BG Pulse Journal USA
ISSN:1947-2536 http://www.bgpulseusa.com/index.php/bg

LEGAL LIMITS OF INCENTIVES GRANTED TO FOREIGN INVESTORS WITHIN THE FRAMEWORK OF WORLD TRADE ORGANIZATION RULES

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Abstract: The goal at completion of this paper is to examine how preferences provided by different countries to foreign investment have been limited by the governing principles of the World Trade Organization (WTO). This will be accomplished by looking in depth at permissible and prohibited types and forms of preferences as they apply to: National Treatment; Most Favored Nation Treatment; and Trade Related Investment Measures (TRIM). These areas of inquiry will include, but not be limited to: areas not explicitly regulated by WTO instruments; the legal ramifications associated with their use; and the importance of clarifying legal standards for evaluating preferences conferred upon foreign investors, ensuring that such preferences are compliant with WTO obligations.

Keywords: WTO law, preferences for foreign investors, national treatment principle, most-favored-nation treatment, TRIM Agreement, SCM Agreement, subsidies, prohibition of discrimination, legal restrictions.

Annotatsiya: Ushbu maqolada Jahon Savdo Tashkiloti (JST) me’yoriy tizimi doirasida xorijiy investorlarga beriladigan imtiyozlarning huquqiy chegaralari tahlil etiladi. Milliy rejim, eng ko‘p qulaylik beruvchi rejim va JST (Jahon Savdo Tashkiloti) doirasidagi savdo bilan bog‘liq investitsiya choralari (TRIMs) nuqtai nazaridan ruxsat etilgan va taqiqlangan imtiyoz shakllarining chegaralari aniqlanadi. Maqolada JST hujjatlarida to‘g‘ridan-to‘g‘ri tartibga solinmagan sohalar va ulardan foydalanishning huquqiy oqibatlari ko‘rib chiqiladi. Xulosa qilib aytganda, xorijiy investorlarga imtiyoz berishning JST talablariga muvofiqligini ta’minlash uchun aniq huquqiy mezonlar ishlab chiqish zarurligi asoslanadi.

Kalit so‘zlar: JST huquqi, xorijiy investitsiya imtiyozlari, milliy muomala tamoyili, eng qulay davlat rejimi, TRIMs Kelishuvi, SCM Kelishuvi, subsidiya, diskriminatsiya taqiqi, huquqiy chegara.

Аннотация. Целью данной работы является изучение того, каким образом преференции, предоставляемые различными странами иностранным инвестициям, были ограничены руководящими принципами Всемирной торговой организации (ВТО). Это будет достигнуто путем углубленного изучения допустимых и запрещенных видов и форм преференций в том виде, в каком они применяются к: Национальному режиму; режиму наибольшего благоприятствования; и инвестиционным мерам, связанным с торговлей (TRIM). Эти области исследования будут включать, но не ограничиваться ими: области, прямо не регулируемые документами ВТО; правовые последствия, связанные с их использованием; и важность уточнения правовых стандартов для оценки преференций, предоставляемых иностранным инвесторам, обеспечивая соответствие таких преференций обязательствам ВТО.

Ключевые слова: право ВТО, преференции для иностранных инвесторов, принцип национального режима, режим наибольшего благоприятствования, Соглашение по TRIM, Соглашение по SCM, субсидии, запрет дискриминации, правовые ограничения.

Although Member States of the World Trade Organization (WTO) retain sovereignty in formulating and implementing their economic policies, the commitments they have undertaken in the fields of international trade and investment significantly constrain the scope of their policy choices. The issue of incentives granted to foreign investors lies at one of the most contested points of these boundaries: on the one hand, States seek to establish preferential regimes in order to attract foreign capital; on the other hand, WTO rules regulate the scope and forms of such incentives.

The relevance of this issue stems from the fact that many developing countries, including Uzbekistan, introduce various incentive schemes in the course of acceding to the WTO or consolidating their membership, with a view to improving the foreign investment environment. However, not all forms of such incentives are necessarily compatible with WTO law. From an academic perspective, clearly delineating the boundary between permissible and prohibited forms of incentives is of considerable importance for legal practice [1].

The purpose of this article is to identify the legal limits of incentives granted to foreign investors through a systematic analysis of the WTO regulatory framework and to classify these limits on the basis of clearly defined criteria.

The National Treatment Principle and Incentives

Article III of GATT 1994 and Article XVII of GATS establish the national treatment principle, under which WTO Members must not accord imported products and services treatment less favorable than that accorded to like domestic products and services. The same principle applies in the context of foreign investment: where a State grants certain incentives to domestic investors, foreign investors should be provided with at least equivalent conditions and incentives. In other words, a State may extend to domestic investors the incentives granted to foreign investors without violating the national treatment principle. However, if a State grants incentives exclusively to foreign investors while denying domestic investors access to those incentives, such a policy may result in de facto discrimination and may be inconsistent with WTO rules [2].

The practice of the *WTO Dispute Settlement Body (DSB)* demonstrates that the mere existence of a formal distinction is not, in itself, sufficient to establish a violation of the national treatment principle. The relevant criteria include whether the products or services are “like” and whether there is an actual competitive relationship between them. Accordingly, when assessing incentives designed for foreign investors, these criteria should be examined separately and carefully.

Most-Favoured-Nation (MFN) Treatment and Incentives

It is well established that many Bilateral Investment Treaties (BITs) grant foreign investors Most-Favoured-Nation (MFN) treatment vis-à-vis the host State. This may enable an investor to claim more favorable conditions granted by the host State to investors from third countries.

Within the WTO framework, however, a key limitation of the MFN principle is that it primarily governs “tariff preferences” and does not directly apply to capital flows or investment incentives. Furthermore, under *Article XXIV of GATT 1994 and Article V of GATS*, members of free trade areas may grant preferential treatment to one another that would otherwise be inconsistent

with the MFN principle. This, in turn, may create opportunities for *"forum shopping"* in the investment sphere [2].

Regulation of Incentives under the TRIMs Agreement

The *TRIMs Agreement (1994)* prohibits trade-related investment measures that are inconsistent with *Articles III and XI of GATT 1994*. The Illustrative List annexed to the Agreement identifies the following measures as inconsistent with *Article III of GATT 1994*: local content requirements that compel investors to purchase or use a specified amount or value of locally produced goods, as well as trade-balancing requirements that restrict the volume of imports to an amount corresponding to the quantity of local products sold by the investor [3].

Although *Article 5 of the Agreement* provides developing countries with transitional arrangements, these flexibilities have, by now, become largely inapplicable. Nevertheless, in practice, WTO Members frequently incorporate into their investment legislation "hidden" *performance requirements* that are not directly inconsistent with the TRIMs requirements but may produce similar effects. In such cases, each measure is assessed individually in WTO dispute settlement proceedings.

A crucial methodological distinction should be noted here: the TRIMs Agreement regulates trade-related measures rather than investment incentives as such. Accordingly, if a State grants a foreign investor a tax incentive—for example, an exemption from income tax—such a measure does not, in itself, fall within the scope of the TRIMs Agreement; rather, it may fall within the regulatory scope of the *SCM Agreement*.

The SCM Agreement and the Limits of Investment Subsidies

The Agreement on Subsidies and Countervailing Measures (SCM Agreement) distinguishes among three categories of subsidies: *prohibited (red), actionable (yellow), and non-actionable (green) subsidies.* Whether incentives granted to foreign investors constitute "subsidies" within the meaning of the WTO SCM Agreement remains a matter of ongoing legal debate.

Under *Article 1.1 of the SCM Agreement*, two principal conditions must be satisfied for a subsidy to exist: (1) a financial contribution by a government or the foregoing of government revenue, and (2) a benefit conferred as a result of such contribution or revenue foregone. Tax incentives may therefore be characterized as the "foregoing of government revenue." However, whether an incentive granted *"exclusively to foreign investors"* satisfies the criterion of "specificity" under the SCM Agreement raises a separate and important legal question [4].

The practical significance of this issue lies in the fact that many States justify investment incentives as part of their policy to "improve the investment climate" and emphasize that such incentives are available to all foreign investors. Accordingly, they generally argue that the specificity requirement has not been satisfied. However, where incentives are limited to a particular sector or region, the likelihood that such a measure will be characterized as a specific subsidy increases substantially under *Article 2 of the WTO SCM Agreement*.

Legal Gaps and the Limits of Their Exploitation

The WTO regulatory framework contains a number of "gaps," manifested in the lack of sufficient clarity in regulating incentive policies relating to foreign investment. First, GATS regulates only trade in services, while there is no separate WTO agreement specifically governing

investment flows as such. This area is therefore regulated primarily through Bilateral Investment Treaties (BITs) and investment chapters of free trade agreements. Second, investment incentives in the fields of the digital economy and electronic commerce have not yet been fully and comprehensively regulated within the WTO framework [5].

Accordingly, States may exploit these gaps by implementing incentive policies that are formally consistent with WTO rules but have substantively protectionist effects. This phenomenon has been specifically recognized by scholars as the problem of "shell norms" in WTO law.

Conclusion

The analysis demonstrates that although the legal limits of incentives granted to foreign investors are established through several WTO agreements, including *GATT, GATS, TRIMs, and the SCM Agreement*, the coordination and interaction among these agreements have not yet been fully developed. In designing and implementing permissible forms of incentives, States should strictly adhere to the following key criteria: refrain from violating the national treatment principle; avoid unjustified reliance on exceptions to the MFN principle; refrain from adopting measures prohibited under the TRIMs Agreement; and avoid measures that may be characterized as *"prohibited subsidies"* under the WTO SCM Agreement.

At the same time, addressing the existing legal gaps—particularly through the development of a separate multilateral agreement on investment within the WTO framework—remains one of the pressing issues in contemporary international legal scholarship and practice. For countries in the process of WTO accession, such as Uzbekistan, a thorough understanding of these legal limits and the alignment of national incentive policies with them are of paramount importance.

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