

Mr. Lukas Siegenthaler
Head of Division International Investments
and Multinational Enterprises State
Secretariat for Economic Affairs SECO
Holzikofenweg 36
3003 Bern

By e-mail: lukas.siegenthaler@seco.admin.ch

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Consultation: Bilateral agreement between Switzerland and Indonesia on the promotion and protection of investments

Dear Mr. Siegenthaler, Ladies and Gentlemen

SwissHoldings is a cross-sector business association and currently represents 61 Swiss corporations in the industrial and service sectors (excluding the financial and insurance sectors). Our members are major issuers on the capital market; they account for around 66 percent of total Swiss stock market capitalization (as of March 31, 2022).

We were invited to comment on the consultation opened on June 3, 2022. We would like to thank you for this opportunity and are pleased to accept it.

Summary of the position and concerns of the association

- **Direct investments are central for Switzerland:** The prosperity of the population and the competitiveness of companies in the small and open Swiss economy depend directly on integration into global value chains.
- **Investment promotion and protection treaties are of essential importance:** For companies, foreign investments are not only associated with economic risks, but also with political risks. This makes treaties between states to protect and promote foreign investment all the more important.
- **Effective investment protection requires an investor-state arbitration mechanism:** Investor-state dispute settlement procedures have proven their worth both for Switzerland and for Swiss companies. They build on existing international structures (ICSID, UNCITRAL) and enable disputes to be resolved in a relatively timely, fact-oriented and politically independent manner.
- **The design of investment protection has been steadily developed in recent years:** The system of investment jurisdiction has been steadily developed in recent years - especially with regard to legal certainty and protection against their



misuse. The association has always supported the corresponding work for the further development of the system.

- **SwissHoldings supports the present investment protection agreement with Indonesia:** the content of the agreement meets current standards and closes a critical gap in the agreement that arose when Indonesia terminated all bilateral investment protection agreements in 2014. In combination with the free trade agreement between the EFTA states and Indonesia, which enters into force in 2021, the investment protection agreement is expected to significantly strengthen the trade and investment dynamics of Swiss companies in Indonesia in the medium and long term.

1. Direct Investment is Central for Switzerland

Switzerland's prosperity is based on the openness of its markets and the international interconnection of production, supply and research networks. As an open economy with a small domestic market, Switzerland is forced to seek growth outside its borders. Investments abroad are therefore a key instrument for Swiss companies to successfully hold their own in international competition. This is the only way to achieve economies of scale compared to foreign competitors and to ensure the necessary productivity.

In the case of foreign investments, the search for lower-cost locations is generally less important than the development of new sales markets. The establishment of a distribution network or a joint venture with a local company makes it easier to gain a foothold in a market. Moreover, many exports from Switzerland first go to the company's own branches abroad before they are processed and sold later. Moreover, when a company's sales increase worldwide, this often leads to an expansion of activities in the home base as well. This in turn leads to an increase in value-added jobs at the company's headquarters (e.g. research, development, sophisticated production processes). Specifically, one in five jobs in Switzerland is accounted for by companies with direct investments abroad. The international presence of a company also promotes the global exchange of know-how and technology and reduces dependence on economic developments in the individual regions.

According to OECD figures, Switzerland ranked eighth among the world's largest direct investors in 2021 with a total of USD 1,456 billion. Measured as a share of GDP, it even ranks 4th (179% of GDP). The number of Swiss companies invested abroad (over 19,000) and the number of people employed there (over 2 million) is also impressive. In 2020, more than CHF 77 billion in investment income flowed back into Switzerland from the operating activities of these companies (around 11% of GDP). In addition, there are substantial direct and indirect tax revenues from companies with direct investments each year. This takes the form of taxes on profits at the federal, cantonal and municipal levels, stamp duties, withholding tax, value-added tax, and income and wealth taxes on employees.

With regard to Indonesia, the figures concerning the investment activity of Swiss companies are also impressive. Together with Japan, Singapore and China, the country is one of the most important recipients of Swiss direct investment in Asia. The capital stock of Swiss direct investment in



Indonesia amounted to around 2.1 billion Swiss francs in 2020. The number of jobs created by Swiss companies in Indonesia was 17,000 in 2020.

2. Investment promotion and investment protection agreements are of essential importance

There are often considerable economic and political risks associated with foreign investments in international markets. While there are now many technical tools to classify economic risks such as currency developments, political risk remains difficult to calculate. Such political risk exists, for example, when a host state fails to abide by contractual agreements. In addition, more "subtle" forms of obstruction can also be observed. For example, investing companies report that they have not been treated in the same way as local competitors in the context of supervisory and control activities or in tax collection by the host state.

It goes without saying that an investor has to bear the economic or entrepreneurial risks himself. However, there are various instruments which, in the interest of investors and nation states, guarantee a limited hedging of political risks and thus create planning security and facilitate long-term stable economic relations. On the one hand, this applies to the investing company, which can often only amortize its expenses over a longer period of time. On the other hand, the host country would also like to attract foreign investors with a long-term orientation in order to enable sustainable economic development.

As an important country of origin for international investments, it is therefore also in Switzerland's interest to create favorable framework conditions for the foreign activities of its companies and to offer them effective legal protection. This is the aim of so-called protective provisions for direct investments, as agreed in bilateral investment protection agreements (ISA). They are a central instrument of Swiss foreign economic policy and create legal certainty in the following areas in particular:

- Prohibition of discrimination: A foreign investor may not be treated worse than a domestic investor (*national treatment*). In addition, a foreign investor may not be treated worse than investors from other countries of origin (*most favored nation treatment*).
- Protection against arbitrary expropriation: *Direct* or indirect *expropriation* - for example, forced nationalization.
- Protection against unjust and inequitable treatment: the principle of just and equitable *Fair and equitable treatment* is violated, among other things, if the investor is denied national legal recourse or the right to be heard, if he is put under political pressure or treated arbitrarily.
- Free capital transfer: This ensures that the investor can, for example, generate profits from of the investment or compensation payments in the course of expropriation can be transferred to its home country.

Another central principle within the framework of ISA is the "*right to re- gulate*" of the respective contracting states. Accordingly, a state may adopt laws and regulations to protect the general welfare in the areas of health, safety, or environmental and social protection.



labor standards - as long as the principles of non-discrimination and proportionality are not affected. In any case, arbitral tribunals cannot invalidate legal measures taken by the state, but can award damages to the investor.

3. Effective Protection Requires Investor-State Arbitration Mechanism

An important element of the ISAs are also provisions on dispute resolution. Switzerland's ISAs usually provide that in a dispute, the investor can choose between the national legal process in the host state and investor-state arbitration. The investor's direct right of action against the host state avoids the need for the investor's home state to take action against the host state under diplomatic protection in the event of a dispute. Moreover, access to international arbitration provides investors with additional legal protection, for example, if the independence and efficiency of national courts in the host state are not given. The basis for investor-state arbitration is provided by the ICSID Convention concluded under the auspices of the World Bank and the Arbitration Rules of the UN Commission on International Trade Law (UNCITRAL). They provide comprehensive guidelines for the structure and composition of the arbitral tribunals, the course of the arbitration proceedings and the enforcement of the judgments.

In addition to its importance for Swiss companies abroad, the dense Swiss investment protection network is also an important locational advantage for international investors who wish to establish themselves in Switzerland and conduct parts of their business activities from here. Switzerland currently has 124 ISAs in force. According to UNCTAD, Switzerland thus has the third largest network of such agreements in the world, after Germany and China. Worldwide, 2219 ISAs are currently in force.

4. The structure of investment protection has been steadily developed in recent years.

In recent years, there have been intensive discussions worldwide about the further development of investment protection and promotion treaties. Efforts have focused, among other things, on improving transparency in ISDS procedures, for example by publishing documents that allow insight into the negotiations. The work also focused on defining legal concepts and definitions more precisely.

Switzerland has also continuously developed its treaty practice based on these international developments. In 2012, for example, elements were introduced to achieve greater coherence of the system with the Sustainable Development Goals. Two years later, Switzerland also improved transparency in investor-state arbitration by implementing the new UN rules (UNCITRAL Rules). These rules provide that the public is generally informed about the course of the arbitration proceedings. In addition, third parties have the possibility to submit written procedural submissions (amicus curiae briefs).

At the beginning of 2015, SECO again reviewed Swiss ISA contract practice. In the course of this work, important protection standards such as "fair and equitable treatment" and "disqualification" were defined more precisely. In particular, the standard "fair and equitable treatment" had previously been formulated in (too) general terms, also in an international context, which led to extensive jurisprudence by arbitral tribunals over the past 15 years. Newly clarified were



Procedural issues such as the application of time limits (for example, the time limit for initiating proceedings) or costs (allocation of procedural costs, etc.).

The investment protection system is to be further adapted in the future in order to improve its functioning and to strengthen the international acceptance of the ISA. Switzerland relies primarily on multilateral processes, which are the best way to develop broad-based solutions.

5. The present investment protection agreement with Indonesia is welcomed

Indonesia's decision in 2014 to terminate all bilateral investment protection agreements has clearly weakened legal certainty in the face of political risks for Swiss investors on the ground. This should be viewed critically, both in view of Indonesia's growing economic importance and against the backdrop of Indonesia's high significance for Swiss direct investments in Asia.

In view of the free trade agreement between the EFTA states and Indonesia, which comes into force in 2021, it is all the more welcome that Switzerland has succeeded in closing this gap in the agreement quickly and in the interests of the economy, and in strengthening legal certainty for Swiss investors on the ground. It can be expected that both agreements will significantly strengthen the trade and investment dynamics of Swiss companies in Indonesia in the medium and long term. In addition, they can also create equivalent competitive conditions with other important contracting states in Indonesia.

At the same time, however, this is also the first time that the Federal Council - based on its decision of 22 June 2016 - has made a standard agreement subject to an optional referendum and accordingly conducted a public consultation.

From the point of view of the business community, the following comments should also be made on the present text of the agreement:

- The fact that the agreement also refers in particular to the importance of foreign investment for sustainable development and also assigns companies an important responsibility in this regard is to be welcomed.
- The fact that the scope of the agreement does not apply to disputes arising before its entry into force is in line with standard practice. However, for disputes that arose after the termination of the previous ISA but before that date, the new agreement is not able to provide additional remedies and certainty.
- The protective provisions provided are in line with current standards (see also Chapter 3). The additional specification of the areas of protection is particularly welcome.
- The right to regulate enshrined in the agreement keeps the political shaping of the agreement maintains both countries' room for maneuver in sensitive areas (e.g. health, safety, environmental protection) and is recognized by the business community. At the same time, however, it is essential that there is no discrimination between domestic and foreign companies, that the applicable procedural rules are complied with and that implementation is provided for with sufficient time limits for the players concerned.



- Investor-state arbitration is an important instrument for Swiss companies abroad. It provides investors with a minimum of legal and planning certainty, which they need for their investments. The agreement rightly refers to the internationally recognized and established principles of ICSID and UNCITRAL and additionally sets out important procedural provisions directly in the agreement. The procedure allows for a relatively timely, transparent, fact-oriented and politically independent resolution of disputes. It is to be welcomed that the obligation to exhaust the national legal channels of the host country beforehand has been waived, while at the same time multiple claims are prohibited.

Thank you for your consideration and consideration of our concerns. Please do not hesitate to contact us if you have any questions.

Kind regards

SwissHoldings
Office

A handwritten signature in black ink, appearing to be "Denise Laufer".A handwritten signature in black ink, appearing to be "Gabriel Rumo".

Gabriel Rumo
Denise Laufer
Director
Member of the Executive Board

