

ENCOURAGING INTERNATIONAL INVESTMENT IN THE ASIA PACIFIC REGION

A Draft Asia Pacific Investment Code



PACIFIC ECONOMIC COOPERATION COUNCIL

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THE PECC is an international organisation with a difference. It is tripartite in structure. Government officials, business and academic participants meet to share their perspectives and expertise in the search for the broadly-based answers to the problems of economic cooperation in the Pacific region.

Each of the 20 members of PECC sends a representative delegation to the plenary meetings at approximately 18-month intervals, and to meetings of specialised task forces and fora based on sponsored studies, and designed to achieve a common basis in fact and enhanced prospects for policy consensus.

One of the PECC's principal activities of continuing importance has been its research for the means of preserving and strengthening the multilateral trading system through the PECC Trade Policy Forum. Other task forces deal with the development of a Pacific economic outlook, and with analyses of market conditions and policy issues relating to various sectors of the regional economy (agriculture, fisheries, and minerals and energy) and with cooperation in the improvement of infrastructure and the transfer of technology in the region.

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**A Draft
Asia Pacific Investment Code**

**PREPARED BY
Trade Policy Forum**



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I

INTRODUCTION

ADVANTAGES OF A REGION-WIDE UNDERSTANDING ON INVESTMENT

The volume of direct international investment has increased rapidly globally as well as within the dynamic Asia Pacific region. Most of the economies in PECC and APEC are now sources of investment as well as hosts, or recipients, of direct investment from other Asia Pacific economies. The nature of investment is also evolving -- it now takes many forms, ranging from the purchase of equity to joint ventures and to strategic alliances of firms from different countries, for example for marketing or technological cooperation.

Investment is also recognized to be a very important complement to trade, promoting mutually beneficial market-driven integration in the region. International investment is also helping to improve trading links through the transfer of technology, the development of human resources as well as by the establishment of more effective marketing channels.

The Uruguay Round is still in progress. Accordingly, it is difficult to define useful regional-level initiatives in areas of trade policy which are under direct consideration in the Uruguay Round (i.e. in the areas of trade in goods and services).

However, the GATT and the Uruguay Round are addressing only a few of the trade related aspects of the international investment. Therefore, there is scope for Asia Pacific economies, who are all important sources and recipients of international investment, to think through related policy issues. As outlined below, there is scope to develop some sensible, GATT-consistent principles which can guide policy-making on investment by regional authorities. If such guidelines can be developed, they could not only facilitate international investment in the Asia Pacific, but such guidelines could also serve, in time, as a basis for a possible subsequent set of multilateral guidelines for global investment flows. Guidelines for international investment, based on the fundamental GATT principles of non-discrimination, could also be helpful for all aspects of international economic transactions, including both trade and investment.

All economies in the Asia Pacific region have a strong interest in attracting international investment, not just for financial reasons, but also to enhance their technological and human resource capacity. However, most governments impose some restrictions on inflows or outflows of investment. In some cases, foreign firms are excluded from any (or majority) ownership in certain sectors; firms from different countries may sometimes be accorded different treatment. Many governments also impose "performance requirements" on international investors (such as minimum shares of local equity, minimum proportion of production to be exported, etc.). Since such performance require-

ments can reduce the attractiveness of economies to investors, governments sometimes seek to offset their effects by offering subsidies to international investors (for example, through generally available “tax holidays”, or subsidies targeted at particular sectors or firms). At times, performance requirements and incentive schemes can lead to overlapping and complex distortions which affect efficient resource allocation. Exports by firms receiving subsidies are often challenged as “unfair” competition, provoking anti-dumping or other countervailing action, creating trade frictions.

Accordingly, there is scope for improving the policy environment in order to facilitate international investment in the Asia Pacific and to steer it in more efficient directions. In addition, private sector participants in PECC have drawn attention to the need for better, and more detailed, information about the policies of regional governments which influence investors, including the need for transparency of approval procedures, incentive policies, relevant foreign exchange regulations as well as procedures for the settlement of any commercial disputes.

Partly in order to help attract more investment, governments are continuously revising their policies on international investment, often (though not always) in the direction of simplifying and streamlining, for example towards simpler or less restrictive approval procedures. Since much of new international investment involves joint participation by firms from the host country, there is a general trend towards equal policy treatment of domestic and international investment. There is also increasing recognition of the value of greater consistency and gradual harmonization of the investment policies of regional governments.

It would be helpful if there were some guiding principles, or a frame of reference, which could help steer the independent decisions on investment policies by authorities in member economies in a gradually more consonant and confidence-building direction.

In order to clarify investment policies and to build greater confidence for two-way investment, several pairs of Asia Pacific economies have entered into bilateral investment agreements. These often cover issues such as: the right of establishment of foreign firms; the right to transfer funds across international boundaries with no (or minimum) restriction; and providing assurances that investments will be nationalized only under well defined conditions (e.g. if the site of the investment was needed for infrastructure development) and that owners would be compensated promptly and fairly. However, it would require 105 bilateral understandings or agreements to link the 15 participants of APEC, and over 200 to link all PECC members. It would take over 1000 bilateral agreements to link the Pacific Island nations to others in PECC or APEC.

For all of these reasons, there may be merit in a region-wide understanding on the basic principles of policies to encourage mutually beneficial international investment in the Asia Pacific.

THE NATURE OF AN ASIA PACIFIC INVESTMENT CODE

In a successful and very diverse region, any guidelines, understandings or codes on international investments should be stated in positive terms. In line with the open outward-looking

nature of both PECC and APEC, any Asia Pacific code should encourage a more harmonized approach to investment on a *voluntary basis*, recognizing the equal right of all governments to make decisions about their own economic, trade and investment policies. This would appear to be consistent with the desire to promote regional economic cooperation which seeks to build an *Asia Pacific Economic Community*; an outward-looking, non-discriminatory *open economic association* of Asia Pacific economies.

In this spirit, any proposed regional code on investment should not seek to impose uniformity, but to encourage more consistency. Any new code should avoid creating a new layer of rules; it should encourage the simplification, or reduction, of rules in order to facilitate international investment. An Asia Pacific code on investment should not demand any immediate policy changes or require legal compliance with externally imposed rules; it would be preferable, and more effective, to see any new code as a frame of reference or guiding principles for promoting greater transparency and consistency of regional approaches to investment. Any new code should not require negotiation; it would be more likely to be adopted and adhered to if signing of the code was on a fully voluntary basis by all PECC or APEC governments.

International investment is recognized by all regional economies to be mutually beneficial. Promoting investment based on market-consistent commercial decisions is a positive-sum game. Therefore, if any government chose to sign a voluntary regional investment code in order to promote investment and to increase the confidence of investors about the consistency of its investment policies, it is very likely that they would also endeavor, seriously, to follow its guidelines. For

these reasons, the code outlined below is designed so there should be no incentive to depart from its guidelines. Since progressively closer adherence to such guidelines will yield positive benefits, in terms of promoting two-way investment flows, there is no need to suggest a legally binding code. There is certainly no need for any regional mechanism to “enforce” a voluntary investment code. Any such code is likely to be self-enforcing, in the sense that scarce investment funds are more likely to flow to those who sign and adhere, voluntarily, to its basic guiding principles.

It is also important that policies towards investors from the Asia Pacific region, or anywhere in the world should be as consistent as possible with policies towards domestic investors. They should also be as consistent as possible with attracting investment from anywhere in the world, in order to be consistent with the outward-looking nature of PECC and APEC. Any regional understanding on investment needs to be consistent with the region's overriding interest in a rules-based multilateral system for both trade and investment. Accordingly, any Asia Pacific code should be on an open, most-favored-nation (MFN) basis; a regional code which could be extended (either by voluntary signature by other economies or through global consultations) to become, or be the basis of, a multilateral code. A regional code would also need to be consistent with, and without prejudice to, other international obligations of signatories (e.g. investment-related provisions of the GATT). Accordingly, the three basic principles of the proposed code are:

transparency;
non-discrimination; and
national treatment.

A voluntary code, by definition, does not require any immediate policy amendments as a condition of signature. Rather, signatories are requested, and expected, to make an “in principle”, commitment to liberalize their investment policies over time, bringing them gradually more closely in line with its central guiding principles.

Firstly, signatories would be expected to make their policies which influence international investment as transparent as possible. Then, they would be asked to avoid introducing any new policies which would depart further from the guiding principles of the code. They would also be encouraged to review, regularly, existing policies which remain inconsistent with the guiding principles, with a view to reducing the extent of such exceptions over time. This approach is known in the GATT as a “standstill and rollback” strategy.

The adoption of such a code should help avoid commercial disputes. Inevitably, however, there will be disputes involving domestic and international firms, or international firms and host governments. Any such disputes should be resolved quickly, efficiently and equitably. The proposed code does not suggest setting up any new regional dispute settlement procedure. It encourages signatory governments and firms to make effective use of already existing mechanisms, either under domestic jurisdiction or international conventions or mechanism (such as ICSID, UNCITRAL or the New York Convention on international arbitration).

Finally, the code should be capable of responding to the continuing evolution of the region and of the nature of international investment itself. There should be regular review, for

example by relevant working groups of PECC and APEC, possibly to extend the scope of the code, or possibly, to recommend converting some aspects of the code to a more binding form, but if, and only if, it is considered to be of mutual benefit.

THE DEVELOPMENT OF AN ASIA PACIFIC INVESTMENT CODE

Recognizing the potential value of a region-wide understanding on investment policy, the PECC Trade Policy Forum established, in 1992, an international Investment Study Group. The group draws on representatives from over 10 PECC member committees, from all parts of the Asia Pacific region. The group includes, business and academic representatives as well as some officials participating in a personal capacity.

Following discussions starting at Trade Policy Forum VI in Batam, Indonesia, the Investment Study Group met in Jakarta on April 29-30, 1993 and drew up an initial draft of a proposed Asia Pacific Investment Code, based on the central principles discussed above.

The draft was then circulated to a wider group from the Trade Policy Forum. Their comments have been incorporated in the second draft which was circulated at the TPF VII.

The desirability of a region-wide investment code was discussed in some depth at the recent Global Contribution Seminar hosted by JETRO in Tokyo on June 1-2, 1993. Senior opinion leaders from more than ten economies from the Asia Pacific region welcomed the proposal. Although there was insuf-

ficient time to discuss the draft code in detail, the group reached a clear consensus that such a code was desirable, provided it was recognized to be a voluntary code at the outset, and was consistent with the central principles of the PECC namely:

- openness
- equality, and
- evolution;

as well as with the more specific investment-related principles of transparency, non-discrimination (or most-favored nation treatment) as well as national treatment.

The Investment Study Group then met in Tokyo to draw up a second draft of the code, as well as an introduction to the code.

REVIEW AT TPF VII

The second draft was reviewed extensively at PECC's Trade Policy Forum VI I in Puerto Vallarta, Mexico, held from 23-25 June, 1993. Helpful comments, as well as some constructive criticism, were received at the Investment Workshop on 23 June as well as during Session I of the Trade Policy Forum itself. These have been included in the third draft of 25 June 1993 which is provided in Section 11 of this document, as well as in the formal report of TPF VII.

It is recognized that this draft is still likely to need further revision in the light of comments from the private sector, from

academics, as well as from governments; especially from those authorities who may subsequently consider becoming signatories to any investment code of this nature.

Private sector representatives drew particular attention to the possible need to develop an effective and binding regional dispute settlement mechanism, given the weaknesses of and sometimes excessive delays involved with currently available mechanisms for settling any commercial disputes. The possible nature and feasibility of any regional commercial dispute settlement mechanism will be considered in more detail by the TPF Investment Study Group, then by TPF VIII.

There was a broad consensus at TPF VII that a code on Investment, based on the basic principles outlined above, was worth serious further evaluation, including by governments, while recognizing that further amendments were likely to be found desirable.

It was agreed that this draft of a potential, voluntary, Asia Pacific Investment Code could be circulated widely for feedback, including from member PECC Committees, the PECC International Standing Committee, PBEC, as well as from APEC.

II

DRAFT

ASIA PACIFIC INVESTMENT CODE

A. GUIDING PRINCIPLES

- Signatories acknowledge the mutual benefits derived from the rapid growth of international investment in the Asia Pacific region and the potential benefits of future investment flows in terms of:
 - accelerated economic development;
 - transfer of technology;
 - capital formation; and
 - human resource development.
- Signatories intend to promote international investment in the region by creating a policy environment characterized by increased confidence, reduced uncertainty and by the liberalization and simplification of policies and rules relating to investment where appropriate.

- Consistent with the overriding commitment of all signatories to an open, multilateral system of rules for international economic transactions and with the basic principles and objectives of the GATT, this code emphasizes the central principles of:
 - transparency;
 - non-discrimination; and
 - national treatment.

- This voluntary code:
 - demonstrates the commitment of signatories to the principles and objectives of open regionalism as stated in the San Francisco PECC IX Declaration and the Seoul APEC Declaration;
 - recognizes that signatories are likely to be capital-exporting as well as capital-importing economies and the guiding principles of this code apply to signatories in their capacities as both home and host to investment;
 - acknowledges the role of international institutions, such as the International Bank for Reconstruction and Development, the International Monetary Fund and the Asian Development Bank, in influencing investment rules in both home and host countries and solicits their support through consistency of their policy recommendations and loan conditions with the provisions of this code.

- In return for undertakings by signatories given in this code work towards an increasingly open and certain environ

-ment, investors are expected, as good corporate citizens, to recognize and respect the diversity of the region, the rights of host governments and to contribute to the well-being and development of host economies.

- It is recognized that the nature of international investment is evolving over time. In addition to the purchase of equity, international investment can take forms such as joint ventures or other forms of inter-firm partnership, including for the development and sharing of technology. The guiding principles of this code should, wherever relevant, apply to all forms of international investment.

B. RESPONSIBILITIES OF SIGNATORIES

1. Transparency

- Signatories undertake to make explicit and transparent all laws and regulations (including administrative guidelines and procedural directions) with respect to foreign investment and the means by which they are implemented.

2. Most-Favored-Nation Treatment

- Signatories will provide to foreign investors and potential investors no less favorable treatment than they provide in like circumstances to investors of any other economy.

3. Establishment of Investments

- Signatories will facilitate foreign investment in all commercial fields and activities other than those explicitly specified:

- activities where foreign investment is restricted or excluded will be explicitly specified by each signatory and the list of such restrictions will be made available to all interested parties.
- Signatories undertake to:
 - make no additions to the list of activities where foreign investment is restricted or excluded; and
 - agree to review regularly this list with a view to reducing the number of activities where foreign investment is restricted or excluded.

4. National Treatment

- After establishment in a signatory economy foreign investors will receive treatment for that investment no less favorable than accorded by the host government to its own investors.
 - exceptions to national treatment will be explicitly specified by each signatory and information on such exceptions will be made available to all interested parties.
- Signatories undertake to:
 - introduce no new legislation or regulation which extends the list of exceptions to national treatment; and
 - agree to review regularly this list with a view to the reduction of the exceptions.

5. Transfers

- Signatories will permit all transfers by a foreign investor in a convertible currency, at the market rate of exchange prevailing on the date of transfer, freely and without undue delay.

6. Nationalization and Compensation

- Signatories will not, directly or indirectly, nationalize or expropriate an asset of a foreign investor, except:
 - for a public purpose;
 - on a non-discriminatory basis;
 - in accordance with due process of law; and
 - on payment of compensation.
- Signatories agree that no nationalization or expropriation will proceed, unless the relevant signatory and the foreign investor otherwise agree, until the due process of law has been completed in the court of final judgment whose decision both parties should accept.
- Compensation will be equivalent to the fair market value of the asset before the intention to nationalize or expropriate became known.
- Compensation will be paid without delay and be transferable in a convertible currency;
 - a commercially reasonable rate of interest will be paid from the date of nationalization or expropriation until the date of actual payment.

7. Performance Requirements

- Consistent with the principle of transparency, signatories undertake to list explicitly any requirements in relation to foreign investment in that economy, including requirements on exports, imports, procurement, sales and distribution, equity and technology transfer.
- Information regarding such performance criteria will be made available to all interested parties.
- Signatories undertake to introduce no new performance requirements and agree to review regularly the list of performance requirements, with a view to their reduction.

8. Taxation and Investment Incentives

- Consistent with the principle of transparency, signatories undertake to make available to all interested parties all information regarding:
 - tax legislation and regulations with respect to foreign investment in that economy,
 - incentives or subsidies available to foreign investment in that economy.
- Signatories endorse increased harmonization of policies on foreign investment in order to:
 - decrease the motive and opportunity for tax avoidance;

- encourage the efficient location of investment.
- Signatories agree, in principle, to negotiate or extend double taxation agreements or arrangements to help achieve these objectives.
- Signatories recognize that it is not appropriate to relax domestic health, safety and environmental measures for the sole purpose of encouraging investment.

C. RESPONSIBILITIES OF INVESTORS

- Signatories will undertake to encourage foreign investors to accept a range of responsibilities and standards of corporate behavior, including the following:
 - contribution to the development of science, technology and human resources of host economies;
 - sensitivity to local community values and customs; compliance with host government legislation and policies, including those relating to the health, safety and environmental standards of host economies; taxation policies, including policies designed to avoid any unfair transfer pricing practices; policies to promote fair competition (e.g. anti-trust) policies as well as reasonable requirements to provide statistical information on their operations; and securities laws and general corporate legislation.

D. DISPUTE RESOLUTION

- Signatories undertake to reduce the likelihood of disputes involving foreign investors in their economies by simplifying, where appropriate, legislation and regulations (including administrative guidelines and procedural directions) affecting their operations.
 - where appropriate, signatories will consider becoming parties to international legal conventions, including conventions relating to procedures for commercial arbitration, which are designed to reduce uncertainty or costs involved in international commercial transactions and to facilitate the settlement of investment disputes.
- Where disputes arise:
 - signatories will encourage parties, including relevant public agencies or authorities, to consult in good faith ; and
 - signatories undertake to facilitate access to domestic courts as well as to internationally recognized processes of conciliation and arbitration.

• E. EXTENSIONS

- Recognizing the dynamic and expanding range of international commercial transactions, including foreign investment signatories agree to consult regularly to evaluate the scope and effectiveness of this code.
- Signatories agree to reconvene within no later than five years for a full review of this code.

F. RELATION TO OTHER AGREEMENTS AND INSTITUTIONS

- Undertakings under this code, or future extension of this code are without prejudice to rights or obligations included under GATT, or other international codes or treaties which signatories had entered prior to signing this code.
- Signatories accept the importance of not entering into subsequent obligations whose provisions are not consistent with this code.
- Signatories undertake to bring this code to the attention of relevant sub-national and international bodies, and to encourage such bodies within their areas of competence to work cooperatively with foreign investors in accordance with the principles and responsibilities set out in this code.

• G. PARTICIPATION

- All signatories undertake to respect the guiding principles of this code and to follow its provisions, except where otherwise specified:
 - signatories agree to review exceptions with a view to their elimination.
- All economies, especially those in the Asia Pacific region, are invited and encouraged to sign this code.