (Political Economy Research Institute Working Paper, February 2011) 11-12.

the protections available to them under the investment protocol between the two countries that was signed in 2011. The commitments to financial firms are subject to exceptions for certain non-conforming measures with respect to the investment chapter's rules concerning non-discrimination, senior management and performance requirements (art 9.11), as well as exceptions dealing with the provision of financial services and prudential measures elsewhere in the agreement.

Finally, there is a novel annex dealing with public debt (annex 9-G). Its existence clearly implies that the parties regard public debt to be a form of protected investment, although a recent investment arbitration tribunal was split on that question.[36] The purpose of the annex is to limit the scope and type of claims relating to public debt. It notes that investment in public debt "entails commercial risk", and reiterates that a claim relating to a default or non-payment of such debt must be based on one of the substantive investor protections of the investment chapter. It then restricts investor claims arising from a debt restructuring to non-discrimination claims and imposes a lengthy 270 day cooling-off period before the claim may be submitted.

(iii) Performance requirements

The investment chapter contains comprehensive prohibitions on "performance requirements" as conditions of foreign investment, such as requirements to buy locally produced goods or services and "advantages" such as subsidies and tax incentives that are conditioned on such requirements being met (art 9.9). The prohibitions apply to requirements affecting all investors, whether from a TPPA party or not.[37] As with provisions on free transfers, the prohibitions against performance requirements are not based on customary international law. Instead, they have emerged through treaty practice, particularly FTAs and investment treaties based on the model investment treaties of the United States and Canada. Performance requirements are also dealt with in a limited way under the WTO's Agreement on Trade Related Investment Measures (TRIMs); as its name suggests, the TRIMs only deals with performance requirements relating to trade in goods.

New Zealand is bound by the TRIMs and has agreed that the TRIMs applies to investments covered by the China, ASEAN and Malaysia FTAs. More recently, New Zealand has agreed to more extensive prohibitions on performance requirements in the investment protocol with Australia and the FTAs with Taiwan and Korea. A broad range of measures is likewise prohibited under the TPPA. Exceptions include existing measures, provided they are listed in New Zealand's annexes of non-conforming measures, and requirements to employ local workers. There are also limited exceptions for certain measures related to environmental protection, health, non-commercial government procurement and public welfare.

Under current policy settings, New Zealand tends not to offer the kind of incentives that might be construed as performance requirements under the TPPA, although there is no blanket policy against them either. For instance, in the film industry government grants have been made available to production companies calculated by reference expenditure on goods and services provided in

36 Poštová Banka v Hellenic Republic ICSID Case No. ARB/13/8 Award, 9 April 2015 at note 424. The definition of "investment" in relevant Greek BITs refer to "corporate" bonds only.

37 This was also the case under the 2011 investment protocol with Australia (art 7) so in effect the only new obligations under the TPPA arise from the wider scope of the prohibitions.

New Zealand. The expansiveness of the prohibitions in the TPPA will largely preclude a change towards greater use of performance requirements, unless covered by an express exception. For the film industry, there is an exception dealing with the promotion of film and television production in New Zealand.[38]

Investor – state dispute settlement

(i) The application of the dispute settlement provisions

The second part of the investment chapter (Section B) deals with dispute settlement. It confers standing on TPPA investors to bring claims directly against TPPA governments through an arbitral process. Investors are able to sue on the basis of an alleged breach of a substantive investor protection in Section A of the chapter (see art 9.18.1). As already noted, investors can also initiate proceedings alleging that a state has breached an investment contract or authorization, independently of any alleged breach of the investment chapter. At their choice, and following a six month "cooling off" period for settlement negotiations, a dispute may be submitted to arbitration (art 9.18).[39] Claims must be brought within three years and six months (art 9.20).

So far, and through a combination of BITs and FTAs, New Zealand has given binding consents to arbitrate potential claims by investors from China, Hong Kong, the ASEAN countries and Korea.[40] New Zealand's involvement in the investment treaty arbitration system will expand significantly through the TPPA, as will its exposure to claims. The increased exposure to claims results not just from the large number of TPPA parties, but also (a) from the fact that a significant proportion of investment into New Zealand is sourced from TPPA countries, including the most litigious in this arena – the United States,[41] (b) the wider scope of the investor protections in Section A, relative to the other FTAs to which New Zealand is a party, and (c) the application of Section B to investment contracts and authorizations.

This is subject to a notable exception. New Zealand and Australia propose to exchange side letters to carve out the application of Section B for Australian investors in New Zealand and vice versa. This follows past practice – New Zealand and Australia did not agree to an investor state dispute resolution process in their 2011 investment protocol, and excluded the bilateral operation of the investment chapter in the ASEAN-Australia-New Zealand FTA via a side-letter. The explanation given for the position taken in the investment protocol was that the countries enjoyed a unique and longstanding relationship and recognized each other's well established judicial systems.[42]

38 See Annex II-NZ-19. This exception is also found in New Zealand's other recent FTAs with Korea and Taiwan, but not in the earlier investment protocol with Australia.

39 For a discussion and comparison of the applicable procedures, see Williams and Kawharu at [27.2.2].

40 For discussion of the treaties entered into by 2011 (which excludes those with Taiwan and Korea, but includes a separate FTA with the ASEAN country Malaysia), see Williams and Kawharu, ch 30.

41 See Statistics New Zealand <stats.govt.nz/browse_for_stats/economic_indicators/balance_of_payments/investment-by-country.aspx> (accessed 10 November 2015).

42 MFAT, Protocol on Investment to the New Zealand – Australia Closer Economic Relations Trade Agreement National Interest Analysis, 25.

Other factors are probably also at play, including litigation risk (in view of the levels of foreign investment flows crossing the Tasman).[43]

(ii) Upgrading the process

There has been a massive increase in the investment treaty arbitration caseload since the early-2000s as compared with previous decades.[44] In turn, the increased visibility and impact on states has prompted calls for reform of the investment arbitration process to better reflect the public nature of the interests involved, improve efficiency, and improve the quality of decision-making. Some commentators and states have suggested that the mechanism should be abandoned altogether in favour of a completely new approach to resolving foreign investment related disputes.[45] The approach taken by the TPPA countries has been to endorse a series of procedural initiatives that have by now become fairly commonplace, including in some of New Zealand's FTAs. In summary:

i. tribunals may admit amicus curiae submissions from interested non-parties to the dispute (art 9.22);
ii. tribunals may deal with preliminary questions on an expedited basis, and strike out claims lacking merit (art 9.22.4-6);
iii. the newly created TPPA Commission may issue a joint interpretation on a matter in dispute and its interpretation will bind the tribunal (art 9.24.3);
iv. there is transparency of arbitral proceedings with exceptions for confidential information (art 9.23). Public information laws (such as New Zealand's Official Information Act 1982) "should" be applied in a manner sensitive to protecting confidential information arising in arbitral proceedings (9.23.5);
v. the amount of damages recoverable is limited to loss incurred in the capacity of an investor, so any trade-related or other losses would be excluded, and punitive damages and specific performance are also excluded (see art 9.28).

Section B includes a standard clause that prevents investors seeking redress through investment treaty arbitration in parallel with judicial review proceedings before domestic courts. It requires investors to waive their rights to continue with domestic proceedings as a condition of bringing claims before an investment treaty tribunal (art 9.20). No explanation has been provided to date as to why the TPPA parties allowed a much stricter approach to be taken for claims against Chile, Peru, Mexico and Viet Nam (see annex 9-J). For those countries, if an investor initiates a claim in domestic courts, that will be the end of the matter insofar as the TPPA is concerned:

43 On the exclusion of investment treaty arbitration from the Australia-United States FTA, see William S Dodge "Investor State Dispute Settlement Between Developed Countries: Reflections on the Australia-United States Free Trade Agreement" (2006) 39(1) Vanderbilt J Trans'l L 1, 26; on Australian policy in this area, see Jurgen Kurtz and Luke Nottage "Investment Treaty Arbitration 'Down Under': Policy and Politics in Australia" (2015) 30(2) ICSID Review 465.

44 See UNCTAD IIA Issues Note (February 2015).

45 For discussion of the problems and possible solutions, see generally Michael Waibel and others (eds) The Backlash Against Investment Arbitration: Perceptions and Reality (Kluwer, 2010); UNCTAD IIA Issues Note – Reform of the IIA Regime: Four Paths of Action and a Way Forward (June 2014).

the election to try their luck in domestic courts will be definitive and exclusive, and not a prelude to investment treaty arbitration. One of the TPPA group (it is not clear which) had proposed to require investors to attempt to seek remedies in domestic courts first, at least for up to 12 months, as a precondition to the bringing of a claim under the TPPA. The proposal was not accepted, reflecting that requiring such resort to local remedies is still not widely accepted by states in their treaty practice.

The lack of rigorous regulation of arbitrators has become a hot topic in recent years, yet there are no provisions addressing arbitrator integrity in the text. Instead, the parties have agreed to develop a code of ethics (9.21.6). It is not clear why they were not able to do this as part of the negotiations to date – perhaps it was not a priority. The parties could refer to the code developed under the recent Australia China FTA for guidance (annex 9-A of that agreement).

There is also no agreement on creating an appeals facility to provide oversight of tribunal awards and improve consistency in decision making. Instead, the text merely provides that if such a facility is developed (and it has been on the reform agenda for many years), then the parties will consider its application to the TPPA, repeating a provision found in many FTAs that so far has paid only lip-service to the idea. This seems like a lost opportunity, given the parties have recognized elsewhere in the agreement that the scale of the TPPA project demands institutional developments, such as the TPPA commission, to support the agreement over the long term.[46] There is a novel requirement that the tribunal provide its draft award to the parties, but this may just prolong dispute resolution (art 9.22.10).

Conclusion

The investment chapter adopts many of the now familiar provisions intended to preserve policy space, and adopts several new ones through a patchwork of exceptions, savings, clarifications and annexes. To this extent, the final agreed text is an improvement on the standard policy safeguards that are included in the United States model BIT. At the same time, more safeguards are needed, because the starting point, the United States model BIT, is a pro-investor template. The chapter takes what might be called moderate approaches to safeguards on core issues like expropriation. This must mean something, and tribunals could reasonably determine that a lower level of safeguarding was intended as compared to other recent investment treaties involving New Zealand and other TPPA countries, increasing legal uncertainty and risk. Again, stating the obvious, agreeing to arbitrate claims made by investors from countries with high levels of inwards investment into New Zealand also increases risk. New Zealand's courts should feel somewhat left out in the cold, through the provisions allowing arbitration of contract claims and the lack of any requirement for prior resort to local remedies.

46 The European Union has recently proposed an appellate mechanism for the TTIP. See <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1364> (accessed 10 November 2015).

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