

ANALYSIS OF THE STATE-OWNED ENTERPRISES CHAPTER

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1. A Snapshot of the State-owned Enterprises ('SOE') chapter¹

- A state-owned enterprise ('SOE') or designated monopoly must comply with all the central government's obligations under the entire TPPA when it carries out a regulatory, administrative or other authority delegated to it or that it has been directed to undertake.²
- A SOE must operate like a private business, using purely commercial considerations when it buys and sells a good or service.³
- The SOE doesn't have to apply purely commercial considerations where, and to the extent that, it has a public mandate to deliver a good or service, but it still can't give preferences to local services and suppliers.⁴
- Any administrative body that regulates a SOE must exercise its regulatory discretion impartially in relation to all the entities it regulates.⁵
- 'Non-commercial assistance' provided, directly or indirectly, by government to a SOE through direct financial support or preferential provision of goods and services can be challenged where it causes 'adverse effects' to 'another Party's interests'.⁶
- The rule on non-commercial assistance does not apply to domestic services supplied by a SOE, but does apply to their cross-border services and to production of goods, which are often institutionally intertwined.⁷
- In addition to the general transparency obligations in Chapter 26, a government must respond to requests for specific information about a SOE and provide extensive information if a dispute is initiated. Failure to respond or do so adequately can attract adverse inferences against the responding state.⁸

2. Why the SOE chapter is significant

The State-owned Enterprises chapter is novel. It was driven by the US and faced strong resistance from all other negotiating parties for several years. Gradually that was broken down, but it was one of the last chapters to be concluded. The rules and coverage are more onerous and intrusive than in existing FTAs, where they are usually limited to a couple of provisions. Previously, the most extensive rules on SOEs were in the US

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² Article 17.3.

³ Article 17.4.

⁴ Article 17.4.1(a).

⁵ Article 17.5.2.

⁶ Article 17.6.

⁷ Article 17.6.4.

⁸ Article 17.10.

Singapore FTA. The TPPA overall goes further, but it does not include the explicitly asymmetrical obligations, notably the requirement for Singapore to privatise.⁹

3. What is the object of this chapter?

US businesses and unions complain that state-supported competitors have an unfair advantage in their homes countries, in the US, and in third countries involved in the TPPA and beyond. Their main target is China, and this chapter exemplifies the use of the TPPA to establish precedent-setting rules that would constrain China's growing role offshore. In President Obama's own words, the goal is to ensure that America US makes the rules for the global economy in the 21st century, not China.¹⁰ The chapter also challenges the state-managed economies of East Asia such as Vietnam, Malaysia, Brunei, and to some extent Singapore, and the dominant role of Japan Post's bank, insurance and delivery network.

4. Why was there such resistance to the SOE chapter?

Public corporations and monopolies are created for a variety of public purposes, including economic development, support for local businesses, employment, regional development, social and cultural needs, and infrastructure. Many now have mixed functions, but the fact that even fully commercialised enterprises are still state owned shows they retain important public roles, especially those engaged in services. In a country like Vietnam, SOEs are undergoing reform but remain a pivotal part of the economy. Other countries have a smaller number of prominent corporations, such as oil, gas and mining, or sovereign wealth funds, or that perform important social or infrastructure functions. In an attempt to address these sensitivities, the chapter provides partial protection for SOEs that deliver services and perform publicly mandated functions domestically. But these provisions only apply to services, not goods, and only to domestic activities. They are complex and untested.

5. Is this chapter promoting privatisation?

Unlike the Singapore US FTA there is no reference to privatisation. Nor is that the inevitable outcome of the chapter. But it becomes more likely. As a SOE becomes more fully commercial, the pressure to privatise always intensifies. Corporatisation is promoted in the name of improving efficiencies, especially by introducing competition. Once a public entity is corporatised, the rationale for it remaining public is undermined, aside from providing a revenue stream to government. Partial privatisation is presented as a

⁹ Singapore is required in Article 12.2.3(f) to 'continue reducing, with a goal of substantially eliminating, its aggregate ownership and other interests that confer effective influence in entities organized under the laws of Singapore'.

¹⁰ <https://www.whitehouse.gov/blog/2015/02/18/president-obama-writing-rules-21st-century-trade>.

benign way of bringing in new equity or paying down corporate or public debt, while maintaining public control. Selling a minority stake creates investor demand and dilutes political resistance to full privatisation down the track.

At the same time, negotiators faced a paradox: states have had to rescue systematically important former SOEs, including banks, airlines, railways, water and other utilities, when privatised businesses failed, often through profit or asset stripping, or when market or social failures created unacceptable costs. During the global financial crisis, the US government became the owner of banks and insurers and the (then) world's largest automobile manufacturer. The US made sure the chapter has special protection for states' responses to an economic crisis, but there is very limited scope for the rescue of a failed SOE at other times.

6. What state activities does the chapter apply to?

The chapter applies to activities of a SOE or Designated Monopoly (DM) that **affect trade or investment** between the TPPA parties.¹¹

Comment: The reach of the chapter is extremely broad. Trade or investment is a generic term, not limited to specific industries or transactions, and there is no requirement for the impact to be serious or, for most rules, even significant. Moreover, 'affect' has been interpreted broadly by the WTO to mean the activity 'has an effect on' trade in goods or services or on investment. It requires an actual or predictable effect, not purely a hypothetical impact.¹² The burden of proving this nexus is on the complainant in a dispute.

7. Does the chapter only apply to TPPA countries?

The chapter applies to all TPPA parties, with delayed implementation by some countries for some obligations. However, one rule - against receiving non-commercial assistance to SOEs that causes adverse effects to another party's interests¹³ - extends to effects of that assistance in the market of a country that is not party to the TPPA.

Comment: Remarkably, this substantive extension to the scope of the chapter into the territories of non-parties is set out in a footnote.¹⁴

¹¹ Article 17.2.

¹² *EC – Bananas III* (WT/DS27/AB/R), para 220.

¹³ Presumably only where these arise from non-commercial assistance, as per Article 17.7.1.

¹⁴ Above n 9.

8. How is a state-owned enterprise defined?

A **state-owned enterprise** is defined as an enterprise that meets three criteria:

- (i) The government owns more than 50% share capital in an enterprise or can appoint a majority of members of the board or equivalent management body or controls the exercise of more than 50% of voting rights.

Comment: SOEs in which government controls a minority share or appointments are not covered. A SOE in which the government controls voting rights over certain key decisions through a golden share is not explicitly addressed. The transparency obligations include disclosure of such shares, which implies that they are seen as a form of 'control', but that is debatable.¹⁵

and

- (ii) Such an enterprise must principally engage in 'commercial activities',¹⁶ which are defined as activities that are undertaken with an 'orientation to profit-making'.

Comment: The chapter applies to entities that perform a mixture of commercial and non-commercial functions. 'Orientation' is not a familiar term in international trade law. Dictionary definitions are unhelpful – they suggest an expectation that the principal activities of the SOE should look to make a profit. The SOE doesn't need to actually make a profit, provided that is its orientation. Where a mixed-purpose SOE has profit making as an explicit statutory obligation or directive it will clearly be covered. Where it is not explicit, the status of the enterprise may be contested.

There is an important clarification in footnote 1 that 'orientation to profit-making' does not include an enterprise that operates on a not-for-profit or on a cost-recovery basis.

Comment: This footnote refers to the entire enterprise, not to selected activities. If it is deemed to have an overall orientation to profit making but has some non-profit activities, it appears to be covered by the chapter. The meaning of 'cost-recovery' is also debatable. The government may require a SOE to achieve surpluses as a buffer to future downturns. Many entities also recover more than immediate costs and retain earnings for contingencies against shifts in government funding. Some enterprises may earn profits from certain activities to make up for shortfalls in government funding of other activities; if they comprise a growing proportion of income as government support declines, there will be questions about which activities are its 'principal' function. Retained earnings to fund future infrastructure and expansion or make provision for depreciation and interest

¹⁵ Article 17.10.3(b).

¹⁶ Article 17.1.

on future borrowings might also be challenged, raising arguments about standard accounting practices.

and

- (iii) The commercial activities of the enterprise involve the production of goods or services that are sold to a consumer and the enterprise determines how much it produces and the price.

Comments: This means an enterprise where government sets the prices or production levels of its activities is not treated as an SOE, but will be a state enterprise or designated monopoly.

9. Does the chapter apply to any other state entities?

State enterprises, not just state-owned enterprises, are subject to several rules. A state enterprise is defined in chapter 1 as an enterprise owned or controlled through ownership interests by a Party. An ‘enterprise’ means ‘any entity constituted or organized under applicable law, whether or not for profit, and whether privately or governmentally owned or controlled, including any corporation, trust, partnership, sole proprietorship, joint venture, association, or similar organization’.

Comment: State enterprises are required to comply with the government’s obligations in the entire TPPA when exercising delegated authority.¹⁷ They also cannot provide non-commercial assistance (financial support and preferential goods and services) to a SOE that causes adverse effects to another Party’s interests.¹⁸ Thirdly, state enterprises are subject to the transparency (disclosure) obligations.¹⁹ The definition is so broad it is impossible to predict which public bodies other states might argue are covered.

- **‘Designated monopolies’ (DMs)**, defined as existing and future public monopolies, and privately owned monopolies created after the agreement comes into force, must also comply with many rules in the chapter.

Comment: The chapter is formally called State-Owned Enterprises and Designated Monopolies and the obligations on DMs are extensive. They are required to comply with the entire TPPA when exercising delegated authority,²⁰ apply commercial considerations to sale and purchase of goods and services,²¹ not engage in anti-competitive practices in

¹⁷ Article 17.3.

¹⁸ Article 17.6.2.

¹⁹ Article 17.10.5.

²⁰ Article 17.3.

²¹ Article 17.4.2(b)-(c).

non-monopolised markets,²² and comply with transparency obligations.²³ A DM can also be an SOE and would be required to meet the responsibilities of both.

10. Core rules

Each of the core rules imposes different and complex obligations on SOEs and often on DMs and state enterprises.

A) A state enterprise, SOE and DM must comply with the rest of the TPPA when it carries out a regulatory, administrative or other authority delegated to it or it has been directed to undertake.²⁴

Comment: Whether an entity, such as a SOE, must comply with the international law obligations of its state owner when exercising authority delegated by the state is not settled at international law.²⁵ The broad range of state enterprises, SOEs and DMs are required to comply with its parent state's obligations in the entire TPPA, including chapters on investment, intellectual property, government procurement, telecommunications, transparency and regulatory coherence, when exercising delegated authority. Footnote 12 gives examples of a delegated authority: any licensing role (e.g. mining, forestry, telecommunications, broadcasting, transport²⁶), setting fees or charges (insurance levies, water charges, telecom licensing fees), allocating quotas (e.g. import licenses, water allocation, fish catch), or powers to expropriate (ports authorities, national park boards).

These obligations carry onerous compliance requirements and significant new legal risks. It is impossible to exclude any entity or activity from compliance with this rule, unless it falls within the small number of total carve-outs.²⁷ It is also not possible to opt out of this obligation by scheduling a non-conforming measure.²⁸

The application to state enterprises is especially significant, as it imposes potentially far-reaching obligations on public entities that are not principally engaged in commercial activities, including a not-for-profit or cost-recovery entities. The definition of 'state enterprise' is so broad and uncertain it could expose entities engaged with health,

²² Article 17.4.2(d).

²³ Article 17.10.2 and 3.

²⁴ Article 17.3.

²⁵ 'Draft articles on Responsibility of States for Internationally Wrongful Acts,' adopted by the International Law Commission (ILC) at its fifty-third session in 2001 and submitted to the General Assembly as part of the Commission's report covering the work of that session (A/56/10), remain a proposal and states have repeatedly declined to formalise this into a treaty.

²⁶ The specific illustrations are the author's.

²⁷ An independent pension fund (Article 17.2.6) and government procurement as narrowly defined (Article 17.2.7).

²⁸ Article 17.2.11.

education, broadcasting, research, environmental or cultural activities to the full force of the TPPA.

B) Non-discrimination when a SOE buys or sells goods and services as part of its commercial activities.²⁹

Comments: This rule applies to activities that have an orientation to profit-making and result in supply of a good or service for sale to consumers. When a SOE buys or sells a good or service it must treat an enterprise from a TPPA party, including a foreign investment inside its territory, no less favourably than a firm from its own country or from any other country, including a non-TPPA party (although it can still discriminate on the basis of commercial considerations).

C) A SOE must act according to commercial considerations when it buys or sells a good or service, unless it is fulfilling the terms of a public service mandate within its territory.³⁰

Comment: ‘Commercial considerations’ are factors that a private enterprise in a similar business would take into account, such as price, quality, demand and supply, transportation, marketability. In other words, the SOE should act as if it was a private firm engaged in the same activity.

There is an exception where the SOE is fulfilling a ‘public service mandate’ within the country. The government must have mandated the SOE to make a service available, directly or indirectly, to the general public. When the SOE sells the publicly mandated service it still can’t discriminate by treating a foreign investment by a TPPA country (a covered investment) less favourably than a domestic firm or a firm from any other country (including a non-TPPA party).

This distinction poses practical problems for a SOE whose publicly mandated services operate within and beyond the territory (e.g. broadcasting, post, telecoms, banking, insurance), and which are functionally integrated and practically indivisible. Likewise, it is problematic for a SOE that produces mandated and non-mandated services (e.g. preferential and commercial housing finance, public and commercial aspects of broadcasting, subsidised and unsubsidised public transport) through integrated operations. Further problems arise where a SOE produces goods as inputs or items for sale (e.g. state forestry, IT development, railways, government print, telecommunications) as well as services.

²⁹ Article 17.4.1 (b)-(c).

³⁰ Article 17.4.1(a).

D) Designated monopolies must apply commercial considerations when buying or selling the monopoly good or service, unless that activity is part of their designation and even then they can't give preferences to local goods or services.³¹

Comment: The aim is to ensure that monopolies act on a fully commercial and competitively neutral basis with foreign (and domestic) competitors when buying and selling the monopoly goods and services. Even when acting within the terms of their monopoly they cannot give preferences to local suppliers or purchasers of goods or services.

E) A designated monopoly cannot use its monopoly position to engage in 'anticompetitive practices' in the non-monopolised market within its country where that negatively affects trade or investment between the parties.³²

Comment: This is not a ban on cross-subsidisation per se. The anti-competitive practice must negatively affect trade or investment with another TPPA country. The competing country bears the burden of proof of showing a negative effect. But the wording is very broad and it does not require the negative affect to be serious. The right of the other country to demand information³³ (discussed below) and potential for challenges at the SOE committee could impose onerous obligations and be used to build the grounds for a dispute.

F) Direct or indirect 'non-commercial assistance' to a SOE with respect to production or sale of goods or of services offshore, must not cause adverse effects to the interests of another Party.

Comment: This provision is complex and spans three articles: Article 17.6 sets out the rule, then Articles 17.7 and 17.8 provide ways of assessing adverse effects and injury. Each element is set out below.

- 'Non-commercial assistance' can take two forms: (i) financial support and (ii) the provision of goods or services on more favourable terms than those commercially available.³⁴

Comment: Financial assistance involves direct fund transfers, or potential transfers of funds or liabilities, through grants, debt forgiveness, loans and loan guarantees, other types of financing on terms more favourable than commercially available to the SOE, or

³¹ Article 17.4.2(b).

³² Article 17.4.2(d).

³³ Article 17.10.3.

³⁴ Article 17.1 definition of 'non-commercial assistance'.

injections of equity capital inconsistent with usual investment practices of private investors. This implies some kind of active assistance and is narrower than early suggestions that even a SOE's credit rating that benefits indirectly from state ownership should be considered as assistance. However, there is still a risk that an implied guarantee that benefits credit ratings and/or interest rates might be challenged.

There is flexibility for provision of general infrastructure in the requirement of neutral provision of goods or services.

- **The assistance to the SOE must be by virtue of its government ownership or control.³⁵**

Comment: This can be established in various ways: the assistance is limited to SOEs, or SOEs predominantly use the assistance, or they are provided with a disproportionately large amount of it, or benefit from its discretionary provision.

- **The assistance is only subject to the rule if it relates to (i) the production and sale of a good by the SOE, or (ii) the supply of a service by the SOE across the border into another TPPA country or as a covered investment in another TPPA country or in a third country.**

Comment: The limited application to services is meant to protect the government's right to support a SOE when it provides a service within its own country.³⁶ But, as with the attempt to protect mandated services in the rule on commercial considerations, it raises problems for SOEs that have integrated production of goods and services, and that supply services both domestically and offshore.

- **The assistance must cause adverse effects**

Comment: Once non-commercial assistance has been established, there must be a causal nexus shown between that assistance and an adverse effect. Footnote 17 makes it clear that other potential causal factors must be examined. It may be extremely difficult to differentiate those factors or attribute proportionality, especially for services where consumer choice is affected by multiple, usually subjective factors.

- **The adverse effects must be caused to the 'interests of another Party'**

Comment: The phrase 'adverse effects to the interests of another Party' is drawn from Article 5 of the WTO Agreement on Subsidies and Countervailing Measures. That arises in a much more specific context than here and it applies in the WTO to goods, not services.

³⁵ Article 17.1 definition of 'non-commercial assistance'.

³⁶ Article 17.6.4.

The WTO case law focuses on the adverse effects of subsidies, not on defining what the ‘interests’ of the other party are. That is a broad and largely unfettered term, and could even apply to non-economic interests.

- **One adverse effect arises where the non-commercial assistance displaces or impedes imports or sale of goods from another TPPA Party. An adverse effect can also arise if the displacement or impediment is in the market of another TPPA country or a non-party.**

Comment: Several forms of ‘adverse effects’ for goods are identified. One test is whether the advantage has displaced ‘like’ goods from another TPPA Party in the home market of the SOE or has impeded their market share. The same test applies if the goods are imported or produced by a covered investor inside the country.³⁷

These effects can be judged in various ways: by a significant change in relative market share of ‘like’ goods, through a significant increase in the SOE’s market share, maintaining a constant share when it was expected to decline, or a less than expected decline in that share than would have happened without the assistance. The change should be tracked over a representative period of at least one year.³⁸

- **Another adverse effect is that the non-commercial assistance significantly undercuts the price of competing goods from another TPPA party**

Comment: This applies where the SOE’s goods ‘significantly’ undercut the price of competing ‘like’ goods of another party, whether the goods are imported or produced by a covered investment, and whether the effect is in the market of a TPPA or non-TPPA country.³⁹ This ‘includes’ situations where a comparison of prices for domestic and imported ‘like’ goods shows undercutting; those comparisons must be at the same level of trade at comparable times, and take due account of factors that affect price comparisons.⁴⁰

These tests are adapted from the WTO Agreement on Subsidies and Countervailing Measures. That means there is some jurisprudence, but even the WTO test it is difficult to apply and calculations are strongly contested in a dispute.

³⁷ Article 17.7.1(a).

³⁸ Article 17.7.2.

³⁹ Article 17.7.1(c).

⁴⁰ Article 17.7.3 and 17.7.4.

- A third possibility is that the non-commercial assistance displaces or impedes imports or sale of services,⁴¹ or significantly undercuts the price of a ‘like’ service,⁴² from another TPPA party.

Comment: This applies a parallel test to services, and is to be assessed using similar criteria.⁴³ But services and services markets, such as media, education or tourism, are fundamentally different from commodities and commodity markets. Market share and price cannot be compared in the same way, because of the intangible and social nature of services and the complex factors behind people’s preferences and the determinants of services markets. Adapting the WTO jurisprudence on goods will be very problematic. The novelty and uncertainty of ‘adverse effects’ in relation to services leaves countries very vulnerable to pressure and potential disputes, especially where the service supplier also provides cross-border services or supplies goods.

- G) A SOE that is a covered investment in another TPPA country and receives non-commercial assistance to produce or sell goods in that country, must not cause injury to the domestic industry of the host country where they produce ‘like’ goods.⁴⁴**

Comment: There is a complex test to show there is an actual or threatened material injury to a domestic industry that produces ‘like’ goods or establish such an industry has retarded.⁴⁵ First, there must be positive evidence that considers the volume of production, the effect of the financial assistance on price and on the domestic producer of like goods, and assesses broad indicators about the state of the domestic industry. Then a causal relationship must be established between the assistance and the injury, considering other known factors, such as changes in the market, new technology, and the export performance and productivity of the domestic industry affected. A complaint of a threat of injury requires evidence that the impact is clearly foreseen and imminent.

- H) Non-commercial assistance provided before the TPPA was signed is protected. So is new assistance for three years after signing the TPPA, so long as it was provided under a law passed, or a contractual obligation undertaken, before the TPPA was signed.⁴⁶**

Comment: This provision seems designed to restrict governments from introducing new supports in the period between finalisation of the TPPA and it coming into force. The protection for assistance provided before signing appears to mean that assistance

⁴¹ Article 17.7.1(d).

⁴² Article 17.7.1(e).

⁴³ Article 17.2 and 17.3.

⁴⁴ Article 17.6.3.

⁴⁵ Article 17.8.

⁴⁶ Article 17.7.5.

provided up to 4 February 2016 is protected, but not assistance that is provided between signing and the TPPA coming into force, unless the empowering legislation was already in place when the TPPA was signed on 4 February 2016 (not its coming into force). This means that governments can no longer pass such laws. New support has a limited life, until 4 February 2019.

D) Initial capitalisation of an SOE, or acquiring a controlling interest in an enterprise, is also protected where it is principally engaged in supplying services within the territory.⁴⁷

Comment: This is an important but very limited form of future proofing. It only applies to services, not goods. ‘Principally’ supplying services in the territory allows for some offshore provision and some goods production, but it is contestable. Another problem is that the exception only applies to initial capitalisation or acquisition of an interest, not ongoing support while it gets established and, if necessary, beyond. That would need to come under a separate exception. The provision also does not protect a government that is a majority owner of a SOE and buys more of the shares, or provides financial support when a strategically important SOE is in trouble for reasons other than an economic crisis.

11. Foreign SOEs must be subject to domestic courts

Domestic courts must be given the same jurisdiction over civil claims against foreign owned or controlled SOEs as applies to domestic enterprises.⁴⁸

Comment: This is intended to remove any question of sovereign immunity in jurisdictions where that extends to a government owned corporation, and the uncertain status of state-owned enterprises at international law. It is unclear how far that might go – for example, whether foreign workers could take action against a foreign controlled SOE for loss they suffered due to breaches of the host country’s labour laws.

12. Which state entities are excluded from the chapter?

- If the **annual revenue that a SOE or DM derives from commercial activities in any one of the three previous fiscal years was below a specified threshold** it will be exempt from the core rules on non-discriminatory treatment of TPPA countries’ goods and services, applying commercial considerations, and receiving non-commercial assistance, but not the obligations to comply with the rest of the TPPA when exercising delegated authority.

⁴⁷ Art 17.7.6.

⁴⁸ Article 17.5.1.

Comment: The obligation to comply with the other chapters of the TPPA is especially onerous, and the legal risks are much higher, for SOEs below the threshold. That threshold is set at 200 million IMF special drawing rights (about US\$376 million⁴⁹) from the date the agreement enters into force, and will be adjusted on a three-yearly basis.⁵⁰ Vietnam, Brunei and Malaysia have a higher threshold (500 million SDR) for the first 5 years.⁵¹

- **An individual party can list activities of a SOE or DM that are not required to comply with rules on non-discrimination, applying commercial objectives and receiving non-commercial assistance, but not the obligations to comply with the rest of the TPPA when exercising delegated authority.⁵²**

Comment: This is a negative list of activities (not of specific SOEs) that do not need to comply with specified rules. It does not apply to the requirement that state enterprises, SOEs or DMs performing delegated functions must comply with entire agreement, or to the procedural and disclosure obligations in the SOE chapter.⁵³ Any current or future SOEs, current or future public monopolies, or future private designated monopolies that a country has not listed will be covered by all the rules of the SOE chapter. Singapore and Japan did not list any.

- **Each party could specify in an Annex⁵⁴ the sub-central government SOEs and DMs that are excluded from the rules on non-discrimination, applying commercial objectives, receiving non-commercial assistance and transparency. Negotiations to extend the application of the chapter to activities listed in the Annex must take place within 5 years after the TPPA enters into force.⁵⁵**

Comment: These exclusions coupled with future negotiations reflects a tension between countries with federal jurisdictions, who were unwilling or constitutionally unable to bind their states or provinces, and unitary governments that felt they were effectively accepting more extensive coverage than the rest. There is no requirement for the new negotiations to produce an outcome.

Annex IV operates as a negative list, so only entities named are excluded from coverage and only to the obligations specified. Most parties have excluded their regional and local government entities from most of the rules. Brunei and Singapore did not list any, presumably because the central government runs their SOEs or DMs.

⁴⁹ http://www.imf.org/external/np/fin/data/rms_five.aspx.

⁵⁰ Annex 17-A.

⁵¹ Above n 35.

⁵² Article 17.9.

⁵³ Article 17.9.1 and Annex IV.

⁵⁴ Article 17.9.2 and Annex 17-D.

⁵⁵ Article 17.14 and Annex 17-C.

- **Independent government pension funds**⁵⁶ are excluded if they are owned or controlled by government, but only if they administer or provide plans for pension, retirement, social security, disability, death and/ or employee benefits, or invest funds for that purpose; they must conduct these activities only for the benefit of the contributors and have a fiduciary duty to those contributors; and must be free from investment direction from the government of the party.⁵⁷ **The exemption extends to an enterprise the fund owns or controls**,⁵⁸ except where the government gives that enterprise non-commercial assistance (financial or goods and services) that causes adverse effects to the interests of another Party.

Comment: The closed list of funds' activities could raise problems of interpretation. For example, would those activities extend to a no-fault accident or sickness compensation scheme where the government funds coverage for some beneficiaries who are not contributors, where benefits of those funds also accrue to others (e.g. those who cause accidents are relieved of legal liability), and/or where there is no direct fiduciary duty to those who are insured.

Significantly, the exclusion does not apply if the government gives directions on their investment (aside from general risk management type laws). A pension fund would therefore lose its protection if the government issued instructions on ethical investment or the proportion of local investment for other than risk management purposes, or on the application of sanctions against certain countries or companies.

- **A sovereign wealth fund (SWF)** owned or controlled by government is excluded,⁵⁹ except where it directly provides non-commercial assistance that causes adverse effects or acts as a conduit for such government assistance.⁶⁰ The fund must operate only as a special purpose mechanism for managing and investing state financial assets and it must belong to the club of sovereign wealth funds or endorse the club's Santiago principles, or similar principles with the consent of the other parties.⁶¹

Comment: This provision was very sensitive for countries with large SWFs. Singapore and Malaysia have special annexes.

Singapore's annex says the government will only exercise influence over a SOE owned or controlled by a Sovereignty Wealth Fund in ways that are consistent with the chapter.⁶² It recognises the government has the right to use its voting rights in ways that are not covered by the rules in the chapter, including the various exclusions and exceptions.

⁵⁶ Article 17.2.6.

⁵⁷ Article 17.1.

⁵⁸ Article 17.2.6(b).

⁵⁹ Article 17.2.5.

⁶⁰ Article 17.6.1, 17.6.2 and 17.6.3.

⁶¹ If this is done at some stage after the TPPA comes into force the Party gains the benefit from that date.

⁶² Annex 17-E.

Neither of these sentences adds anything new; nor do they protect Singapore from challenges that its actions do breach the rules.

The annex explicitly protects state-owned subsidiaries of Singapore's sovereign wealth funds Temasek and GIC Private Ltd from the rule on non-discrimination and applying commercial considerations. The protection from the rule on receiving non-commercial assistance is more limited; it does not apply if the government or its SWF has appointed the CEO or a majority of senior management or directors, or taken other action that would breach the SOE chapter, within the preceding 5 years. Likewise, it won't apply if the government has required the SOE controlled by the SWF to provide non-commercial assistance to another SOE or has directed its commercial decisions. This will have been a precondition for Singapore supporting the chapter, but is limited in scope.

Malaysia's annex⁶³ exempts Permodalan Nasional Berhad⁶⁴ and Lembaga Tabung Haji,⁶⁵ and any SOEs they own or control, from the chapter, except where the government provides non-commercial assistance directly or indirectly to enterprises owned or controlled by the funds. The exemption only applies to specific investment operations for the benefit of beneficiaries to which a fiduciary duty is owed, and where investment is independent of government direction. Malaysia's other major SWF Khazanah Nasional Berhad is only exempt from enforcement through the dispute settlement mechanism for 2 years after the agreement comes into force while Malaysia undertakes reforms.⁶⁶

13. What government activities are excluded?

➤ Government procurement⁶⁷

Comment: Government procurement serves important roles in supporting local employment and businesses and ensuring security of supply. For the purposes of the entire TPPA it is defined very narrowly in Chapter 1 to mean purchase of goods or services by government for its own purposes and not intended for sale or resale or use in producing goods or services that it will sell. That description rules out the exclusion applying to most procurement-related activities of SOEs. Indeed, those activities are principal targets of this chapter.

- **Measures a government adopts as a temporary response to a national or global economic emergency, and a SOE that is the recipient of such measures for the duration of the emergency.**⁶⁸

⁶³ Annex 17-F.

⁶⁴ Malaysia's largest sovereign wealth fund.

⁶⁵ Malaysia's pilgrims fund board.

⁶⁶ Above n 10.

⁶⁷ Article 17.2.7.

⁶⁸ Article 17.13.1.

Comment: This exclusion only applies to the rules on non-discrimination, applying commercial considerations and providing non-commercial assistance,⁶⁹ not to those requiring compliance with the rest of the TPPA when performing delegated responsibilities, or transparency. It does not allow ongoing support for a SOE that was damaged during a crisis. The parties can be expected to disagree about the duration of an economic emergency.

- Government mandated supply by a SOE of financial services to support exports and imports and private investment overseas, or through an Officially Supported Export Credit Scheme; this support must not be intended to displace commercial financing and not provide terms more favourable than could be obtained in the commercial market.⁷⁰

Comment: This exception applies to the rules on non-discrimination, applying commercial considerations, and parts of the rule on providing non-commercial assistance. The proviso means it will have limited application and it seems specially tailored to protect the US Export-Import Bank.

- Financial assistance provided during temporary ownership of an offshore enterprise by a SOE as a consequence of foreclosure or debt default.⁷¹

Comment: The exclusion only applies to financial assistance given to an offshore enterprise in order to recoup the SOE's investment through a restructuring or liquidation plan that is undertaken with a view to ultimately divesting ownership of that enterprise.

- Resolution of failing financial institutions or financial service suppliers.⁷²

Comment: The wording is ambiguous. It does not say 'this chapter shall not apply to' (as it does for government procurement), but that nothing in the chapter shall prevent a government from undertaking activities for that purpose (similar to 'nothing affects the right to regulate'). There is no express right for a government to choose what measures to adopt, including discriminatory measures, and its actions are still open to challenge where they allegedly breach the rules of the chapter.

- Regulatory and supervisory authority over financial services suppliers, and a central bank's exercise of monetary and exchange rate policy.⁷³

⁶⁹ Article 17.13.1(a) and (b).

⁷⁰ Article 17.13.2.

⁷¹ Article 17.13.4.

⁷² Article 17.2.4.

⁷³ Article 17.2.2 and 3.

Comment: It is not clear why the provision says the chapter ‘shall not prevent’ those entities conducting those activities, rather than simply excluding them from the chapter. Their legal structure means many would not be defined as SOEs, and hence would fall outside most of the rules anyway, but they are likely to be considered state enterprises. A challenge is likely only to question whether measures are an exercise of those particular functions (for example, derivatives trading by the central bank).

➤ **Services supplied in the exercise of government authority.**⁷⁴

Comment: This is standard wording drawn from the General Agreement on Trade in Services (GATS). It only applies where the service is not commercial and there is no public or private competitor.

‘Commercial’ has never been defined in the GATS. ‘Commercial activities’ are defined in Article 17.1 of the SOE chapter as activities an enterprise undertakes with an ‘orientation to profit making’. A footnote excludes activities of an enterprise that operates as on not-for-profit or cost-recovery basis. This is said to be ‘for greater certainty’, which means it is an interpretation of the wording. However, there is no equivalent clarification for this provision and the different wording - a ‘commercial service’ rather than ‘commercial activities’ - makes it hard to draw analogies.

Even if a similar meaning was applied, the service not being commercial is only one of the criteria for the exclusion. There must also be no competitor. In other words, the service must be provided as part of a public monopoly.

The exception only covers the rules on non-discrimination, applying commercial considerations, receiving non-commercial assistance, and transparency. It does not apply to the exercise of delegated authority.

➤ **Non-conforming activities of SOEs or designated monopolies listed in the Schedule to Annex IV.**⁷⁵

Comment: Each party could list activities its own annex,⁷⁶ in the form of a negative list that specifies which activities – not which SOEs – are excluded from which rules. As noted above, some TPPA governments have sought to exclude future, as well as existing, entities that undertake those activities. Annex IV only applies to non-discriminatory treatment, applying commercial considerations and receiving non-commercial assistance causing adverse effects. It does not exclude activities of SOEs when they exercise delegated authority, or the transparency obligations.

⁷⁴ Article 17.2.10.

⁷⁵ Article 17.9.

⁷⁶ Singapore and Japan opted not to have an annex.

- Sales and purchases by a SOE or DM are protected to the extent they are listed in country-specific annexes of non-conforming measures in the investment, cross-border services and financial services chapters.⁷⁷

Comment: The annexes in those chapters are negative lists of activities that governments have shielded from specified rules in those other chapters.⁷⁸ Annex I preserves and freezes the status quo (a standstill at current levels of liberalisation). Annex II provides long term exclusions. They are meant to complement Annex IV on SOEs. These other annexes only apply to the rules in the SOE chapter on non-discrimination and applying commercial considerations to purchase or sale of goods and services.⁷⁹ Their content was not designed for the SOE chapter and they are especially ill-suited to the requirement that SOEs apply commercial considerations. Working out whether, and the extent to which, they apply to these rules will be difficult.

14. Barriers to creating new SOEs

The chapter doesn't prevent a government setting up or maintaining a state enterprise or SOE or designating a monopoly.⁸⁰ But they still have to comply with the rules.

Comment: Initial capitalisation of a SOE or acquisition of a controlling interest in an enterprise by a state is protected from the rule on non-commercial assistance causing adverse effects, but only if the enterprise is principally engaged in supplying services within the country.⁸¹

Otherwise, when new SOEs are created or new monopolies are designated the rules in the chapter will apply to them unless the government has reserved a yet-to-be established entity through its schedule, or it falls within an exclusion or exception.

A number of governments have sought to 'future proof' their policy space through country-specific entries in Annex IV.⁸² The Annex protects the non-conforming activities of SOEs and DMs that are listed from obligations under the rules on non-discrimination, applying commercial considerations and receiving non-commercial assistance. A Party can list a specific non-conforming activity for 'all existing and future state-owned enterprises' in relation to one or more of those rules.⁸³ Some parties, especially those like

⁷⁷ Article 17.2.11.

⁷⁸ In practice, a number of countries imported their 'positive list' annexes, which list subsectors they are committing to the market access rule on services, from the General Agreement on Trade in Services (GATS) at the WTO, and supplemented this with a number of negative list entries.

⁷⁹ Article 17.4.1(b)-(c); art 17.4.2(b)-(c).

⁸⁰ Article 17.2.9.

⁸¹ Article 17.7.6.

⁸² Annex IV to chapter 17.

⁸³ Article 17.9, pertaining to Annex IV.

Vietnam that have many SOEs, have done so extensively. Others, such as New Zealand, have limited this reservation to certain of the available rules and a small number of sectors.⁸⁴

15. Intrusive and onerous disclosure obligations

- There are several onerous transparency provisions.⁸⁵ The annexes on non-conforming measures do not apply to this provision and only some of the exceptions do.

Comment: The transparency provisions are additional to the Transparency chapter. These provisions provide numerous opportunities for one TPPA party to pressure another and to seek commercially sensitive information about its SOEs and public monopolies that private firms do not have to provide. The Party providing the information can ask for sensitive information not to be shared without prior consent, but the other government will still have it.

Compliance costs to respond to repeated requests could be very burdensome and there are no restrictions on how often requests can be made or on how many SOEs.

- All parties must provide a list of their SOEs within 6 months of entry into force and update it annually.⁸⁶

Comment: This obligation is not subject to the threshold, so all of a country's SOEs must be listed. Implementation is delayed and/or phased-in for Brunei, Vietnam and Malaysia, but the latter two must list publicly their larger SOEs within 6 months from the date of entry into force;⁸⁷ Brunei has 3 years to do so.⁸⁸

- Any newly designated or extended monopoly must be promptly notified.⁸⁹

Comment: Vietnam has been allowed to list some exclusions.⁹⁰

- A Party can ask another Party in writing for two kinds of detailed information, which must be provided promptly.

The first is information about a SOE or government monopoly.⁹¹ This relates to:

⁸⁴ Infrastructure supporting cross-border communications and cross-border air transport and maritime services.

⁸⁵ Article 17.10.

⁸⁶ Article 17.10.1.

⁸⁷ Above n 29.

⁸⁸ Above 28.

⁸⁹ Article 17.10.2.

⁹⁰ Annex IV, Vietnam, entry 9.

⁹¹ Article 17.10.3.

- the % of state-held shares or voting power;
 - any golden share or special voting rights (even though this is not mentioned as a defining criteria for a ‘SOE’);
 - the entity’s annual revenue and total assets over the most recent 3-year period;
 - titles of government officials who are officers of the company or on the board;
 - any exemptions or immunities the SOE benefits from under law; and
 - any additional information sought that is publicly available.
- A Party can also require provision of information on a policy or programme that provides non-commercial assistance, which it says has already or could affect trade or investment between those parties.⁹²

The information provided must be specific enough for the requesting Party to understand how the policy or programme works and its potential effects on their trade or investment relationship. The information provided must include:

- the form of assistance (e.g. grant, loan);
- where it is a loan or guarantee, details of how much, at what interest and what fees were charged;
- where it is equity capital, how much was invested, how many shares of what type were received, and any assessments that underpinned the investment decision;
- which entities provide the assistance and which are eligible to receive it;
- the legal basis and policy objective;
- the budget per unit where goods are involved or the total amount budgeted in relation to a service;
- the price charged for any goods or services provided on a non-commercial basis;
- the duration of the policy or programme;
- and statistical data that would help assess its effects on trade or investment between the parties.

Comment: There is no barrier to repeated intrusive and costly requests. All the requesting Party must do is include an explanation of how the activities of that SOE or government monopoly ‘may be affecting trade or investment’ between the parties.⁹³ There is no mechanism for the recipient Party to challenge the validity of the explanation. Disclosure cannot be refused on the grounds of confidentiality, but it cannot be passed on to others without consent of the provider. This gives that state better information than other states and the private sector.

⁹² Article 17.10.4.

⁹³ Article 17.10.3 and Article 17.10.4.

- A further special annex⁹⁴ sets out processes for securing information when a dispute is initiated under the chapter, alleging a breach of non-discrimination, applying commercial considerations or receiving commercial assistance.⁹⁵

The Annex allows one party to submit written questions to the other party within 15 days after a tribunal has been established under the TPPA's dispute settlement provisions; the recipient has 30 days to respond. There is a similar timeline for follow up questions and answers.

If the questioner doesn't think the recipient has been cooperative it can inform the tribunal, giving reasons; the other party has the right to reply. After considering the reasonableness of the questions and efforts made to respond, the tribunal can draw adverse inferences from lack of cooperation. It can also seek additional nonpartisan information that it considers necessary to resolve the dispute. Information provided in response to a request can be designated confidential.

16. Extending the scope of the SOE chapter

There are two inbuilt negotiations:

- (i) Annex 17-C requires negotiations within 5 years of the TPPA coming into force to extend the coverage in relation to **sub-central SOEs and DMs** of countries listed in Annex 17-D; and
- (ii) the extension of the non-commercial assistance and adverse effects test to address effects caused by an SOE's supply of services in the market of **non-TPP countries**.

Comment: There is no requirement that either negotiation results in changes. However, the US will resist the first and promote the second, consistent with its driving concern that SOEs impact on US commerce globally.

17. Committee oversight and leverage

- A special Committee on SOEs and DMs will meet at least annually

Comment: The committee provides a forum for collective or individual country pressure on one or more of the parties.⁹⁶ Its roles include:

⁹⁴ Annex 17-B.

⁹⁵ Article 17.15.

⁹⁶ Article 17.12.

- *to review the operation and implementation of the chapter. One Party can ask the committee to consult on any matter under the chapter, which could be generic or targeting individual countries.*
- *develop cooperative efforts to promote the underlying principles through regional and multilateral fora, such as APEC and WTO.⁹⁷*
- *plan, resources permitting, to undertake agreed technical cooperation activities including information exchanges, workshops, and sharing ‘best practice’ with special reference to ‘competitive neutrality’ (the core concept underpinning Australia’s competition policy and approach to SOEs).⁹⁸*

⁹⁷ Article 17.12.2(c).

⁹⁸ Article 17.11.