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TREATY BETWEEN THE UNITED STATES OF AMERICA AND THE ORIENTAL REPUBLIC OF URUGUAY CONCERNING THE ENCOURAGEMENT AND RECIPROCAL PROTECTION OF INVESTMENT (TREATY DOC. 109–9)

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Mr. LUGAR, from the Committee on Foreign Relations, submitted the following

REPORT

[To accompany Treaty Doc. 109–9]

The Committee on Foreign Relations ("committee"), to which was referred the Treaty Between the United States of America and the Oriental Republic of Urguay Concerning the Encouragement and Reciprocal Protection of Investment, with Annexes and Protocol, signed at Mar del Plata on November 4, 2005 ("Proposed BIT") (Treaty Doc. 109–9), having considered the same, reports favorably thereon and recommends that the Senate give its advice and consent to ratification thereof, as set forth in this report and the accompanying resolution of advice and consent to ratification.

CONTENTS

I. PURPOSE

The basic purposes of the bilateral investment treaty ("BIT") program are to: protect investment abroad in countries where investors' rights are not already protected through existing agreements, such as free trade agreements; encourage the adoption of market oriented domestic policies which treat foreign investment in an open, transparent, and non-discriminatory manner; and support the development of international law standards consistent with these objectives. There are six primary benefits which flow to parties whose investments are covered by BITs. First, a BIT provides that investors and their "covered investments" are entitled to be treated as favorably as the host country treats its own or third country investments. Second, it provides a defined limit on the expropriation of investments and for prompt payment of adequate and effective compensation if and when expropriation may take place. Third, it provides for transferability of funds into and out of the host country without undue delay under a market rate of exchange and encompasses all transfers related to a covered investment, creating a predictable environment. Fourth, it limits circumstances in which performance requirements can be imposed. Fifth, it gives investors from each country the right to submit an investment dispute with the treaty partner's government to international arbitration, rather than domestic courts. Finally, a BIT gives investors the ability to utilize management personnel of their choice, regardless of nationality.[1]

II. Background

The United States and Uruguay announced their intent to negotiate a BIT on November 21, 2003, at the conclusion of the ministerial meeting of the Free Trade Agreement of the Americas in Miami, Florida. According to the negotiating parties, the decision to pursue BIT negotiations emerged from work conducted by the United States–Uruguay Joint Commission on Trade and Investment, which was created in 2002 to enhance trade and investment relations between the two countries. Negotiations began in the spring of 2004 and were concluded on September 7 of that year. The treaty was signed on November 4, 2005 and was approved by the Uruguayan legislature in December 2005. It was submitted to the United States Senate for advice and consent to ratification on April 4, 2006.

The Proposed BIT is the 40th such treaty concluded by the United States, but the first negotiated since 1999. It is the first BIT negotiated on the basis of a new U.S. model BIT text, which was completed in 2004. The new model BIT is intended to encompass certain objectives from the Bipartisan Trade Promotion Authority Act of 2002.[2] The model also contains similar provisions to the investment chapters of recently negotiated free trade agreements. U.S. business interests have indicated their support for the Proposed BIT.[3]

III. Summary of Key Provisions

A detailed article-by-article discussion of the Proposed BIT is attached to the Letter of Transmittal from the Secretary of State to

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[1] U.S. Bilateral Investment Treaty Program, Fact Sheet, Bureau of Economic and Business Affairs, November 7, 2005; www.state.gov/e/eb/rls/fs/22422.htm

[2] *See, e.g.*, Sec. 2102(b)(3) of P.L. 107–210 (19 U.S.C. § 3802(b)(3)).

[3] Through communications with the committee, business groups such as the Emergency Committee for American Trade and The National Foreign Trade Council have recently indicated their support for approval of the proposed treaty.

the President, which is reprinted in full in Treaty Document 109–9. A summary of the key provisions of the Proposed BIT is set forth below.

ARTICLE 1

Definitions. The Proposed BIT defines the term "investment" broadly: the term means "every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk." The definition contains a non-exclusive list of the forms that an investment may take, beginning with an "enterprise," and including, *inter alia,* equity, bonds, futures, turnkey operations, intellectual property rights, licenses and authorizations conferred under domestic law, and other tangible or intangible, movable or immovable property and related property rights, such as leases and the like. An "enterprise" includes non-profit as well as commercial entities and both private and governmentally owned or controlled firms. An "investor of a Party" is "a Party or state enterprise thereof, or a national or an enterprise of a Party, that attempts to make, is making or has made an investment in the territory of the other Party; provided, however, that a natural person who is a dual citizen shall be deemed to be exclusively a citizen of the State of his or her dominant and effective citizenship." A "covered investment" means, with respect to a Party "an investment in its territory of an investor of the other Party in existence as of the date of entry into force of this Treaty or established, acquired, or expanded thereafter."

ARTICLE 2

Scope and Coverage. The Proposed BIT applies to "measures adopted or maintained by a Party relating to: (a) investors of the other Party; (b) covered investments; and (c) with respect to Articles 8, 12, and 13 (regarding transparency of investment laws and regulations, environment, and labor) all investment in the territory of the Party." The obligations in Articles 1–22 apply to state enterprises or other persons exercising any governmental authority delegated to it by the Party as well as to the political subdivisions of the Party.

ARTICLE 3

National Treatment. This article requires each Party to accord national treatment to investors of the other Party and to covered investments with respect to the entire life cycle of an investment. National treatment is deemed to be "treatment no less favorable than that it accords, in like circumstances" to its own investors or to investments in its territory of its own investors, as the case may be. With regard to regional governments, it is defined as "treatment no less favorable than the treatment accorded, in like circumstances" by the regional government "to natural persons resident in and enterprises constituted under the laws of other regional levels of government and to their respective investments."

ARTICLE 4

Most Favored Nation Treatment. Under this article, Parties are required to grant to investors of the other Party and to covered investments the treatment no less favorable than that accorded "in like circumstances" to non-Party investors and to investments in its territory by non-Party investors, respectively, with respect to the activities listed in Article 3.

ARTICLE 5 AND ANNEX A

Minimum Standard of Treatment. This article establishes a minimum standard of treatment that each Party owes to covered investments. The minimum standard of treatment is defined as "treatment in accordance with customary international law, including fair and equitable treatment and full protection and security." It also states that a breach of another provision of the Proposed BIT or of a separate international agreement would not necessarily constitute a breach of this article.

Annex A

Annex A contains the understanding of the Parties that "customary international law," as referenced generally in the Proposed BIT, and as specifically mentioned in Article 5 "results from a general and consistent practice of States that they follow from a sense of legal obligation." For purposes of Article 5, the "customary international law minimum standard of treatment of aliens refers to all customary international law principles that protect the economic rights and interests of aliens."

ARTICLE 6 AND ANNEX B

Expropriation and Compensation. This article states that neither Party may expropriate or nationalize a covered investment, directly or indirectly, unless for a public purpose, in a non-discriminatory manner, with compensation, and in accord with due process and the treaty's minimum standard of treatment requirements. Compensation must be timely and equivalent to the value of the expropriated investment immediately before the expropriation.

Annex B

Annex B states the understanding of the parties that Article 6 reflects customary international law, and that expropriation results only when the state's interference is with a property right in an investment. Annex B further explains that Article 6 addresses two types of expropriation: direct expropriation, involving formal transfer of title or outright seizure, and indirect expropriation, involving a case-by-case inquiry that considers the economic impact of the government action, its interference with investment-backed expectations, and its character. Under paragraph 4(b) of Annex B, the Parties confirm their shared understanding that, except in rare circumstances, nondiscriminatory regulation "to protect legitimate public welfare objectives, such as public health, safety, and the environment," do not constitute indirect expropriation.

ARTICLE 7

Transfers. This article requires each Party to permit all transfers relating to a covered investment to be made freely and without delay into and out of its territory, thus ensuring that an investor may repatriate funds associated with investment activities. Such transfers are expressly deemed to include contributions to capital; profits, dividends, capital gains, and proceeds from the sale or liquidation (or any partial sale or liquidation) of the investment; interest, royalty payments, and various fees; contract payments; compensation from expropriations; restitution for losses resulting from war or armed conflict or civil strife; and payments arising out of a dispute. Transfers must be allowed to be made in a freely usable currency at the market rate of exchange prevailing on the date of transfer.

ARTICLE 8

Performance Requirements. This article prohibits the Parties from imposing requirements on the establishment, acquisition, expansion, management, conduct, operation, or sale or other disposition of an investment of an investor of a Party or of a non-Party in its territory that may impair the profitability and competitiveness of an investment. In addition, neither Party may condition the receipt, or continued receipt, of an advantage during the life-cycle of an investment of a Party or of a non-Party on compliance with certain specified requirements in this article. A Party may, however, condition the receipt or continued receipt of an advantage on compliance with a requirement to locate production, supply a service, train or employ workers, construct or expand particular facilities, or carry out research or development in its territory. The prohibition on technology transfer requirements does not apply with regard to certain measures consistent with the WTO Agreement on Trade-Related Intellectual Property Rights or when the requirement is designed to remedy a practice determined after judicial or administrative process to be anti-competitive under the Party's competition laws.

ARTICLE 9

Senior Management and Boards of Directors. This article states that a Party may not place a nationality requirement on the individuals appointed to senior management of an enterprise of the Party that is a covered investment, but may require that a majority of the board of directors, or a committee of the board, be of a particular nationality, or resident in its territory, provided that the requirement does not "materially impair" the investor's ability to exercise control over its investment.

ARTICLE 12

Investment and Environment. In this article the Parties recognize that it is "inappropriate to encourage investment by weakening or reducing the protections afforded domestic environmental laws" and are required to "strive to ensure" that they do not waive or offer to waive such laws in a way that "weakens or reduces the protections afforded in those law as an encouragement for" an investment in its territory. If one Party considers that the other has offered such an encouragement, it may request consultations and the Parties are to consult with the aim of "avoiding any such encouragement." Nothing in the Proposed BIT may prevent a Party from taking any measure otherwise consistent with the Proposed BIT "that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns."

ARTICLE 13

Investment and Labor. In this article the Parties recognize that it is "inappropriate to encourage investment by weakening or reducing the protections afforded in domestic labor laws" and are required to "strive to ensure" that they do not waive or offer to waive such laws in order to encourage investment "in a manner that weakens or reduces adherence to the internationally recognized labor rights" listed in the article. It also provides that nothing in the Proposed BIT may be construed to prevent a Party from taking any measure otherwise consistent with the Proposed BIT "that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to labor concerns."

ARTICLE 14, AND ANNEXES I, II, III

Non-Conforming Measures. This article provides that Articles 3, 4, 8, and 9 (regarding, respectively, national treatment, MFN treatment, performance requirements, engagement of senior management) do not apply to non-conforming central and regional government measures listed in a Party's Schedule to Annexes I or III, or to a local level of government. In addition, these articles will not apply to any measure that a Party adopts or maintains with respect to sectors, sub-sectors, or activities listed in its Schedule to Annex II.

ARTICLE 17

Denial of Benefits. This article allows a Party to deny benefits to enterprises and investments if persons of a non-Party own or control the enterprise and the denying Party (1) does not maintain diplomatic relations with the non-Party or (2) adopts or maintains measures with regard to the non-Party that prohibit transactions with the enterprise or that would be circumvented if the treaty benefits were accorded to the enterprise.

ARTICLE 18

Essential Security. This article contains an exception for measures related to a Party's essential security interests.

ARTICLE 20

Financial Services. This article provides extensive provisions regarding financial services and special procedures for disputes in the area. A Party is not prevented from "adopting or maintaining measures relating to financial services for prudential reasons . . . or to ensure the integrity or stability of the financial system." The term "prudential reasons" is understood to include "the maintenance of the safety, soundness, integrity, or financial responsibility of individual financial institutions." This article also sets forth special procedures for State-to-State disputes involving financial services.

ARTICLE 21

Taxation. This article specifies that the Proposed BIT does not apply to "taxation measures" except as provided in Article 21. It does not affect the rights and obligations of a Party under any tax convention, and to the extent that there is an inconsistency between a tax convention and the Proposed BIT, the tax convention prevails. Departing from the 2004 Model, it provides that national treatment and MFN obligations apply to all taxation measures other than tax measures relating to direct taxes (i.e., income and capital gains taxes, estate and gift taxes, and the like). In addition, the expropriation article applies to all taxation measures, except that if an investor-state claimant asserts that an expropriation is involved, the claimant may only submit the claim to arbitration if the claimant had first referred the issue in writing to the competent tax authorities of both Parties and the Parties failed to agree, within 180 days after the date of the claimant's referral, that the measure was not an expropriation.

ARTICLES 23–34

Investor-State Dispute Settlement. Article 24 provides that if a disputing party considers that a dispute cannot be resolved through consultations and negotiations, the claimant may initiate arbitration. An investor may file a claim at least six months after the "events giving rise to the claim" and may do so under the ICSID Convention, the ICSID Additional Facility Rules, the UNCITRAL Arbitration Rules, or if the disputing parties agree, to any other arbitral mechanism. The arbitration rules invoked by the claimant will govern the arbitration except as modified by the Proposed BIT.

Article 26 provides that claims cannot be submitted if more than three years have elapsed from the date on which the claimant acquired (or should have acquired) knowledge of the alleged breach and knowledge that loss or damage was incurred. The claimant must consent in writing to arbitration according to conditions set out in the Proposed BIT and the claim must be accompanied by a waiver of the right to initiate or continue before any administrative tribunal or court under the law of either Party, or under other dispute settlement procedures, any proceeding with respect to any measures alleged to constitute the breach.

Article 27 addresses the selection of arbitrators. Tribunals are normally to be composed of three arbitrators, one appointed by each of the Parties and the third and presiding arbitrator, appointed by agreement of the Parties. Except as provided for financial services disputes, if a tribunal is not constituted within 75 days of the date the claim is submitted, the Chairman of the ICSID Administrative Council, on request of a disputing Party, is to appoint the remaining panelists.

Article 28 governs the conduct of the arbitration, including the venue, the ability of the non-disputing party to make oral and written submissions to the tribunal, and the possibility of amicus briefs from a non-disputing person or entity. It also provides that the tribunal may award an interim award of protection to preserve a disputing party's rights.

Article 29 provides for transparency in arbitral proceedings, requiring that documents be made public and that the tribunal conduct hearings open to the public, and Article 30 addresses the law that the arbitrators are to apply in the proceedings.

Article 34 specifies that a tribunal may award only monetary damages and any applicable interest, and restitution of property, in which case the award is to provide that the respondent may pay monetary damages and any applicable interest in lieu of restitution. The tribunal may also award costs and attorney's fees in accordance with the Proposed BIT and the applicable arbitration rules; a tribunal may not award punitive damages. The award has no binding force except between the disputing parties and with regard to the particular case. Each Party must provide for the enforcement of an award within its territory and, where a Party fails to abide by or comply with an award, the non-disputing Party may seek State-to-State dispute settlement under Article 37.

ARTICLE 37

State-to-State Dispute Settlement. This article sets forth dispute settlement procedures between states. Except for disputes arising under Articles 12 and 13 (environment and labor), any dispute between the Parties concerning the interpretation or application of the Proposed BIT that is not resolved through consultations or other diplomatic means is to be submitted, at the request of a Party, to binding arbitration by a tribunal in accordance with international law. Where there is no agreement by the Parties, the UNCITRAL Arbitration rules are to apply, except as modified by the Parties or the Proposed BIT. Generally, tribunals are to consist of three arbitrators, one appointed by each Party and the presiding arbitrator appointed by agreement of the Parties. If a panel is not constituted within 75 days after a claim is submitted, the Chairman of the ICSID Administrative Council, on request of a disputing Party, is to appoint the remaining arbitrators.

ANNEX C

Submission of a Claim to Arbitration. Annex C departs from the 2004 Model in placing a special limitation on U.S. investors seeking local remedies in the territory of the other Party. Specifically, a U.S. investor may not submit to investor-State arbitration a claim that Uruguay has breached an obligation under Articles 3–10 if the investor has alleged that breach of the obligation in proceedings before a court or administrative tribunal of Uruguay. The limitation reflects the fact that treaty claims may be brought in Uruguayan local courts.

ANNEX F

Financial Services. Annex F, a departure from the 2004 Model BIT, expands on the obligations that the Parties undertake under Article 3 (national treatment) and Article 4 (MFN treatment) regarding a "financial institution of the other Party" (defined for the purposes of paragraphs 1 and 2 as "a financial institution, including a branch, located in the territory of a Party that is controlled by persons of the other Party"). It further provides in paragraph 4 that no claim that a measure relating to an investor of a Party, or a covered investment, in a "financial institution" (defined for the purposes of paragraph 4) located in the other Party breaches Article 3 or 4 may be submitted to investor-State arbitration.

ANNEX G

Sovereign Debt Restructuring. Annex G, which addresses investor-State claims involving sovereign debt restructuring by Uruguay, is another departure from the Model BIT. The Annex states that no claims that the "restructuring of a debt instrument issued by Uruguay" breaches an obligation in Articles 5 though 10 may be submitted for investor-State arbitration if the restructuring is a "negotiated restructuring," as defined in the Annex, at the time the claim is submitted or becomes one after submission of the claim. A U.S. investor may not submit a claim for investor-State arbitration that a "restructuring of debt issued by Uruguay" breaches an obligation under Articles 5 through 10 unless 270 days have elapsed from the date of the events giving rise to the claim.

IV. COMMITTEE ACTION

The committee held a public hearing on the Proposed BIT on June 12, 2006. The hearing was chaired by Senator Lugar.[4] The committee considered the proposed treaty on August 1, 2006, and ordered the proposed treaty favorably reported by voice vote, with a quorum present and without objection, with the recommendation that the Senate give advice and consent to its ratification, as set forth in this report and the accompanying resolution of advice and consent to ratification.

V. COMMITTEE RECOMMENDATION AND COMMENTS

On balance, the committee believes that the Proposed BIT is in the interest of the United States and urges that the Senate act promptly to give advice and consent to ratification. The committee urges the executive branch to continue to work with interested parties, including those in the U.S. business community, to ensure the highest standards of protection for U.S. investors overseas.

VI. RESOLUTION OF ADVICE AND CONSENT TO RATIFICATION

Resolved (two-thirds of the Senators present concurring therein), That the Senate advise and consent to the ratification of the Treaty between the United States of America and the Oriental Republic of Uruguay Concerning the Encouragement and Reciprocal Protection of Investment, with Annexes and Protocol, signed at Mar del Plata on November 4, 2005 (Treaty Doc. 109–9).

[4] A transcript of the June 12, 2006 hearing is included as an appendix to this report.

VII. APPENDIX: HEARING—U.S.–URUGUAY BILATERAL INVESTMENT TREATY

U.S.–URUGUAY BILATERAL INVESTMENT TREATY

MONDAY, JUNE 12, 2006

U.S. SENATE,
COMMITTEE ON FOREIGN RELATIONS,
Washington DC.

The committee met, pursuant to notice, at 3:03 p.m. in Room SD–419 Dirksen Senate Office Building, Hon. Richard G. Lugar, chairman of the committee, presiding.

Present: Senator Lugar.

OPENING STATEMENT OF HON. RICHARD G. LUGAR, U.S. SENATOR FROM INDIANA

The CHAIRMAN. This hearing of the Foreign Relations Committee is called to order. The committee meets today to review the Bilateral Investment Treaty with Uruguay, which was signed last fall. This agreement promotes investment and economic cooperation with a friend and partner in the Western Hemisphere. It would deliver important benefits to the United States, and it would reinforce the significant economic reforms that Uruguay has undertaken in the recent past.

The agreement has already been approved overwhelmingly by both houses of the Uruguayan legislature. This support is a measure of President Vázquez's political leadership and his commitment to build a stronger political and economic relationship between Uruguay and the United States.

More than 80 United States companies have operations in Uruguay. The United States became Uruguay's largest export market in 2004. In the absence of the Free Trade Agreements of the Americas that facilitates trade on a hemispheric scale, we should move forward where we can to create open markets on a bilateral basis. Consequently, the United States should consider whether the groundwork laid by this bilateral investment treaty could be expanded into a full Free Trade Agreement with Uruguay.

I encourage the administration to continue its successful pursuit of bilateral investment treaties. These agreements open opportunities for our domestic companies and establish greater security for mutual investments. They promote open, transparent, and non-discriminatory treatment of private investment, which is essential to ensuring that American companies can compete equitably in foreign markets. Cooperation on the commercial front also enhances our broader relationships with other nations.

I welcome our distinguished witness, Mr. Daniel Sullivan, and congratulate him on his recent confirmation as Assistant Secretary of State for Economic and Business Affairs. The committee looks forward to our discussion about the treaty. And in a moment, we look forward to the testimony of Secretary Sullivan. Would you please proceed and let me indicate at the offset that your full statement will be made a part of the record. You may deliver it in full or summarize, as you wish.

STATEMENT OF HON. DANIEL S. SULLIVAN, ASSISTANT SECRETARY FOR ECONOMIC AND BUSINESS AFFAIRS, DEPARTMENT OF STATE, WASHINGTON, D.C.

Mr. SULLIVAN. Thank you, Mr. Chairman. I would like to just summarize the key points of my written testimony. And thank you for the opportunity to testify before your committee, today. The administration strongly recommends that the Senate give its advice and consent to the U.S./Uruguay Bilateral Investment Treaty. This treaty will protect the rights of U.S. investors in Uruguay; create opportunities for U.S. exports to Uruguay; and promote growth, economic reform and greater awareness of the benefits of open investment and trade regimes both in Uruguay and throughout the region.

This is also the first such treaty negotiated on the basis of the new U.S. 2004 model BIT, which was developed in consultation with this committee, other members of Congress, the private sector, NGOs, and your staff. The new model BIT, like the older one, is a valuable tool to promote sound investment policies, and economic growth with our partners.

The 2004 model draws on our experience with the NAFTA and is similar to the investment provisions in the FTAs that we've been negotiating. It enhances the core investment principles that have been the foundation of our BIT program for more than 20 years. The Uruguay BIT conforms closely to the new model. Although Uruguay is a small country, it is an important political and economic partner for the United States in the Americas.

The United States is one of Uruguay's largest trading partners, and President Bush and President Vázquez agreed last month to broaden and deepen our economic and trading relationship. A BIT with Uruguay would be an important milestone in our growing economic partnership, will provide strong protections for U.S. investors, and will reinforce Uruguay's commitment to free and open trade in investment.

I thank the committee for its consideration of this treaty and I will be glad to answer any questions that you may have. Thank you, Mr. Chairman.

[The prepared statement of Mr. Sullivan follows:]

PREPARED STATEMENT OF DANIEL S. SULLIVAN

Chairman Lugar, ranking member Biden, members of the committee, and staff: Thank you for the opportunity to testify before the Senate Foreign Relations Committee as the administration seeks the advice and consent of the Senate to ratification of the U.S.-Uruguay Bilateral Investment Treaty.

The administration strongly recommends that the Senate give its advice and consent to the U.S.-Uruguay Bilateral Investment Treaty (BIT). This treaty, the first negotiated on the basis of the text of the new U.S. 2004 Model BIT, will protect the rights of U.S. investors in Uruguay. It will also serve to promote a more open investment and trade regime in the region and potentially more broadly in Latin America.

The United States, with over $2 trillion invested abroad as of 2004, has a major stake in extending protections to our investors and improving their access to foreign markets. The U.S. BIT program, which has enjoyed bipartisan support throughout its existence, is a key tool in that effort. Over the past 24 years, the BIT program has had the same basic objectives: Protecting United States investment abroad; encouraging the adoption of market-oriented investment policies that treat private investment in an open, transparent, and non-discriminatory way; and supporting the development of international legal standards consistent with these policies.

The BIT program was initiated to promote and protect U.S. investors in other countries by building on the principles contained in earlier Treaties of Friendship, Commerce and Navigation (FCN). The program has helped to reinforce sound investment policy in a variety of developing nations and in economies that have undertaken the transition from central planning. By creating conditions more favorable to U.S. private investment, these treaties assist countries in their efforts to develop the private sector, thereby strengthening their economies. Furthermore, as more nations agree to conclude a BIT with the United States, the important investment principles they contain gain wide acceptance and contribute to the development of international law in directions consistent with U.S. interests.

Since the inception of the Bilateral Investment Treaty program in 1982, the United States has concluded 46 BITs, 39 of which have entered into force. We have active discussions underway with Pakistan and are exploring potential BITs with several other countries. The Department of State and the United States Trade Representative co-lead negotiations with the support of Commerce, Treasury, and other agencies.

BITs are negotiated on the basis of a model text that has been periodically updated. The most recent revision of the model BIT was completed in 2004, and, as noted earlier, is the model on which the U.S.-Uruguay Treaty is based. The 2004 model text embodies the same basic investment principles as its predecessors. It is similar to the investment provisions of the North American Free Trade Agreement (NAFTA) and, in keeping with our policy of maintaining consistency across our agreements, is very similar to the investment chapters of our recently-concluded free trade agreements, including those with Chile, Singapore, five Central American countries and the Dominican Republic (CAFTA-DR), Morocco, Australia, Oman, Peru, and Colombia.

In addition to containing greater specificity than earlier model texts with respect to key provisions, our new model text contains several clarifications and procedural innovations designed to eliminate or deter frivolous claims and to make the investor arbitration process more efficient and transparent.

Our BIT with Uruguay conforms very closely with the new model and embodies the following core protections: (1) national treatment and most-favored nation treatment both before and after the establishment of an investment, which creates a level playing field for U.S. investors; (2) a minimum standard of treatment based on customary international law; (3) international law principles governing expropriation; (4) limitations on performance requirements, such as local content requirements; (5) the right to hire senior managers of their choice; (6) improved transparency with respect to investment-related laws and regulations; (7) a guarantee of free transfers of investment-related funds; and (8) binding international arbitration of investment disputes that can be invoked either by investors or by the Parties to the agreement.

Although Uruguay is a relatively small country, it has long been an important partner for the United States in the Americas. Our bilateral economic relationship has grown more important in recent years. In 1998, Uruguay sent over 55% of its exports to Mercosur countries.

By 2004, the United States had overtaken Mercosur as Uruguay's number one trading partner. The United States is also Uruguay's largest single source of foreign investment, with an accumulated stock of investment of over $600 million. Uruguay's GDP in 2005 was approximately $16.8 billion; its GDP growth in 2005 is estimated to be an impressive 6.6%, with export and investment growth rates of 16% and 20%, respectively. Uruguay's economy is projected to grow by 4.8% in 2006.

In 2004, the U.S.-Uruguay Joint Commission on Trade and Investment launched the negotiations that led to this BIT, and the Treaty was originally signed in Montevideo, just days before the election of the new Uruguayan President, Tabaré Vázquez, on October 31, 2004.

Following President Vázquez's inauguration in March 2005, his party began to examine the BIT and its options for proceeding. In September 2005, President Vázquez requested that the United States make several small changes to the text to accommodate Uruguayan concerns. The United States was able to agree to two of these proposed changes, and the text was altered and re-signed at the Summit of the Americas in Mar del Plata, Argentina, on November 5, 2005. The Uruguayan Parliament completed its domestic ratification procedures for the Treaty on December 27, 2005. President Bush transmitted the Treaty to the Senate on April 4, 2006.

The U.S.-Uruguay BIT differs in minor respects from the 2004 model BIT text. None of these differences represent departures from core BIT principles. The most important changes derived from Uruguay's desire to maintain flexible oversight of its financial sector. For example, one change prohibits all investor-state claims, except fro discrimination, for negotiated sovereign debt restructurings carried out under collective action clauses and certain other processes. Another arbitration-related difference form the model bars U.S. investors from submitting claims to investor-state arbitration if the investor or enterprise had previously alleged the same breach of a BIT obligation before a Uruguayan court or tribunal.

The Treaty text also includes a new clause to the Labor and Investment Article clarifying that a Party may adopt any non-discriminatory measure to ensure that investment is conducted in a manner sensitive to labor concerns provided the measure is otherwise consistent with the Treaty. This language is similar to the provision in the model text on environmental concerns. Other changes include relatively minor changes in defined terms, and other small, technical changes. A full description of each part of the Treaty text, including the departures from the model, has been included in the transmittal package, immediately following the end of the Treaty text.

In conclusion, the U.S.-Uruguay BIT will help protect the rights of U.S. investors in Uruguay; create more opportunities for U.S. exports to Uruguay by stimulating our already strong bilateral economic ties; and promote growth, continued economic reform, and greater awareness of the benefits of open investment and trade regimes. In addition, the U.S.-Uruguay BIT is the first of what we expect will be a new series of BITs based on the 2004 model text—BITs that will have more robust protections for U.S. investors than we have had in the past. These BITs will preserve the legitimate regulatory prerogatives of the United States and its negotiating partners, protect U.S. investors, and promote open and fair investment policies around the world. I thank the committee for its consideration of this treaty and I will be glad to answer any questions.

The CHAIRMAN. Let me just indicate, as you've pointed out, that the two Presidents met and discussed further deepening of our relationship, especially our trading ties, specifically now. I just raise the overall question, trying to outline how the administration is proceeding to accomplish these goals. And I touched upon this in the opening statement. After a successful conclusion of this investment treaty, isn't a Free Trade Agreement a natural step in the direction of deepening of these ties? Wouldn't a free trade agreement with Uruguay be in accordance with the U.S. Building Block Strategy in this region?

Mr. SULLIVAN. Thank you, Mr. Chairman. As you know and as you mentioned at the outset, the administration has been pursuing policies to increase trade and investment throughout Latin America through a number of different kinds of economic tools. I should note that I think, in a lot of ways, we've made significant progress in this regard. The statistic, I believe, that is most informative is—if you looked at the current FTAs that we either have, or that we are negotiating, or have completed—that the economies represented by those FTAs would account for over two-thirds of the GDP of the Western Hemisphere, without including the United States. So, there's been significant progress on that front.

As you mentioned, and as I stated in my opening remarks, President Bush and President Vázquez met and committed to deepening that economic relationship. The BIT is primarily the way that we're looking at doing that right now. There are a number of economic issues that can be addressed by the BIT, but it will also, as you mentioned, help the economic reform program that the Uruguayan government is committed to.

So, with regard to next steps in that relationship, the BIT is the primary focus. Specifically, with regard to an FTA, as you know, that is a process that requires significant consultation. Oftentimes, looking at potential FTA partners, there are a lot of issues that need to be addressed first, in terms of economic or investment issues. But as you know, prior to moving to an FTA, the consultation process on that decision, not only includes our potential partners, but the Congress, the private sector, and the interagency. And in terms of the specific question regarding an FTA with Peru, I think it might be a little bit premature to get into specifics, because I think that we're kind of at the beginning stages of that consultation process, Mr. Chairman.

The CHAIRMAN. Well, without pressing the issue, is the Brazilian influence in the area a factor in consideration of a free trade agreement? Does that play into the situation at all?

Mr. SULLIVAN. I think the answer to that is, we have said and I believe Ambassador Portman has said, with regard to trade in the Hemisphere, we welcome deepening our trading and investment relationship with all countries including those in Mercosur.

The CHAIRMAN. In which Brazil is a major factor.

Mr. SULLIVAN. That's right. That's correct. But, with regard to whether or not there's a prospect—well, let me back up here. With regard to the BIT, my understanding is that we haven't heard anything with regard to whether or not the Brazilian government has been supportive of this so we're assuming that is has. As I mentioned, it's an important building block.

So again, I want to get back to the point. It's more an issue of going through the consultations that we need to do, both in terms of domestic audiences, the Hill, private sector, and our trading partners in the area to—where we would move forward on that issue. So, I do not believe that the specific issue of Brazil, with regard to that question, has been raised and I am not aware of it.

The CHAIRMAN. For those listening to our dialogue and hearing the word BIT used, let me just indicate, as you have already, that this is the Bilateral Investment Treaty. And we have such treaties with 39 countries, according to our committee information.

What factors are a criteria for considering which countries are going to be possibilities for negotiation of a Bilateral Investment Treaty? And what was the impetus for seeking this particular treaty with Uruguay at this time? Was it the meeting of the two Presidents, or were there other factors that entered into this?

Mr. SULLIVAN. Thank you, Mr. Chairman. With regard to the general question, it's an especially important question now, because, as I noted in my testimony, we have developed a new model BIT and there's an interagency process that's ongoing, again, with close consultation with this committee and congressional staffs on possible future BIT partners, who we would be considering.

So, some of the factors that are important in that process—in that decision making process—include the depth of the economic relationship, the commitment to reform that the country that we would look at a possible BIT partner has, the way in which U.S. investors have been treated in the country, and key sectors in the country that we are considering, that may be of interest, and more broader foreign policy considerations.

One point that I want to emphasize is this idea of our BIT not only as providing protection for U.S. investors, but also as a vehicle to help drive economic reform programs. I think that's very important. And so, the extent to which a partner country is interested in a BIT is obviously a very important issue that goes into the consideration of possible future BIT partners.

With regard to your specific question, with regard to Uruguay, a lot of those considerations that I mentioned, came into play. As I mentioned earlier, a goal of the administration has been to increase trade and investment throughout the region and a Bilateral Investment Treaty is an important tool in that regard. And we saw Uruguay as a very good candidate for a number of the reasons again, that I have touched on. One of which is, they were very interested in 2004, approaching the administration with their interest in a Bilateral Investment Treaty. Also, there is—as you mentioned—a significant amount of economic reform being undertaken by the government, and we thought that a BIT would enable that process to gain some ground and to help in that regard. But also, more generally, in terms of our economic relationship, we understand right now, there are no investment disputes that we have involving any U.S. investors. They have been a success story in terms of IPR recently. They got off the 301 watchlist due to some of their activities. Even in terms of areas like corruption, where I think they ranked number two on the Transparency International List for its very pro-anticorruption policies. So, it's a number of these factors and given these factors, we thought it was an important move to make now.

The CHAIRMAN. As you know, as countries have been evaluated for the Millennium Challenge Account program, the corruption factor is one that really is very large among many. But it is one that has been difficult for some countries to meet. And by the same token, the incentive to do so, has led to many countries being interested in the program. But, you have testified that this isn't the case for Uruguay. Uruguay ranks second in terms of transparency. In other words, quite apart from this new treaty, they have made a great deal of progress. And I think that's an important point to make.

I would like to assess what kind of consultation process the administration undertook. I'm not certain what you're obligated to do under a bilateral investment treaty. You indicated that under the free trade agreement, apparently much more consultation with many parties, that you have enumerated, is required. Who, in the private sector, are really involved in the process of consultation? Does the 2004 model on which this agreement is based, reflect private sector input? Finally, is there private sector support for the treaty that you are presenting this afternoon?

Mr. SULLIVAN. Thank you, Mr. Chairman.

To answer your last question first, there is private sector support for this treaty. With regard to the consultations on the model BIT, as I believe you know, it took a fair amount of time to actually develop and come to agreement on different elements of the final model, that was produced in 2004. That consultation process—it took some time, because it involved a number of different parties. It involved a very robust interagency process, where different agencies weighed in on their different concerns. It also involved a significant consultation with the Congress, and members, and staffs. We were also guided in part by the TPA legislation, which had a number of provisions that were guiding new trade agreements.

Additionally, it included private sector involvement and civil society, the specific individual private sector entities. I do not have that at my fingertips, but I'd be glad to take that for a submission——

The CHAIRMAN. And share that for the record.

Mr. SULLIVAN. Yes, sir. We'll make sure we get back to you both in terms of that and then, the other NGO group, but the consultations were, as I mentioned, quite robust across a broad section and I believe that there is a lot of different interests involved, but I believe that we have struck a balance that has primarily succeeded in gaining support from all these groups.

The CHAIRMAN. Has there been some manifestation of that support of the individual firms? Have entities endorsed this treaty?

Mr. SULLIVAN. Mr. Chairman, again, I'll take that for submission. I know that, in general, the private sector support for this treaty has been strong. As to specific firms, I will take that for submission and get back to you on that.

[The additional information referred to above follows:]

ADDITIONAL INFORMATION SUBMITTED IN RESPONSE TO SENATOR LUGAR'S QUESTION

Mr. SULLIVAN. The Uruguay bilateral investment treaty is the first negotiated on the basis of the 2004 U.S. model text. In developing the model, the administration undertook extensive consultations with a wide range of private sector groups, as well as the Congress. We received input from private sector advisory bodies including the State Department's Advisory Committee on International Economic Policy, and the Industry Trade Advisory Committees administered by the Office of the U.S. Trade Representative and the Department of Commerce. Collectively, these groups encompass hundreds of representatives of interested constituencies, including business groups, trade unions, and other elements of civil society. In addition, several firms and organizations provided input in their individual capacities. To facilitate these consultations, we posted a draft of the model text on the State Department website in early 2004, while its development was underway.

Business associations involved in these consultations included the American Council of Life Insurers, the Emergency Committee for American Trade, the National Association of Manufacturers, the National Foreign Trade Council, the U.S. Coalition of Services Industries, and the U.S. Council of International Business. These groups represent a wide spectrum of U.S. businesses ranging from consumer products, manufacturing, and financial services, to energy sectors.

Labor, environmental, and other civil society groups involved in these consultations included AFL-CIO, the Center for International Environmental Law, Earthjustice, Friends of the Earth, Georgetown University Environmental Policy Project, Oxfam America, National Wildlife Federation, National Resources Defense Council, and the Sierra Club.

All of these groups made important contributions that helped to inform our work on the new model investment treaty, which was concluded in late 2004.

With respect to the Uruguay BIT in particular, we briefed private sector advisers through the Industry Trade Advisory Committee on the negotiations and consulted them on requests by Uruguay to depart from the model text.

Specific groups that have expressed support for the Uruguay BIT include the Emergency Committee for American Trade, the National Association of Manufacturers, and the U.S. Council for International Business.

The CHAIRMAN. For that matter, with trade groups and aggregates of firms, has someone spoken favorably about this? I presume then, that you have an affirmative answer to this question. Do private American investors feel secure in this treaty? Do they believe that this treaty offers them the protection that they would need in order to have—to use your terms—a robust relationship back and forth with Uruguay?

Mr. SULLIVAN. I think the answer to that, Mr. Chairman, is yes. The provisions—and I layout the provisions in my written statement—the eight core principles that are in this treaty that offer protection to private sector individuals. Really the essence of the treaty is the protection of investor rights, the opportunity to settle disputes, either through the domestic courts in Uruguay or through binding international arbitration. And that is a key component of this treaty. I might add, that with regard to the support that we've seen, one of the reasons is because there have been improvements in this treaty versus the previous model BIT. Both this treaty and the previous model BITs have the eight core protections, core principles that I mentioned in my opening statement, and we can discuss those if you have any questions on the particulars. But, where we think there's been improvement, is in the areas that have been of concern to investors, such as transparency. There are a number of provisions that make the process more transparent. And also in terms of the arbitration process itself, it clarifies some of the rules. It offers the opportunity to get rid of frivolous claims.

And so, the improvements that we think that build on this treaty from the previous model BIT, have engendered generally widespread support. So, we're confident that in a number of sectors, the support is very strong.

The CHAIRMAN. Now sometimes, even though we may have the best of intentions, there are things that go awry. An arbitration process is set up in previous bilateral investment treaties, as well as in this one. What has been the experience as you've examined the bilateral investment treaties in the past? Has the arbitration mechanism worked in ways that were beneficial to the United States, and at a minimum, provided fairness to our interest?

Mr. SULLIVAN. Yes. In general, the arbitration procedures have been followed and again—now sometimes, it's a lengthy process, which can be somewhat problematic—but in general, the arbitration procedures have been followed and they've also in general, been able to get investors the action and the justice really, that they have sought.

And again, I want to go back and emphasize the importance of having that option to make a choice between the domestic court of the country in which that individual is investing, binding international arbitration. And so having that option, is something that's the essence of the treaty. But the history of the program and our relations and in terms of where we have had other BITs, the BITs actually have been quite successful.

The CHAIRMAN. During your negotiation of this treaty, can you describe the kinds of investments in which the United States is involved? I mentioned in the opening statement that there are as many as 80 companies. But, what sort of industries are most prominent in this? What are the logical aspects of the flow of trade between the United States and Uruguay? What do they export to us and what do we export to them? In terms of pure financial arrangements, what kind of mechanisms are likely to be set up between the two countries that would be advantageous?

Mr. SULLIVAN. Thank you, Mr. Chairman. Our exports in 2005 totaled about $260 million to Uruguay, that was primarily in a number of high-tech goods, TV equipment, medical equipment. It is important to note that—and again, this is another reason we think this is an important treaty, U.S. exports are up—although from the small number, they're up by about 50—over 50 percent since 2002. So, we see that oftentimes what the case is, is that investment in a foreign country can be a platform for additional exports from the United States. And I think in this case, there's an opportunity to see that.

So, we also have investments in the financial area within Uruguay. And, although I do not believe that we have any large scale investments in any kind of energy sector there, an area in which I know you are very focused, a lot of the BITs that we have the individual investor is using the BIT as you know in the energy sector. Now, what we do have, in terms of the energy sector with Uruguay, is that they have been a purchaser also of energy equipment.

The CHAIRMAN. Yes.

Mr. SULLIVAN. That's an area of U.S. exports that has the potential to grow. Finally, it's not just investments, but one important element of the revised model BIT, is that if there are large service contracts between a government—the Uruguayan government—and an investor. So, those kind of large—so, for example say some kind of energy related service contract, that kind of contract would actually fall under the provisions of the BIT. So, it's fairly robust in terms of the different areas in which U.S. companies would be engaged, or could be engaged. And again, I think that's another reason why we believe this is a strong treaty.

The CHAIRMAN. This is a topical—almost current events question, as opposed to a broader problematic or philosophical one. In the past three weeks, many of the currencies in Latin America have been under stress. That has been true of currencies in other parts of the world. This may lead, during the latter part of the week, to central banks in six countries raising their interest rates very substantially.

I'm curious whether Uruguay is undergoing such a predicament presently. That is, is it experiencing rapid declining currency or fears of either inflation or of liquidity being terminated? If so, what effect is this likely to have in terms of the debate on this treaty in either country?

Mr. SULLIVAN. Mr. Chairman, with regard to the specific question, again, I'll—I'd like to take that for the record in terms of the specifics of the Uruguayan currency and what the situation is going—well, with regard to their financial markets.

[The information referred to above follows:]

ADDITIONAL INFORMATION SUBMITTED IN RESPONSE TO SENATOR LUGAR'S QUESTION

Mr. SULLIVAN. Many emerging-market currencies have depreciated over the past month. We have also seen volatility in emerging-market stocks and sovereign bonds in recent weeks. These developments are a reminder of the risks of investment. The government of Uruguay ratified the BIT before the most recent market turbulence; so it did not affect the debate in Uruguay.

I would like to point out that while many emerging-market currencies depreciated in recent weeks, the Uruguayan peso has remained quite stable. The Uruguayan economy has made a strong recovery since the financial crisis of 1999–2002. Most analysts expect real GDP growth of close to 5% this year, and annual inflation is running at about 6%. While the economy still has some vulnerabilities, the government of Uruguay has taken many steps to improve the strength of the financial system.

I should note that although we have been discussing BIT protections for foreign direct investment, portfolio investments, such as stocks and bonds, are also covered by the BIT. Together with the provision guaranteeing unrestricted transfers related to an investment, the BIT limits capital controls on covered portfolio investments. Such protections make it less likely governments will resort to controls, which can serve to exacerbate a crisis, and correspondingly can reassure investors, making it less likely they will act precipitously.

The BIT also addresses sovereign debt restructurings that can result from financial crises. If those restructurings are carried out under collective action clauses and certain other processes, the Uruguay BIT prohibits investors from filing claims, except for cases of discrimination. We believe that by supporting collective action clauses we help ensure orderly debt restructurings, which benefit investors and debtor nations.

Of course, while a BIT provides significant benefits to investors, it cannot create an investment environment that is entirely free of exchange-rate risk, default risk, or other risks.

Mr. SULLIVAN. But, the broader point that's raised, is an important one and it does relate to a provision in the BIT. In one of those provisions, is—and I believe, it goes to both Uruguayan and U.S. support for the agreement, but one of the provisions in the BIT that's been negotiated, which again, does not affect the core eight principles, but it is an important departure, that's important to highlight. And I did highlight it in my written testimony, was with regard solving debt restructuring with the Uruguayan's and to the degree to which, if that is done per the terms of the instrument, that that—those kind of activities would not fall within the provisions of the BIT, unless there was a claim by an investor that there was some kind of discriminatory practice.

So, unless that claim can stand a broader solving debt restructuring, would not be subject to the scope of the BIT and I believe that this was a provision that Uruguayan's were interested in, because it relates to some of the issues that you're talking about, which is to have, in your minds, flexibility to address potential financial emergencies and other issues with regard to financial crisis and our negotiators accepted that as important—as an important point for them.

The CHAIRMAN. So, translating this into less technical terms, it would mean, that United States investors still need to venture into the Uruguayan market, eyes wide open, with an idea of the debt structure of that government, and likewise its currency, because this treaty creates flexibility, in the event that Uruguay needs it to manage its situation. This could lead to a reduction in value of the currency or some type of restructuring of the debt, that could create some economic losses for an American investor or anybody else, including Uruguayan investors in this situation.

So, what you're saying is that the treaty, with respect to the Uruguayans in particular, recognizes that this is a difficult world, that restructuring and changes sometimes occur, and it provides for that flexibility. And so, we understand that, eyes wide open, as we enter into this treaty?

Mr. SULLIVAN. That's correct, Mr. Chairman. And that's an excellent point. The provisions of the BIT, as I mentioned, focus on the eight core principles, but there are some areas in which there are some exceptions and they're narrow and we tried to make them as narrow as possible in the treaty and it is important for investors to be aware of what these are, because it could affect their ability to bring actions under the BIT. And so, this one, the one that you have raised, particularly given this situation, and the condition of some of the other developing country economies is an important one to note.

The CHAIRMAN. Correspondingly, I think from the standpoint of Uruguay, it ought to be pointed out that investors in our U.S. Treasury bonds, of which there are many coming from all over the world presently, accept the fact that the dollar may go up or down. That's the value of what they hold. But, that is taken for granted in the United States, in a very transparent set of markets everyday with futures markets and indicators of which way the winds may be blowing.

Mr. SULLIVAN. Yes, sir.

The CHAIRMAN. It is a world of risk when it comes to current financial transactions involving currency quite apart from investments in real material—real estate.

Well, I thank you very much for your testimony and your forthcoming responses. Do you have any other comments that you want to make for the benefit of the record before we conclude our hearing?

Mr. SULLIVAN. I would like to make one comment and again, Mr. Chairman, it goes to some of the current events that are occurring in the region. You see what is a slightly troubling—not slightly—a troubling trend within the region with regard to expropriation and nationalization with certain countries. This kind of BIT, this kind of investment treaty is designed exactly to address these kinds of situations and therefore, although those kind of circumstances do not exist between the United States and Uruguay, it is important to recognize the broader intent of the Bilateral Investment Treaties and the importance both in terms of protecting investor rights, but also in terms of ensuring that when there are problems that we are seeing in other countries, that having a protection of this kind of treaty, is extremely valuable to both—primarily to the American investors, but also to the economies of the countries in which they're investing.

So, I would just like to conclude on that point, sir.

The CHAIRMAN. Well, it was an excellent point on which to conclude. I think we are all delighted to note the very fine visit by the distinguished President of Chile with our President last week and the reaffirmation of the strength of that relationship, which has been based upon the principles we have discussed today, and maybe even some beyond, and offers a source of influence in highlighting in South America at this point that the Uruguayan friendship certainly is another one in which we celebrate. We are hopeful we may be able to take action upon this treaty promptly.

I would ask that the record be kept open for the rest of today for other questions or testimony by members who were unable to attend and likewise, that as rapidly as possible you submit for the record the responses to questions that we have raised today and that you indicated your willingness to respond to.

Mr. SULLIVAN. Yes, sir.

The CHAIRMAN. Having said that, we appreciate your coming and the hearing is adjourned.

Mr. SULLIVAN. Thank you.

[Whereupon at 3:37 p.m., the hearing was adjourned.]

RESPONSES TO ADDITIONAL QUESTIONS SUBMITTED FOR THE RECORD TO ASSISTANT SECRETARY DANIEL SULLIVAN BY MEMBERS OF THE COMMITTEE

Responses to Questions Submitted by Chairman Lugar

Question. Article 24.1 of the U.S.-Uruguay BIT, Investor-State arbitration, with respect to breaches of "investment agreements" with a national authority is available "only if the subject matter of the claim and the claimed damages directly relate to the covered investment that was established or acquired, or sought to be established or acquired, in reliance on the relevant investment agreement." This provision diverges from the Model BIT. How will this affect the ability of investors to resolve disputes with national authorities?

Answer. The quoted language from Article 24.1 is the same as that found in the model BIT, and therefore does not represent a departure. The same language can also be found in our recent free trade agreement texts. This provision clarifies that for claims for breach of an investment agreement, the claimant must allege that both the subject matter of the claim and the alleged damages "directly relate" to the covered investment made in reliance on the relevant investment agreement. In other words, a claim for breach of an investment agreement can be made if the subject matter and damages relate to a covered investment (for example, a claim that failure to perform affected, and caused damages to, a covered investment, which depended on such performance), but not if they relate to aspects of the investment agreement that do not have a significant connection to the covered investment (for example, a claim for contract damages stemming from simple failure to perform pursuant to a specific term that was not a significant basis for the establishment or acquisition of the covered investment).

Question. There have been criticisms from the U.S. business community, who BITs are intended to protect, that the model and new direction of BIT negotiations are trending towards "defensive concerns" at the expense of the U.S. community investing overseas. Can you address this criticism, and if you find it to be inaccurate, please explain why.

Answer. We believe that the model BIT and the Uruguay BIT reflect long-standing U.S. policy of concluding investment treaties that provide meaningful, high-standard protections to U.S. investors. The Uruguay BIT adheres closely to the text of the model BIT, which was developed in close consultation with Congress, the business community, and other stakeholders. The model BIT includes strong provisions on the free transferability of funds, standards for expropriation and compensation consistent with U.S. legal principles and practice, national treatment and most favored nation treatment, limits on trade-distorting performance requirements, investor-state arbitration and other core protections. The model also contains clarifications of key substantive provisions, such as expropriation and the minimum standard of treatment, and new procedures to eliminate frivolous claims and make the arbitration process more efficient and transparent. In developing the model, we took account of our experience in defending claims against the United States under the investment chapter of the North American Free Trade Agreement. In addition, we took into account the negotiating objectives on investment contained in the Trade Promotion Authority Act of 2002, as our objective is to maintain consistency between our BITs and our free trade agreement investment chapters.

Question. Can you explain the relationship between the investment chapters of free trade agreements and BITs generally? How about specifically in terms of dispute resolution procedures? Will investors be able to determine without difficulty which dispute settlement procedures are available to them at any given point in time of their investment?

Answer. U.S. free trade agreements (FTAs) with investment chapters contain the same basic protections as U.S. bilateral investment treaties (BITs), and many of their core provisions use identical or nearly identical language. When we negotiate an FTA with a country with which we have a pre-existing BIT, we consider whether it is desirable to include an investment chapter to update our investment commitments to more closely reflect our present standards. We consider factors such as the level of investor protection afforded by the pre-existing BIT and the likelihood of successfully negotiating higher standards in a new FTA. We did not include an investment chapter in our FTA with Bahrain, with which we have a BIT, but we did include one in our FTA with Morocco, also a BIT partner, and in the Central American–Dominican Republic Free Trade Agreement, where we have a BIT in force with Honduras.

If there is a pre-existing BIT, and a new FTA that includes an investment chapter is negotiated, our practice has been to make the FTA effectively supersede the BIT. This is accomplished by the two Parties mutually agreeing to suspend dispute settlement under the BIT. A key exception to this suspension, however, is that BIT dispute settlement provisions continue to apply, for a period of 10 years, to covered investments and those BIT disputes that existed prior to the entry into force of the FTA. This exception ensures that investors who invested prior to the FTA continue to have access to dispute settlement under the BIT for 10 years after entry into force of the FTA. These investors have the choice of access to dispute settlement either under the BIT or the FTA during the 10-year period. Disputes arising after entry into force of the FTA involving investment made after the entry into force of the FTA may only be brought under the FTA. After the 10-year period, no dispute that arose before entry into force of the FTA may be taken to arbitration under the BIT or the FTA, and all disputes that arise after the 10-year period may only be brought under the FTA. These rules are described in the text of the Morocco FTA (Article 1.2(3)–(5)), and in an August 5, 2004 exchange of letters with Honduras, respectively. Both texts are available on the website of the Office of the U.S. Trade Representative.

Question. Article 5 of the 2004 Model revises the provisions for minimum standard of treatment. One of the specific criticisms of this alteration is that there is not a clear definition in international law for minimum standard treatment of aliens. Can you explain the thought process behind the revision of this provision and include your understanding of minimum standard of treatment of aliens?

Answer. In developing the 2004 model BIT, we sought to clarify that the obligation set forth in Article 5 prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments. In addition, Article 5 contains greater detail than prior models concerning "fair and equitable treatment" and "full protection and security," and provides that these concepts do not expand the Parties' obligations beyond those required under the customary international law minimum standard of treatment of aliens. These clarifications in part reflect our experience with international arbitration under Chapter 11 of the North American Free Trade Agreement (NAFTA). These clarifications also track the July 2001 interpretation of the NAFTA Free Trade Commission, which is comprised of the three government Parties to the NAFTA, regarding a similar Minimum Standard of Treatment article in the NAFTA. Customary international law, by definition, may evolve over time. Any attempt to provide more specificity on the customary international law minimum standard of treatment of aliens in the BIT text could risk denying investors the benefits of the protections provided by customary international law, as it may continue to evolve.

Question. Does Article 30, Governing Law, in effect, give the respondent state the ability to turn an investor-State case into a State-State case? If not, please explain why not.

Answer. Articles 30.1 and 30.2 specify the law a tribunal must apply to investor-State disputes. If the two government Parties seek to address an interpretive issue regarding a provision of the Treaty, they may do so in accordance with Article 30.3, which ensures that arbitral tribunals respect the intent of the two Parties that entered into the Treaty. It allows the Parties to issue a joint decision, binding on tribunals, expressing the Parties' interpretation of a provision of the BIT. By exercising this right, Parties to the BIT may, by their agreement, affect the way in which the treaty is interpreted by an investor-State tribunal. However, this does not change the nature of the dispute from one between an investor and a Party to the BIT. The fact that the Parties to the BIT do not issue a joint interpretation in a particular circumstance does not necessarily imply any disagreement with respect to the interpretation of the treaty that would suggest the possibility of a State-State dispute. It may simply reflect that the Parties see no need to clarify their interpretation of the text.

Responses to Questions Submitted by Ranking Member Biden

Question. You stated in your testimony that "by 2004, the United States had overtaken Mercosur as Uruguay's number one trading partner." According to the CIA publication "The World Factbook" (2005), in 2003 the United States was the third largest exporter to Uruguay, and the second largest market for products from Uruguay. What caused the significant expansion of trade between the United States and Uruguay in 2004? In what sectors, in particular, did this expansion occur?

Answer. In 2004, the United States became Uruguay's largest export market, followed by Brazil and Argentina. In 2005, Uruguayan exports to the United States grew further and almost reached total sales to Mercosur (the Southern Cone Common Market, consisting of Argentina, Brazil, Uruguay, and Paraguay, to which Venezuela has just been admitted as a full member). In 2005, Uruguay sold $760 million to the United States (22.4 percent of total exports), $781 million to Mercosur (22.9 percent) and $587 million to the EU (17 percent).

The surge in sales in recent years was led by rising exports of beef—Uruguay's traditional export—and gasoline. Although Uruguay is a net importer of crude oil, it has excess refining capacity and is a net exporter of gasoline. U.S. imports of petroleum products from Uruguay increased from none in 2003 to $97.5 million in 2005. Beef sales rose significantly beginning in 2003, when the United States reopened its beef market after Uruguay contained an outbreak of foot-and-mouth disease. In 2005, beef sales accounted for 60 percent of total exports to the United States, and gasoline sales 17 percent. U.S. exports to Uruguay—which consist mainly of high-tech goods like computers, radio/TV equipment, telecommunications equipment, and medical equipment—dropped significantly in 1998–2002 following a steep economic crisis, and resumed growth in 2003. U.S. exports rose 60 percent in 2003–2005.

Question. Are there any outstanding commercial disputes or expropriations claims involving the government of Uruguay (or an agency of that government) and U.S. firms? If so, please provide summary information about each dispute or claim, and the current status thereof.

Answer. We are not aware of any outstanding commercial disputes or expropriation claims between U.S. persons and the government of Uruguay or its agencies.

Question. Please provide a general summary of the investment climate in Uruguay for foreign direct investment, as well as a summary of the investment climate in Uruguay for U.S. firms.

Answer. The Government of Uruguay acknowledges the important role that foreign investment plays in economic development and works to maintain an open investment regime. Uruguay's 1998 Investment Law (no. 16906) declares that the promotion and protection of national and foreign investment is in the national interest. The law provides for national treatment, supports the establishment of foreign investment in country, and provides for the repatriation of capital and profits from investments. The law provides for 100 percent foreign ownership of investments, except where restricted for national security purposes. Uruguay maintains few restrictions on foreign investment and generally does not require that firms receive specific authorizations to invest.

Uruguay has a history of state monopolies in a number of areas, such as telecommunications and energy. However, in the past two decades the government has undertaken a privatization process to increase private sector participation in these areas. In the telecommunications sector, Uruguay maintains a monopoly on basic telephone services but has opened wireless services to private competition. The energy generation, petroleum, transportation, sanitation and financial services industries are all characterized by varying degrees of government involvement or monopolization, but are increasingly open to private investment.

U.S. firms have generally encountered few major obstacles to investing in Uruguay, but have noted difficulties with bureaucratic procedures and tenders, and with numerous changes in tax codes and regulations since 2001. The World Bank's "Doing Business" report, which ranks countries according to the quality of their investment climates, ranks Uruguay 85th globally and 9th regionally of 155 countries surveyed. The annual report of the U.S. Embassy in Montevideo concerning Uruguay's investment climate is available on the website of the U.S. State Department (http://www.state.gov/e/eb/ifd/2006/62048.htm).

Question. How does this treaty assist U.S. firms protect their intellectual property rights in Uruguay?

Answer. BITs comprise one element of our efforts to protect U.S. intellectual property rights abroad. Consistent with long-standing U.S. BIT practice, the treaty's definition of "investment" lists "intellectual property rights" as one of the forms that an investment may take. Thus, where an investor owns or controls an intellectual property right that is, or is part of, a covered investment, it is subject to BIT protections.

Question. The definition of "covered investment" in the 2004 model BIT, and in this treaty, provides that it applies to investments "in existence as of the date of entry into force of this Treaty or established, acquired, or expanded thereafter." This language is not contained in the 1994 model BIT. Is there a material difference between the language contained in this definition from the 1994 model and the 2004 model BIT?

Answer. The 1994 model BIT defines "covered investment" in Article I as "an investment of a national or company of a Party in the territory of the other Party." Article XVI, paragraph one, of the 1994 model provides that the BIT "shall apply to covered investments existing at the time of entry into force as well as to those established or acquired thereafter." The 2004 model BIT consolidates both concepts in the definition of "covered investment," which in substance is not a change from the 1994 model.

Question. Article 1 defines "investment" as an asset that "has the characteristics of an investment." What does that phrase mean? Is that not a tautology? Please provide examples of an asset owned by an investor that would not satisfy this requirement.

Answer. The forms that investment may take evolve over time, in response to changed economic and legal circumstances. For this reason, and consistent with long-standing U.S. BIT practice, the definition of "investment" is intentionally broad. The definition does, however, provide guidance on what constitutes an investment, notably by identifying certain "characteristics" of an investment, and setting out an illustrative list of forms that an investment may take. Additional elaboration is provided in several footnotes to the definition. Among other things, these footnotes set forth the types of debt that are less likely to have the characteristics of an investment; state that investments do not include claims to payment that are immediately due and result from the sale of goods or services, or orders or judgments entered in judicial or administrative actions; and provide that licenses, authorizations, permits, and similar instruments do not have the characteristics of an investment if they do not create any rights protected under domestic law. In general the definition provides more elaboration on the concept of "investment" than the prior 1994 model. At the same time, the definition is broad enough to encompass the evolving nature of investment throughout the life of the treaty.

Question. Article 21 contains several departures from the model BIT. Please explain the rationale for these departures, and the benefits to the United States that result.

Answer. Article 21 addresses the coverage of the BIT with respect to taxation measures. The principal departure from the U.S. model in this article is found in paragraph 2, and it is an area where the Uruguay treaty provides a higher level of investor protection than the model. This paragraph provides that the national treatment and most-favored-nation treatment obligations shall apply to all taxation measures, other than those relating to direct taxes (such as taxes on income, capital gains, and inheritances), and subject to other limitations. In other words, the Uruguay BIT provides protection against indirect taxation measures (such as excise or value-added taxes) that discriminate based upon nationality. We have included this provision in recent U.S. free trade agreements containing investment chapters and in the North American Free Trade Agreement, and we consider on a case-by-case basis whether to include it in individual BIT negotiations. In making the decision we consider factors such as U.S. investor interest in the protection and whether comparable provisions are contained in a tax convention between the United States and the other country. We do not presently have a tax convention with Uruguay.

Paragraphs 5 and 6 of Article 21 clarify the application of dispute settlement provisions to taxation measures alleged to be a breach of treaty obligations or an investment authorization or investment agreement. This is not a substantive change from the model, as the same substantive effect is achieved through paragraph 1 of Article 21 in the model. Our model BIT was not completed until after the Uruguay text was tabled and these paragraphs are intended to be consistent with our approach to this issue in the model.

Question. Annex F is a significant departure from the model BIT. Please explain the rationale for this departure, and the benefits to the United States that result.

Answer. A leading priority of Uruguay in the BIT negotiation was to ensure the government's ability to regulate financial services and financial institutions in appropriate ways consistent with the treaty. This is reflected in Annex F, which contains additional provisions on financial services.

The first two paragraphs of the annex clarify the shared understanding of the Parties concerning the relative standards of treatment to be compared in analyzing national treatment and most-favored-nation treatment with respect to financial institutions. Similar language is found in the financial services chapters of recent U.S. free trade agreements (FTAs) and the North American Free Trade Agreement (NAFTA). This language is intended to help ensure proper application of these obligations in the financial services sector. The United States agreed to this language because Uruguay requested it and it was consistent with our interpretation of the provisions in the text that it is intended to clarify.

Both the United States and Uruguay believed that State-State arbitration, rather than investor-State arbitration, should be the sole means of dispute settlement for claims relating to the treaty's national treatment or most-favored-nation treatment obligations for measures relating to financial institutions. This rule is reflected in paragraph 4 of the Annex. Language to the same effect is found in recent U.S. FTAs with investment and financial services chapters, as well as the NAFTA. This rule can help to prevent inappropriate claims of discrimination based on nationality in response to regulation in the financial sector, by vesting the decision of whether to submit a dispute in the hands of the investor's home country. The United States determines on a case-by-case basis whether such a provision should be tabled in individual BIT negotiations. In making this judgment we consider factors such as the U.S. investor interest, the nature of the other country's financial regulatory regime, the preference of our negotiating partner, the concerns of U.S. financial regulators, and whether investor-State arbitration is needed to protect the rights of U.S. investors in financial institutions of the other country. Even where the United States proposes this exclusion from investor-State arbitration for claims relating to U.S. measures in this sector, we allow for the possibility that our negotiating partner might choose to have investor-State arbitration apply to such claims for measures relating to its own financial institutions.

Finally, paragraph 5 of the annex clarifies that the treaty does not prevent a Party from taking measures relating to financial institutions that are necessary to secure compliance with laws or regulations that are not inconsistent with the Treaty, such as measures relating to the prevention of deceptive and fraudulent practices. This language, which was proposed by Uruguay, is also found in the financial services chapters of recent U.S. FTAs and is consistent with our interpretation of the relevant provisions in the text.

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