SAFTA – Response to Query from the Joint Standing Committee on Treaties, 19 June 2003

Can you comment on the differences between the investor-state dispute settlement measures in SAFTA compared with those in NAFTA, and how a state might be vulnerable to complaints by investors in the other state?

The Department is aware of the existence of an active public debate about the use of the investor-state dispute settlement provisions in NAFTA. However, it is important to emphasise that while there are some commonalities between NAFTA and SAFTA, in that both provide mechanisms allowing investor-state settlement of disputes, there are also significant differences. Furthermore, the focus of the public debate about NAFTA has generally been on the substantive provisions that can be invoked in investor-state dispute settlement, rather on the actual investor-state dispute settlement mechanism. It is these substantive provisions that determine the extent to which a state might be subject to challenge by investors through the investor-state dispute settlement mechanism.

One way in which the investor-state dispute settlement mechanism in SAFTA differs from that in NAFTA is the fact that the latter contains detailed, agreement-specific, provisions on the procedural aspects of the dispute settlement mechanism. SAFTA relies on the multilaterally-agreed procedures followed by the International Centre for Settlement of Investment Disputes (ICSID) and the arbitration rules of the United Nations Commission on International Trade Law (UNICTRAL) rather than prescribing detailed procedures specific to the Agreement.

There are general similarities between the investor-state dispute settlement mechanisms in SAFTA and NAFTA in relation to:

a) the fact that they can only be invoked in cases where an investor alleges that a Party has breached an obligation under the investment chapter which causes loss or damage to the investor or its investment;

b) the requirement that the dispute must be submitted to conciliation or arbitration within three years of the time at which the disputing investor became aware, or should reasonably have become aware, of a breach of an obligation causing loss or damage to the investor or its investment; and

c) the requirement that the investor resorting to international arbitration must waive its right to initiate or continue any proceedings before domestic courts or administrative tribunals in relation to the matter under dispute.

These points of similarities are ones which place careful limits on the scope of the investor-state dispute settlement mechanisms and provide protection against their abuse.

A Party to SAFTA would only be vulnerable to a successful challenge under the investor-state dispute settlement provisions if it had breached its treaty obligations under the investment chapter of the Agreement. In such a situation the other Party

would also be successful in a challenge using the state-to-state dispute settlement provisions. The investor-state dispute settlement provisions create the possibility for an investor of either Party to directly resort to international arbitration rather than relying on its Government to pursue the issue. However, Government measures are not vulnerable to challenge under the investor-state dispute provisions if they are not also vulnerable to challenge under the state-to-state dispute settlement provisions.

The value of treaty obligations depends on the extent to which the Parties to the treaty ensure their compliance with those obligations. The dispute settlement provisions of SAFTA – whether state-to-state or investor-state – are a means for resolving disputes about whether a Party is complying with its obligations. They serve the important function of providing greater confidence that treaty obligations can be relied on in making investment and other decisions affected by the treaty. But the dispute settlement provisions in SAFTA provide no basis for concluding that a government measure in compliance with Australia's treaty obligations could be subject to a successful challenge.

In relation to the substantive provisions of SAFTA and NAFTA, there are both similarities and differences. One difference is in the treatment of expropriation in both SAFTA and NAFTA. In NAFTA the expropriation article (Article 1110, para 1) begins:

"No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ('expropriation')..."

There has been concern expressed that this wording has led to some confusion as it seems to suggest that there are three types of expropriation, i.e. direct, indirect, and measures tantamount to nationalization or expropriation of such an investment. This confusion has led to some uncertainty as to the types of measures that could be subject to the expropriation article in NAFTA. By contrast, the expropriation article in the investment chapter of SAFTA (Article 9, para 1, of Chapter 8) begins:

"Neither Party shall nationalise, expropriate or subject to measures having effect equivalent to nationalisation or expropriation (hereinafter referred to as 'expropriation')..."

This formulation makes clear that the distinction being drawn is between direct expropriation and measures having effect equivalent to expropriation (i.e. indirect expropriation). This distinction is common in bilateral investment treaties, including Australia's, and it appears that the NAFTA Parties were intending to make the same distinction in their Article 1110 but the wording they adopted does not convey this unambiguously. It is notable that in its recent treaty practice the United States has moved to a formulation similar to that used by Australia in its treaties rather than to that used in NAFTA. For example, the recently concluded United States-Singapore Free Trade Agreement uses the following wording in its expropriation article (Article 15.6):

"Neither Party may expropriate or nationalize a covered investment either directly or indirectly through measures equivalent to expropriation or nationalization ('expropriation')..."

Given that there are a range of differences as well as similarities between SAFTA and NAFTA in relation to both the investor-state dispute settlement mechanisms and the substantive provisions of the two agreements, it would be misleading to assume that concerns that have been raised about NAFTA would necessarily have direct relevance to SAFTA.