

## E-ALERT | International Trade and Investment Policy

April 20, 2012

### UNITED STATES RELEASES NEW MODEL BILATERAL INVESTMENT TREATY

On April 20, 2012, the U.S. Department of State and the Office of the U.S. Trade Representative released the 2012 U.S. Model Bilateral Investment Treaty (“BIT”), the template document that likely will serve as the starting point for negotiating new BITs with countries such as China, India, and Russia. The new Model BIT replaces the version released in 2004.

In addition to being closely involved in the stakeholder input process which led to the new BIT, Covington & Burling LLP’s attorneys and non-attorney policy advisors include former senior officials from both the State Department and the U.S. Trade Representative’s Office. With first-hand knowledge and experience in BIT negotiation and implementation, Covington is uniquely positioned to advise clients on the legal and policy implications of current and future BIT negotiations and to represent clients in disputes arising under BITs.

#### INTRODUCTION

The new U.S. Model BIT has been eagerly anticipated, since at least 2009, when the Obama Administration initiated a review of the Model BIT and solicited input from stakeholders and the public. A significant source of stakeholder input was the report by the Subcommittee on Investment of the Advisory Committee on International Economic Policy (“ACIEP”). Formed at the behest of the State Department and co-chaired by Covington Senior International Policy Advisor Alan Larson, the ACIEP Subcommittee on Investment reviewed the 2004 Model BIT and submitted a report on October 1, 2009 that made a number of recommendations for changes. As explained further below, the 2012 U.S. Model BIT incorporates a number of these recommendations as well as makes significant changes to other key areas of interest to our clients.

The State Department and the U.S. Trade Representative’s Office are jointly responsible for negotiating new BITs, and they are expected to use the release of the 2012 Model BIT as a starting point for a renewed push to conclude BITs with other countries. This is a welcome step forward as the United States has far fewer BITs in force than many comparable nations, and lacks BITs with a number of major trade partners, including China, India, and Russia. As American diplomats and trade negotiators begin or renew attempts to negotiate BITs with their counterparts in other countries, they will attempt to use the new Model BIT as a guide, though the other countries’ negotiators will approach the negotiation with their own preferences.

#### NOTABLE PROVISIONS IN THE 2012 U.S. MODEL BIT

Discussed below, the most notable provisions in the 2012 U.S. Model BIT are in the areas of transparency, standards-setting, and performance requirements. These rather far-reaching changes should be beneficial for business, labor and environmental groups. In addition, the 2012 U.S. Model BIT contains new language addressing several other important issues:

- **State-Owned Enterprises.** The 2012 U.S. Model BIT has language that both directly and indirectly addresses the increasingly relevant issue of the duties and responsibilities of state-owned enterprises. The new Model BIT clarifies when a Party’s obligations under the BIT apply to a state-owned enterprise

which exercises delegated authority. Revisions to the articles on Performance Requirements (Art. 8) and Transparency (Art. 11), including addition of a new provision on Standards-Setting (Art. 11 (8)), also lower some of the barriers often erected to protect state-owned enterprises. Although the 2012 U.S. Model BIT creates no new review process for inward investments by state-owned enterprises, the Foreign Investment and National Security Act of 2007 (FISIA) already requires that the Committee on Foreign Investment in the United States (CFIUS) give closer scrutiny when a foreign state-owned enterprise acquires and gains control of a U.S. business where national security may be affected.

- **Performance Requirements (Art. 8).** The 2012 U.S. Model BIT broadens the prohibition against performance requirements to encompass requirements either that an investor “purchase, use, or accord a preference to” indigenous technology of the host country or that preclude an investor from purchasing, using, or according preference to “particular technology.” This prohibition prevents a Party from enacting protectionist measures to benefit its own investors, investments, or technology. However, there are possible exceptions in the context of the TRIPS Agreement, government procurement, or enforcement of a Party’s competition or certain environmental laws.
- **Standards Setting (Art. 11(8)).** The new U.S. Model BIT now expands the opportunities for U.S. companies to participate in the setting of standards in host countries. The new text requires Parties to “allow persons of the other Party to participate in the development of” standards, technical regulations, and conformity assessment procedures by its central government bodies. It also instructs Parties to recommend that “non-governmental standardizing bodies in its territory” similarly open participation to foreign persons. One of the exceptions to the applicability of the new standard-setting provisions is in the area of sanitary and phytosanitary measures.
- **Transparency (Art. 11).** The 2012 U.S. Model BIT incorporates language establishing requirements similar to domestic rulemaking practices. As a general matter, a Party now is obligated to publish (with an explanation of its purpose and rationale) any “regulations of general application that are adopted by its central level of government.” Where the Party is publishing in advance a proposed regulation of general application, the Party is obligated to publish (with an explanation of its purpose and rationale) and receive public comment on the proposed regulations. At the time of adopting regulations published in this manner, a Party must both address “significant, substantive comments” and explain any “substantive revisions” which were made to the regulations. This new text is a clear recognition that transparency with respect to the laws and regulations regarding investors and investments is an important aspect of securing the rights of investors in a foreign country.
- **Financial Services (Art. 20).** The new U.S. Model BIT includes several changes to the provisions on Financial Services. The understanding of prudential reasons for a Party to adopt or maintain measures relating to financial services now includes “the maintenance of the safety and financial and operational integrity of payment and clearing systems.” The 2012 U.S. Model BIT also introduces clarifying language that, as a general matter, a Party is permitted to adopt or enforce measures “related to the prevention of deceptive and fraudulent practices or that deal with the effects of a default on financial services contracts.” In the context of investor-State dispute settlement, both Parties’ “competent financial authorities” still retain special responsibilities in the arbitration process thereby ensuring that the Parties remain involved in determining whether a measure has been invoked for a prudential reason. Although an investor still must request that the State Parties make a joint determination as to the validity of a Party’s “prudential reason” defense, an arbitration tribunal now cannot draw an inference where the State Parties fail to make any such determination. However, the tribunal does now have the authority to make its own determination on issue(s) left unresolved by the competent authorities.
- **Environment (Art. 12) / Labor (Art. 13).** In contrast to the aspirational language of the previous Model BIT, the 2012 U.S. Model BIT mandates Parties to neither waive nor derogate (nor offer to do so) from their domestic environmental and labor laws and helpfully clarifies the definition of what is meant by those terms. For “any matter arising under” either the environment or labor articles, the 2012 U.S. Model BIT allows States Parties to request a consultation with its co-Party as well as, where appropriate,

“provide opportunities for public participation.” However, both State-State and investor-State dispute settlement remains unavailable for alleged breaches of either the environment or labor provisions of the BIT.

- **Territory.** The 2012 U.S. Model BIT expands the definition of a Party’s “territory” to include its territorial sea and any area beyond over which the Party exercises sovereign rights “in accordance with customary international law as reflected in the United Nations Convention on the Law of the Sea.”

It should be noted that the Administration has declined to make any changes to certain provisions which were the subject of considerable debate within the ACIEP Subcommittee. These provisions include Investor-State dispute settlement; Essential Security; Expropriation; and the Minimum Standard of Treatment.

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Covington is deeply familiar with the BIT negotiation and implementation process as a result of our attorneys and non-attorney policy advisors such as Alan Larson (Career Ambassador and former Under Secretary of State for Economic, Business, and Agricultural Affairs); John Veroneau (former Deputy United States Trade Representative; former General Counsel to the U.S. Trade Representative Office); and Marney Cheek (former Associate General Counsel at the Office of the U.S. Trade Representative).

They and others are closely monitoring developments in the Administration’s approach to BIT negotiation, and are well-placed to advise clients on current and future treaty negotiations. In addition, our robust international arbitration practice has extensive experience in representing clients seeking to resolve disputes which arise under BITs. We would be pleased to discuss these matters further as they may relate to your business.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our international trade practice group:

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If you have any questions concerning the material discussed in this client alert, please contact the following members of our international public policy practice group:

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