

High-Level IIA Conference 2017: Moving to the next Phase of IIA Reform organized by UNCTAD, 9-11 October 2017, Geneva

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Kick-starting the next phase of IIA reform – identifying and addressing challenges – Montenegrin experiences

Existing BIT model

One of the important tasks Montenegro has decided to undertake is the review of the existing BIT model. We are at the beginning of the model BIT review process – it can perhaps be described as a “phase 1” IIA reform action.

The BIT model which Montenegro is currently using is rather outdated.

On 14 April 2016, Montenegro reached the **Decision to stop signing new bilateral investment treaties** until it defines a new BIT model.

For the preparation of the BIT model, it is necessary to:

- Change the spirit of the existing BIT model and harmonise it with the current investment trends,
- Follow recommendations and international legal standards reached by international institutions dealing with investment and investment-related policies such as UNCTAD, OECD, and others.
- Found a cross-sectorial Working Team which will be composed of representatives of relevant ministries and agencies.

The objective of the review

The objective of the review is to provide a detailed analysis of the existing BIT model and key shortcomings that need to be resolved. It shall also focus on:

- Defining the strategic approach to signing new bilateral investment treaties
- Establishing coordinated activities on all levels (national, regional and multilateral),
- Undertaking comprehensive activities, in order to encompass the reform of the entire investment regime of the country.

In this sense, the model BIT review is part of a broader review of our BIT policy approach.

Activities undertaken

Montenegro has already undertaken several activities to advance this process. **These activities will also help us to move to the next phase of IIA reform and evaluate the options we have for our existing and future BITs:**

- ✓ **We participate in the development of the Investment Policy Review** (undertaken, with the help of, among others, UNCTAD (while working in the CEFTA – RCC – EC Joint Working Group)).
- ✓ **We are strengthening administrative capacities (capacity building)** – attending different types of professional training (conferences, seminars, workshops...).
- ✓ **We receive expert assistance.**
- ✓ **We are analyzing key provisions of the existing BIT model** (legal consultations, expert assistance).

Analysis of key provisions of the existing BIT model

- ✓ **Narrow the definition of the notion of “investor”**

International practice has shown that individuals often know how to use definitions of “investors” which are broad enough, to only formally acquire citizenship of a country in order to gain access to arbitration, based on its BITs. Bearing this in mind, a change in formulation was proposed, in order to prevent the so-called “treaty shopping”, i.e. the abuse of international treaties by formally acquiring citizenship.

- ✓ **Define the notion of “seat”**

The meaning of this term is not the same in all legal frameworks. The adequate definition of a seat would additionally limit the implementation of a Treaty to real investors from other member countries. It was also proposed to introduce additional changes in order to incite only real investors, prevent potential abuse, and exclude fake companies (“shell companies”) from the field to which the Treaty is applied.

- ✓ **Narrow the definition of “investment”**

It is recommended to consider to further narrow, or define more precisely, the notion of investment, since the proposed definition is quite broad. Certain BITs, for example, exclude portfolio investments, i.e. ownership of 10% or less shares in a company, which does not give the right to effective management, state loans, debt securities issued by the state, letters of credit, etc.

We are proposing to limit the application of Treaties only to foreign direct investment, and to exclude indirect investment. Namely, indirect investment does not contribute essentially to economic development and cooperation between Contracting Parties. Therefore, such changes would be in accordance with the general aim of the Treaty.

It was proposed to narrow the implementation of the Treaty to investments with significant value, which last for a defined period of time, which imply taking certain risks by the investors, which are important for the host country's economy, etc.

✓ **Define more precisely the content of FET**

FET is by nature imprecise and unpredictable, and is made concrete by a court or an arbitration tribunal. However, the more precise the definition in the BIT is, the less discretion is left to the court or the arbitration tribunal. Therefore, it should be considered to limit this standard, since today there are practically no investment disputes in which investors are not invoking the violation of this standard.

The proposed changes in the text are the basic way to limit this standard and the similar standard of full protection and security, by referring to customary international law. It is recommended to further limit the framework of these standards by more precisely defining the contents of this standard.

✓ **Separate the breach of FET standards from the breach of other protection standards**

Arbitration tribunals in practice often see the FET clause as a comprehensive standard which essentially covers all other violations of obligations that a state can make. Such an approach broadens the international responsibility of a country – which is to be avoided by this proposal. BIT models of certain countries do contain such limitations.

✓ **Narrow the field of application of the most favoured nation clause (MFN)**

Since the most favoured nation clause (MFN) is often used in practice as the basis to determine the jurisdiction of the arbitration tribunal, this aspect of the Treaty should also be taken into account. Any doubts which exist in practice about the “procedural” use of MFN would be avoided with the proposed change, whereas the countries would be sure that investors from the other contracting party have access to only those forums for dispute resolution which had been envisaged by this Treaty. Accordingly, we would like to propose the narrowing of this provision so as to avoid such problems in practice, i.e. to avoid the broadening of BITs to other agreements.

✓ **Limit or more precisely define the expropriation clause**

In contemporary practice, the standard of protection from expropriation is more frequently used as referring to indirect expropriation (measure equal to expropriation), than to direct expropriation. Therefore, if state authority is to be further protected in this provision, it would be

necessary to limit or exclude the part of the text that pertains to indirect expropriation.

✓ **Exclude or more precisely define the so-called “umbrella clause”**

This provision is the famous umbrella clause, which most theorists see as the clause with the effect to turn a contractual obligation into a BIT obligation. This practically means that the state could also be responsible internationally for the violation of the BIT by violating the commercial agreement with the investor. Of course, this will always depend on the circumstances of a specific case and the formulation of the clause itself.

Seeing that in general such a clause puts a state under risk to be sued before an international forum for the violation of a BIT due to the violation of the agreement with the investor, we consider that such a clause should be excluded from the BIT. If it is not possible to completely exclude this clause, we would recommend to include a different formulation of this provision, which could potentially affect its more restrictive application.

✓ **Narrow the provision on dispute resolution**

Even though standard practice implies that investors have the right to choose the forum before which they wish to initiate a proceeding, it was proposed to consider the option that initially the state and the investor attempt to agree on the choice of forum. If this is not adopted, than it would mean that the investor has the right to choose before which body or institution to initiate the procedure.

It is recommended to narrow the provision on dispute resolution in order to narrow the jurisdiction and the opportunity to submit disputes from other agreements for arbitration according to the BIT.

✓ **Exclude the so-called sunset clause, or introduce a provision on statute of limitation**

In order to regulate the mechanism of dispute resolution between the state and the investor in as many details as possible, it is suggested to consider the inclusion of a provision on the statute of limitation from the BIT. This is suggested mostly taking into account the models of Canadian and US BITs which envisage that the investor shall not have the right to initiate the procedure for the violation of a BIT, if a certain deadline passed after the alleged violation was discovered.

In addition to the given general exemption, this clause could also include: protection of public morals and security, health safety, environment protection, financial system protection, etc.

Main challenges

1. Since Montenegro is a candidate for accession to the European Union, some of the main challenges for us in the next years could arise from the discussions in the European Commission about the validity of BITs signed between EU member states.

It should be noted here that Montenegro is party to 25 bilateral investment treaties which are in force. Most of these BITs were concluded with EU member countries. (In addition, two agreements were signed in 2010 and 2012, which are not in force.) Also, many treaties which are in force were inherited from former countries of which Montenegro was a member.

2. Another main challenge is coordination within Montenegro's public administration. Currently, investment policy activities and bilateral agreements are divided among several institutions and sectors within these institutions and organisations – without a central coordinating authority.

3. A more general challenge are insufficient administrative capacities.

Key policy tools for overcoming these challenges

- **SEE IPR recommendations**

Provide an objective evaluation of Montenegro's legal, regulatory and institutional framework for FDI to attract increased foreign and direct investment, as well as how to maximize the benefits from it.

Recommendations are concrete and action-oriented.

- **The World Investment Report 2017**

Assist in addressing the challenges arising from old-generation treaties

Take stock of reform areas and available policy options

Chart the way forward for sustainable development-oriented IIA reform