

**NATIONAL
TREATMENT FOR
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Chapter III

CLARIFICATIONS OF THE NATIONAL TREATMENT INSTRUMENT

"Clarifications" refer to opinions by the Committee on International Investment and Multinational Enterprises on how particular aspects of the instrument should be applied in practice. They may concern general provisions of the instrument or the specific categories used for classifying National Treatment measures.

Clarifications help Member countries decide whether a specific measure is an exception to National Treatment, whether it should be reported for purposes of transparency, or whether the measure falls outside the scope of the instrument. They also assist in classifying measures in their proper categories.

In general, the Committee develops clarifications during its periodic review of the instrument or when it examines Member country measures relating to National Treatment. The Committee may however, formulate a clarification whenever it sees the need.

This chapter looks first at the general clarifications before turning to those concerning the specific categories of measures.

Clarifications of the scope of the instrument

Operating in their territories

The National Treatment instrument calls for treatment by a host government of foreign-owned or controlled enterprises operating in their territories no less favourable than that accorded to domestic enterprises in like situations. The term "operating in their territories" in the instrument conveys the idea of doing business from a place of business in the host country, as distinct from conducting business in the country from abroad. This recognises that Member countries' practices differ regarding recognised forms of business organisation, but that the main forms of doing business are through locally incorporated subsidiaries and branches. The main factor is the existence of an effective presence and not the legal form this present may take, except in certain cases concerning direct branches (see section 1.4, and the clarification of the category of measures "Investments by Established Foreign-Controlled Enterprises", below.)

Foreign-controlled enterprises, owned or controlled

The 1976 Declaration provides that National Treatment should be accorded to foreign-controlled enterprises owned or controlled directly or indirectly by nationals of Member countries. However, it is not appropriate, or feasible, to follow the lines of ownership which might result in excluding companies already established in a Member country. The key element is the recognition of the parent company as a national enterprise by an OECD Member country, provided that it is effectively present in the OECD area.

Treatment no less favourable than that accorded in like situations to domestic enterprises

As regards the expression "in like situations", the comparison between foreign-controlled enterprises established in a Member country and domestic enterprises in that Member country is valid only if it is made between firms operating in the same sector. More general considerations, such as the policy objectives of Member countries, could be taken into account to define the circumstances in which comparison between foreign-controlled and domestic enterprises is permissible inasmuch as those objectives are not contrary to the principle of National Treatment. In any case, the key to determining whether a discriminatory measure applied to foreign-controlled enterprises constitutes an exception to National Treatment is to ascertain whether the discrimination is motivated, at least in part, by the fact that the enterprises concerned are under foreign control.

Equivalent Treatment

According National Treatment to branches and other unincorporated entities of foreign-controlled enterprises may sometimes be subject to certain constraints. The Committee developed the concept of equivalent treatment to take care of situations where identical treatment cannot be accorded to these entities because of their special nature. These situations are those where prudential considerations relating to financial or insurance sector activities, or legal/technical differences preclude a Member from according identical treatment.

These considerations, as opposed to those relating solely to foreign control, permit Members to apply measures to branches and other unincorporated entities of foreign-controlled enterprises which differ from those applied to domestic enterprises. The difference in treatment should, however, be no greater than that which is strictly necessary to meet prudential requirements or other legal/technical differences, and should not, beyond that, result in requirements that unfavourably affect the equality of competitive opportunities on the market.

Under these circumstances, measures providing equivalent treatment conform with the National Treatment commitments and are not notified to the

Organisation. Where a Member believes that equivalent treatment is not given in a specific instance, that Member may ask that the measure in question be reported and explained. The measure can then be examined by the Committee.

Relation to the OECD Codes of Liberalisation

The Committee has established a clear operational dividing line between the National Treatment instrument and the OECD Codes of Liberalisation, thereby avoiding any gaps or overlaps in regard to direct investment operations. The Codes deal with investment by non-resident enterprises including the right of establishment, e.g. limitations on non-resident (as opposed to resident) investment affecting the operations of enterprises; and other requirements set at the time of entry or establishment, even if these concern operational requirements. After entry, the treatment accorded to foreign-controlled enterprises operating in Member countries, including new investment by already established foreign-controlled enterprises, is covered by the National Treatment instrument.

Although the scope of the instruments are quite distinct, a given measure may have to be reported under both if that measure sets conditions at the level of enterprise establishment as well as on the activities of foreign-controlled enterprises already operating in the country concerned. In applying this general rule, it is necessary to look separately at the situation of subsidiaries and branches (and other non-incorporated entities).

In the case of subsidiaries, the general rule is applied without difficulty. In the case of branches, a distinction is made between "direct" branches (whose parent company is a non-resident) and "indirect" branches (whose parent company is the local subsidiary of a non-resident). "Indirect" branches are clearly covered by the National Treatment instrument in respect of all categories of measures in the same way as subsidiaries. The National Treatment instrument does not, however, cover measures concerning the investment activities of "direct" branches (i.e. measures in the category of investment by established foreign-controlled enterprises). These branches are not considered legally capable of direct investment operations on their own account. Rather, when making such investment, direct branches are considered as agents of their foreign parent who would be the beneficial owner of assets acquired. However, measures affecting investment by direct branches are covered by the Code of Liberalisation of Capital Movements. Measures in all other categories (government procurement, official aids and subsidies, access to local finance, and tax obligations) affecting "direct" branches continue to be covered by the National Treatment instrument. [See also the clarification below of the category "Investment by established foreign-controlled enterprises".]

Standstill

The Committee recently reaffirmed its understanding on standstill reached in November 1988. According to that understanding, the Committee stressed that