



CEFTA ISSUES PAPER 2

National Treatment Restrictions and Review of Bilateral Investment Treaties



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FOREWORD

As we approach the fourth year of implementation of the CEFTA 2006, the challenge for the parties to the agreement is to ensure full implementation of all commitments. These commitments are important as they provide us with a means of strengthening our economic ties through greater regional trade and investment integration. Our shared goals are EU accession, sustainable long-term economic growth and improved living standards – CEFTA 2006 is a key instrument by which we can attain those goals.

The investment-related clauses of CEFTA 2006 are a novel feature of the trade agreement. The Parties recognised that without providing non-discriminatory treatment to investments from other Parties, coordinating our investment policies as much as possible, protecting intellectual property rights and opening our government procurement markets the benefits of closer trade ties would only be partially realised.

As CEFTA chair for 2010, Serbia welcomes the series of publications produced by the OECD Investment Compact for South East Europe on monitoring the implementation of the investment-related clauses in CEFTA 2006. The analysis contained in these series of papers will help the CEFTA Parties understand where progress has been made and where more work needs to be done. These publications would not have been possible without the financial support of the European Commission.

Closer cooperation between the CEFTA institutions, the European Commission and organisations such as the OECD Investment Compact ensure that the benefits of CEFTA 2006 reach their maximum potential.



Bojana Todorovic
Assistant Minister
Ministry of Economy and Regional Development
Republic of Serbia

INTRODUCTION

The Central European Free Trade Agreement (CEFTA) 2006 represents a significant accomplishment for the economies of the Western Balkans along the path to EU accession. By focussing on greater economic integration through trade and investment, the parties recognise that the CEFTA 2006 is an important stepping stone to sustainable long-term growth and improved standards of living.

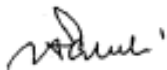
In addition to implementing traditional trade-related liberalisations such as tariff reductions, the CEFTA 2006 obligates the parties to undertake commitments related to investment policy. The investment-related clauses provide for non-discriminatory treatment of investments underpinned by the principle of national treatment, a commitment by the parties to broadly co-ordinate their investment policies, progressive opening of their government procurement markets, and effective protection of intellectual property rights (IPRs).

In an effort to monitor implementation of investment-related clauses, the CEFTA parties have mandated the CEFTA Secretariat to periodically review these commitments. With the financial support of the European Commission (EC), the CEFTA Secretariat requested the Organisation for Economic Co-operation and Development's Investment Compact for South East Europe (OECD-IC) to assist in this effort.

This publication is part of a series produced by the OECD-IC in the framework of this EC-funded exercise to monitor the implementation of the investment related clauses of CEFTA 2006. It presents an update of the restrictions to national treatment that exist in the CEFTA 2006 parties. In addition, the report reviews the consistency of bilateral investment treaties signed amongst the CEFTA 2006 parties. The results of this report were presented by the OECD-IC during on 27 October 2009 during CEFTA week organised by the government of Montenegro.

The other papers in the series include a review of the IPR legal frameworks found in the CEFTA 2006 parties and an econometric analysis on industry location and the determinants of foreign direct investment in the original CEFTA parties. The views expressed in these publications are those of the OECD-IC and do not reflect the official position of CEFTA institutions or CEFTA parties themselves.

The continued co-operation between the CEFTA institutions and the OECD-IC to monitor the investment-related clauses of the CEFTA 2006 is an example of the type of collaboration necessary to ensure maximum benefits from closer trade and investment integration across the Western Balkans.



Antonio Fanelli
Deputy Head
Private Sector Development Division
Organisation for Economic Co-operation and Development



Renata Vitez
Director
CEFTA Secretariat

ACKNOWLEDGEMENTS

The OECD Investment Compact would like to thank all the CEFTA contact points and stakeholders who participated in workshops on the investment-related clauses during CEFTA week in Podgorica, Montenegro between 27-28 October 2009.

Antonio Fanelli, from the OECD IC, has had overall management responsibility for the series of working papers on the implementation of the investment-related clauses of the CEFTA. The working paper on national treatment restrictions and review of bilateral investment treaties was prepared by Milan Konopek from OECD-IC, and Lotte Van Mechelen from OECD-IC provided vital research assistance.

The OECD-IC will continue providing input into the implementation of the CEFTA 2006 and step up debate of the benefits of regional trade integration in the broader framework of European economic integration.

The views expressed in this publication are of the OECD-IC and do not reflect the official position of the CEFTA institutions or any of the CEFTA parties.

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EXECUTIVE SUMMARY

These working papers cover two important aspects of the investment-related clauses in the CEFTA 2006: restrictions to national treatment and the consistency of bilateral investment treaties (BITs) signed among the CEFTA parties themselves.

Restrictions to National Treatment

The CEFTA parties have taken steps to modify or reduce restrictions to national treatment in their primary or secondary legislation covering foreign investment and certain sector-specific laws. No evidence was found to suggest that a CEFTA party was trying to reverse reforms or impose new restrictions to national treatment.

The majority of CEFTA parties refrain from using trans-sectoral screening procedures for foreign investment. In almost all cases, foreign-controlled enterprises are required to notify their entry in the host economy by registering in local commercial courts (*e.g.*, Bosnia and Herzegovina, Croatia, the former Yugoslav Republic of Macedonia, Montenegro, and Serbia). The Republic of Moldova, however, does use screening mechanisms for competition policy purposes. Moldovan authorities indicate that this screening mechanism is applied on a non-discriminatory basis.

For sectors covered by separate legislative frameworks, screening mechanisms do exist, for example, in areas such as air and maritime transport, banking, financial services, and fishing. The presence of numerous foreign providers involved in banking and telecommunications services in the CEFTA parties contributes to reducing restrictions to national treatment in these sectors. In particular, modifications to laws and regulations covering insurance services were noted in Bosnia and Herzegovina, Croatia, the former Yugoslav Republic of Macedonia, Montenegro, and Serbia.

The most prominent types of restrictions to national treatment include the following:

- 49% foreign ownership limitation in industries and sectors related to arms manufacturing, trading, and production (*e.g.*, Bosnia and Herzegovina, the former Yugoslav Republic of Macedonia, Montenegro, Serbia and UNMIK-Kosovo¹);
- foreign ownership of agricultural land (nearly all CEFTA parties);

¹ Throughout the paper “UNMIK-Kosovo” refers to “the United Nations Interim Administration Mission in Kosovo on behalf of Kosovo in accordance with United Nations Security Council Resolution 1244.”

- restrictions on the purchase of real estate in sensitive areas such as border zones, national parks, and historical areas (all CEFTA parties);
- restrictions on maritime transport services (*e.g.*, Albania, Croatia, Montenegro, and Serbia) air transport (*e.g.*, Bosnia and Herzegovina, Croatia, and Serbia) and fishing (*e.g.*, Albania, Croatia, and Montenegro).

Consistency of Bilateral Investment Treaties

The BITs identified in Annex 6² of the CEFTA 2006 are broadly consistent in terms of the treatment and protection they provide to investors and their investments. The majority of these BITs use similar definitions for terms such as “investment,” “investor,” and “returns.”

Nearly all of the BITs reviewed include provisions on “fair and equitable” treatment providing “full security and protection.” In terms of relative standards of treatment, most favoured nation (MFN) treatment at the post-establishment phase of investment is included in all of the BITs. Only the Croatia-former Yugoslav Republic of Macedonia (1995) BIT excludes national treatment at the post-establishment phase of investment.

The BITs in Annex 6 provide for: compensation against expropriation; rights to transfer capital and returns; subrogation; and dispute settlement mechanisms at the state-to-state and investor-to-state level. Provisions on expropriation are formulated in a similar manner. However, the approaches regarding calculation of interest on compensation payments differ among some treaties. For example, three treaties refer to an interest rate calculated on an “annual LIBOR basis,” while six others refer to interest rates calculated according to “normal commercial rates.”

Furthermore, the BITs in Annex 6 typically include transparency-related provisions on consultations. In most BITs, the contracting parties agree to hold consultations at the request of either party on matters related to the application and interpretation of the agreement. A novel feature found in BITs signed by Bosnia and Herzegovina-former Yugoslav Republic of Macedonia (2002), Bosnia and Herzegovina-Republic of Moldova (2003), Bosnia and Herzegovina-Yugoslavia (2004), and Croatia-former Yugoslav Republic of Macedonia (1995) are clauses specifying an additional consultation mechanism for exchanges of extra information on the impact of laws, regulations, decisions, administrative practices, or procedures or policies.

The majority of BITs in Annex 6 apply to investments made after the entry into force of the treaties. However, Albania-Croatia (1994), Albania-Republic of Moldova (2004) and Croatia-Republic of Moldova (2001) differ as these treaties also cover investments made prior to entry into force.

² The BITs in Annex 6 which were reviewed exclude those concluded with Romania and Bulgaria. In addition, only BITs where English copies existed were reviewed. English versions of the following BITs were not available for this review: Albania-former Yugoslav Republic of Macedonia, Bosnia and Herzegovina-Croatia (along with Protocol), and Croatia-Republic of Moldova.

NATIONAL TREATMENT RESTRICTIONS IN PARTIES TO THE CEFTA 2006

This working paper reviews existing restrictions to national treatment found in parties to the CEFTA 2006. The review covers restrictions to national treatment such as approval and licensing/screening procedures, equity and other discriminatory measures on establishment, corporate organisation, and transparency measures.

INTRODUCTION

National treatment is the commitment of a country to accord to foreign investors and to foreign-controlled enterprises in its territory treatment no less favourable than that accorded in similar situations to domestic enterprises. In OECD countries, the principle of national treatment is a cornerstone of instruments such as the OECD Declaration and Decisions on International Investment and Multinational Enterprises and the Code of Liberalisation of Capital Movements.

In the CEFTA 2006, national treatment is captured by Article 32(2) which commits the parties to apply it at the pre- and post-establishment phases of investment. In addition, Article 32(3) commits the CEFTA parties not to adopt any new discriminatory regulations or measures against companies from any of the other parties.

This working paper reviews the status of existing restrictions to national treatment identified in a previous 2003 Investment Compact study.³ Between August and September 2009, Albania, Bosnia and Herzegovina, Croatia, the former Yugoslav Republic of Macedonia, Republic of Moldova, Montenegro, and Serbia were invited to update the status of those restrictions to national treatment identified in 2003.⁴ A summary of restrictions (including modifications) to national treatment is found in Table 1. It should be noted that the restrictions to national treatment compiled in this paper are only indicative and do not represent an exhaustive review.

Table 1. Summary of restrictions to national treatment

Measures	Albania	Bosnia and Herzegovina	Croatia	Former Yugoslav Republic of Macedonia	Republic of Moldova	Montenegro	Serbia	Kosovo (UNMIK)
1. Investment by foreign investors and by established foreign-controlled enterprises								
1.1. Approval and licensing/screening procedures								N/A

³ OECD (2003), National Treatment of International Investment in South East European Countries: Measures Providing Exceptions. Kosovo (UNMIK) was not included in the 2003 review.

⁴ Information gathered for the OECD Investment Compact's Investment Reform Index 2010 was used to assess restrictions to national treatment in Kosovo (UNMIK).

Measures	Albania	Bosnia and Herzegovina	Croatia	Former Yugoslav Republic of Macedonia	Republic of Moldova	Montenegro	Serbia	Kosovo (UNMIK)
Trans-sectoral		x		x	x	x		N/A
Banking	x						x	N/A
Insurance	x	x						N/A
Security market and other financial services			x					N/A
Air transport		x					x	N/A
Maritime transport							x	N/A
Mining and quarrying								N/A
Fishing						x		N/A
1.2 Equity and other discriminatory measures on establishment								N/A
Trans-sectoral		x	x		x	x	x	N/A
Banking			x				x	N/A
Insurance		x	x	x		x	x	N/A
Telecommunications			x					N/A
Air transport			x					N/A
Maritime transport	x		x				x	N/A
Fishing	x		x					N/A
Trade		x					x	N/A
Other sectors		x	x	x		x	x	N/A
Real estate	x	x	x	x	x	x		N/A
1.3 Corporate organisation								N/A
Trans-sectoral	x	x			x			N/A
Maritime transport						x		N/A
Other sectors								N/A
2. Transparency measures								N/A

Measures	Albania	Bosnia and Herzegovina	Croatia	Former Yugoslav Republic of Macedonia	Republic of Moldova	Montenegro	Serbia	Kosovo (UNMIK)
2.1 Security considerations								N/A
Approval		x						N/A
General/equity restriction		x		x	x	x	x	x
Location restriction		x	x			x	x	x
2.2 Nationality of management								N/A
Banking	x							N/A
Energy					x			N/A
Other sectors								N/A
LEGEND	Modified since 2003				Not modified			

To be consistent with the approach in the 2003 report, similar terms are used in this working paper. These include:

- *foreign investors* are defined as legal entities of one country (investing or home country) investing in another country (host country);
- *established foreign-controlled enterprises* are enterprises which operate in the territory of a particular country and are owned or controlled directly or indirectly by nationals of other countries;
- *restrictions or exceptions* concern measures that do not conform to the national treatment principle because they treat foreign controlled-enterprises differently, *i.e.*, less favourably, than their domestic counterparts in like situations. Measures which qualify as exceptions include restrictions banning foreign investment in certain sectors or requiring authorisation or licensing as prerequisites for investment, setting ceilings on foreign ownership, etc.

Furthermore, the working paper is limited to restrictions to national treatment on the following:

1. Investment by foreign investors and by established foreign-controlled enterprises, with measures related to:

- (i) approval and licensing/screening procedures;
- (ii) equity and other discriminatory measures on establishment and/or expansion; and

(iii) corporate organisation.

2. *Transparency measures* which concern measures that discriminate against foreign-controlled enterprises but are motivated by reasons of public order and essential security interests. The working paper will also include other means that do not discriminate against foreign-controlled enterprises, but nevertheless represent an impediment to foreign investment. Transparency measures are classified into the following:

(i) security considerations, which relate to approvals, general/equity restrictions, location restrictions, etc.; and

(ii) nationality of management.

SUMMARY OF RESPONSES BY THE CEFTA 2006 PARTIES

Albania

Approval and licensing/screening procedures: Albania does not maintain trans-sectoral screening or approval procedures for foreign investment.

Approval and licensing procedures are applied on a sector-specific basis for foreign investors investing in banking and insurance activities. The authorisation procedures which existed in 2003 have been confirmed by Albanian authorities for this review. Foreign banks intending to own qualified holdings in a domestic bank must be authorised by the respective authorities to carry out acceptance and collection deposits in money or other repayable funds in the foreign country where its legal seat is located, prior to obtaining a license from Albanian authorities (Law 9662/2006). Likewise, the conditions necessary for foreign companies to obtain authorisation from the Albanian Financial Supervisory Authority to perform insurance activities in Albania have not changed since the 2003 review (confirmed by Albanian authorities and Law 9267/2004).

With respect to issuing licenses for health care professionals, Albania has abrogated a previous requirement that foreigners interested in establishing a practice had to co-operate with an Albanian professional.

Equity and other discriminatory measures on establishment: Albania does not maintain discriminatory equity restrictions or other measures on establishment on a trans-sectoral basis.

A modification has been made with respect to maritime transport activity. Albanian authorities have indicated that local and foreign ships must fly the Albanian flag to exercise cabotage services and that licensing procedures are the same for both. In the previous review, only Albanian ships carrying the Albanian flag were permitted to conduct cabotage activity. Albanian authorities have confirmed that a prohibition on foreign vessels applying for demersal fishing with trawls and collection of bivalve molluscs exists.

With respect to real estate, foreign investors are still required to prove that the value of their intended investment must be three times higher than the value of state-owned non-agricultural land they intend to purchase. However, Albania's obligations deriving from its Stabilisation and Association Agreement (SAA) with the EU will require that seven years after its entry into force, EU citizens will have equal treatment as Albanian nationals to purchase immovable property.

Corporate organisation: Albania has indicated that previous discriminatory registration fees based on shareholder nationality no longer exist. In the operation of the National Centre for Registration, the fee for all shareholders is 1 Euro.

Transparency measures: Albania no longer requires that a foreign bank employ at least two resident administrators in the branch of a foreign bank.

Bosnia and Herzegovina

Approval and licensing/screening procedures: Bosnia and Herzegovina does not maintain a trans-sectoral approval or screening procedure. Foreign-controlled enterprises are, however, required to register at local courts.

In the insurance sector, laws in the entities (Law 24/05 in the Federation and Law 17/05 in the Republika Srpska) have been modified to permit unrestricted levels of foreign ownership in companies providing insurance.

In the air transport sector, foreign companies are required to register for air operators. In order to be registered, certain technical criteria must be met and verified by the Directorate for Civil Aviation.

Equity and other discriminatory measures on establishment: Foreign-controlled enterprises are restricted to a limit of 49% equity holdings in sectors related to the production and sale of arms, ammunition and explosives for military use, military equipment and public information. Foreign investors must receive prior approval from the competent body of the respective entity to invest in the mentioned sectors.

In the Federation of Bosnia and Herzegovina, foreign natural persons cannot be owners of trade shops. In both the Federation of Bosnia and Herzegovina and Republika Srpska, laws on handicrafts stipulate that a foreign natural person can open handicraft shops under conditions of reciprocity.

The Federation and Republika Srpska have modified their respective laws governing auditing and accounting services and allow foreign and domestic physical persons to establish firms in these areas.

Foreign-controlled enterprises are treated as domestic legal persons in Bosnia and Herzegovina with respect to real estate acquisition. However, foreign investors who are citizens of one of the successor states to the former Socialist Federal Republic of Yugoslavia have such rights subject to the investors' citizenship and legal status.

Corporate organisation: For this review, Bosnia and Herzegovina has indicated that it does not apply discriminatory court registration fees for foreign-owned companies.

Transparency measures: See section on "Equity and other discriminatory measures on establishment" above. Bosnia and Herzegovina has indicated that a location restriction no longer applies to wholly foreign-owned companies locating in a military zone.

Croatia

Approval and licensing/screening procedures: Croatia does not require foreign enterprises to undergo any specific trans-sectoral approval or screening procedures. Registration procedures are similar to those for domestic enterprises, which require notification in Commercial Courts.

With respect to the securities market and other financial services sectors, the 2003 report noted that the Law on Securities Market (2002) allowed foreign legal persons to issue securities through

public offerings only if represented by a broker house registered in Croatia. Furthermore, foreign broker houses could establish a branch office in order to deal with security transactions provided they obtained approval by the Croatian Securities Commission (CROSEC), according to the conditions of Article 50 of the Law on Securities Market. Croatian authorities have since clarified certain elements of the law as a result of specific amendments (*e.g.*, Laws 88/08, 146/08, and 74/09). For example, once Croatia becomes a full EU member, foreign legal persons will not be required to issue securities through domestic brokerage houses. Currently foreign enterprises offering investment services cannot establish a branch office in Croatia, however they can establish a legal company and request approval from HANFA (Croatian Financial Services Supervisory Agency). Once in the EU, foreign enterprises offering investment services (from the EU) will be able to deliver services via branch offices, provided the necessary information is sent from the home-country regulator to HANFA (Articles 144 to 147 of the Law on Securities). Investment service companies from third countries would also be permitted to provide services via branch offices, provided they have permission from HANFA (Articles 148 to 151 of the Law on Securities).

Equity and other discriminatory measures on establishment: As part of efforts to harmonise laws with the EU legislation and regulations, previous restrictions on foreign participation in the insurance sector have been removed. Companies for mutual insurance could be set up by at least 250 exclusively individuals and legal persons. As a result of a new Law on Insurance (Law 151/05, 87/08 and 75/09), the restriction on “exclusively domestic individuals and legal persons” has been removed.

In the telecommunications sector, the Electronic Communications Act (73/08) provides that any natural or legal entity can install, use and make available an electronic communications network and services without obtaining a special authorisation. This appears to remove a previous reciprocity condition notified by Croatia in the 2003 review.

Croatia has confirmed that restrictions on foreign equity exist in the air transport sector: cabotage services and fishing are reserved for ships flying the national flag. Restrictions in the energy sector remain as indicated in the 2003 review.

Corporate organisation: Croatia does not impose restrictions on foreign enterprises with respect to corporate organisation.

Transparency measures: Location restrictions remain, whereby the ownership of real estate is prohibited to a foreign person if the real estate is situated in territories which are designated by law as important for the protection of security interests (*e.g.*, borders, coastline, islands, forests and agricultural land). The majority of foreign-controlled enterprises established in Croatia as domestic legal persons receive national treatment with respect to acquisition of real estate.

Former Yugoslav Republic of Macedonia

Approval and licensing/screening procedures: The former Yugoslav Republic of Macedonia does not maintain trans-sectoral approval or licensing/screening procedures. However, both inward and outward direct investments must be registered at the Central Register.

Equity and other discriminatory measures on establishment: In the insurance sector, the former Yugoslav Republic of Macedonia (Law on supervision of insurance No. 27/2002, 79/2007 and 88/2008) maintains that individual shares of a legal entity or natural person in an insurance company can go up to only 25% of the equity, a rule which applies to both foreign and domestic investors (article 16 of the abovementioned Law). In the case of a foreign-controlled insurance company, individual shareholding may go up to 65%, and with special approval of the Minister of Finance, up to 80%.

In the gaming sector, foreign investors cannot independently organize games of chance other than machine games in their own four- or five-star hotels. (They may organize games of chance in conjunction with domestic legal or natural persons in their own hotel if the foreign equity share is higher than 50%.)

The former Yugoslav Republic of Macedonia maintains restrictions to foreign ownership of rural land, however opportunities for leasing exist (new Law on Construction Land 82/08).

Corporate organisation: The former Yugoslav Republic of Macedonia does not maintain restrictions on corporate organisation.

Transparency measures: Authorities have confirmed that a previous restriction on foreign investment in the production and trade with armaments exists. Foreign investors are allowed to invest in military industry and arms trade (Law on production and trade with armament and military equipment No. 54/2002 and 84/2007). According to Article 13 of the Law, foreign legal entities and persons (alone or together with domestic legal entities and persons) can establish a company for the production of armaments and military equipment following approval from the Government. Foreign legal entities and persons, together with domestic legal entities and persons, can also establish a company for trade of armaments and military equipment following approval from the Government. The share of foreign legal entities and persons cannot be higher than 49% from the total amount of shares of the company.

Real estate limitations exist, as there are restrictions on foreign investment designed to protect historical monuments and the cultural assets of the country.

Republic of Moldova

Approval and licensing/screening procedures: The Republic of Moldova has indicated that since the adoption of Law on Investments in Entrepreneurial Activity (No. 81/04), the principle of national treatment is applied to investments. Republic of Moldovan authorities have confirmed that some companies need approval from the National Agency for the Protection of Competition as a result of

the Law on Competition Protection (no.1103/00). However, the approval requirement is not linked to the amount of foreign equity but to the size of the company on the local market.⁵

Equity and other discriminatory measures on establishment: The Republic of Moldova maintains a restriction on foreign ownership of agricultural land.

Corporate organisation: The Republic of Moldova has indicated that it does not maintain restrictions on the management of foreign equity by foreign-controlled enterprises. A previous restriction mandated that foreign-controlled enterprises should maintain at least 10% of foreign equity in the form of hard currency.

Transparency measures: The sale and production of combat and special military technical equipment are under state monopoly. Medical and treatment services are no longer part of this list. The Republic of Moldova has removed a previous condition whereby a manager of an enterprise holding an energy licence must have permanent residence in the Republic of Moldova.

Montenegro

Approval and licensing/screening procedures: Montenegro does not maintain trans-sectoral approval or screening procedures. A previous reciprocity condition has been removed in amendments to the Foreign Investment Law in 2007. The only trans-sectoral procedure required is registration with a local court.

On a sector-specific basis, Montenegro maintains screening procedures regarding fishing activities. According to the Law on Marine Fishery and Mariculture (56/09), fishing vessels under foreign flags are prohibited to fish in Montenegrin waters. However, foreign fishing vessels may fish in Montenegrin waters if they possess fishing licenses issued in accordance with international agreements and confirmed by the Ministry of Agriculture.

Equity and other discriminatory measures on establishment: The amended Montenegrin Foreign Investment Law maintains a 49% foreign ownership restriction in industries related to the production of arms and arms trade and areas which are defined by law as forbidden zones (national parks and border areas etc.).

In the insurance sector, Montenegro appears to have lifted a previous reciprocity condition with a new Law on Insurance (78/06). Foreign insurance companies may establish in Montenegro provided they comply with requirements listed in Article 42 of Law 78/06 and receive approval from the appropriate Montenegrin regulatory authority.

⁵ The 2003 report indicated that companies with foreign equity exceeding US\$ 5 million needed approval from the National Agency for the Protection of Competition as a result of the Law on Competition Protection (No. 1103/00)

In the gaming sector, Montenegrin authorities have indicated that a previous restriction on majority foreign ownership of domestic enterprises permitted to engage in games of chance has been lifted.

With respect to ownership of real estate, previous reciprocity requirements have been removed. Under the new Property Law (19/09), a foreign person cannot have an ownership right to *inter alia* natural resources, agricultural land, forest and forest land (complete list identified in Article 415 of Law 19/09). However, Law 19/09 does provide certain exceptions where a foreign physical person could acquire ownership rights on agricultural land, forests and forest land of a surface up to 5 000m² provided a residential building is located on this land and is subject to a contract of divestiture, lease, concession or build-operate-transfer (BOT).

Corporate organisation: In the 2003 review of national treatment restrictions, it was noted that foreign legal entities in Montenegro who used ships, yachts, or aircraft for the purpose of earning income were required to establish a company according to the provision of the Law on Off-shore Companies. Montenegrin officials have indicated that the Law on Off-shore Companies has been repealed for nearly five years and those restrictions no longer apply.

Transparency measures: See section on “equity and other discriminatory measures on establishment” for restrictions related to arms and arms trade and industries operating in forbidden areas such as national parks and border areas.

Serbia

Approval and licensing/screening procedures: Serbia does not apply a trans-sectoral approval or screening procedure for foreign investment.

In the insurance sector related to establishing insurance joint stock companies or re-insurance joint stock companies, foreign legal and natural persons have the same rights and treatment as domestic investors. In the basic version of the Law on Insurance from 2004, there was only one restriction concerning foreign investors: the reciprocity principle. However, Serbia has indicated that this condition will be abolished by the date of accession of Serbia to the World Trade Organization (amendments No. 101/07).

In the air transport sector, Serbia has clarified that an aircraft, whose owner or user is a foreign legal entity or natural person, may be registered in the Aircraft Register of Serbia after a special permit has been granted by the Civil Aviation Directorate of the Republic of Serbia. Article 54 and the Law on Air Transport (No. 12/98, 5/99, and amendments 44/99, 73/00, 70/01 and 101/05) are in force.

In the maritime transport sector, Serbia has confirmed that approval for cabotage services, *i.e.*, towing, which begins and ends in a Serbian river port that is on the inland waterway of Serbia cannot be given to a foreign ship without the approval of the Ministry of Transport (Article 686 of the Law on Maritime and Inland Navigation). Serbia indicates that a new Law on Navigation Safety and Ports in Inland Waterways of Serbia is being drafted and will contain a provision by which European Economic Community Regulations 3921/91 and 1356/96 will be incorporated in national legislation.

These regulations stipulate the abolishment of restrictions related to cabotage in inland waterways of Serbia for EU vessels and carriers that are residents of the EU member states. This provision will enter into force when Serbia becomes a member of the EU.

Equity and other discriminatory measures on establishment: Serbia has clarified its position on the issue of reciprocity. According to the new Constitution (2006) and the Company Law (2004), the reciprocity principle is not a condition for a natural or legal person to establish an enterprise in Serbia. Article 22 of the Foreign Investment Law stipulates that registration of enterprises from countries with which Serbia does not have reciprocity principle is only for record-keeping purposes and is not a precondition for establishing an enterprise in Serbia.

The only case where reciprocity still exists is in the acquisition and owning of real estate in Serbia, whereby a foreign natural or legal entity doing business in Serbia may acquire real estate if the reciprocity requirement is met and if the acquired property is related to doing the business. This issue is regulated within the Law on the Elements of Property Law Relations (SFRY laws No. 6/80 and 36/90 and FRY No. 29/96). A new Law on Public Property is currently in the process of adoption by Parliament and it will not contain the reciprocity principle.

The previous Law on Banks and Other Financial Organisations was replaced by a new Law on Banks in 2005. According to Article 11 of the Law on Banks, foreign and domestic legal and natural persons may found a bank without reciprocity-related restrictions.

With respect to the insurance sector, Serbia has clarified that there are no other restrictions except those which are related to a specific legal form for incorporation of financial institutions in Serbia (Law on Insurance, No 55/04 and amendments No. 70/04, 61/05, 85/05 and 101/07). As a general rule, and in a non-discriminatory manner, financial institutions incorporated in Serbia must adopt a specific legal form. Insurance companies, reinsurance companies, banks, broker and dealer companies, investment funds, founder of over-the-counter market and stock exchange must be incorporated as joint stock companies. Exceptions exist for insurance brokerage, insurance agency services, other insurance services, legal entities that perform financial leasing, legal entities for provision of investment advisory services and companies for investment fund management must be incorporated as joint stock companies or limited liability companies. Asset management companies that manage and organize voluntary pension funds must be established as non-public joint stock companies. According to Article 10 of the Law on Insurance of Property and Persons (No. 30/96), these restrictions were abolished with the adoption of the new Law on Insurance from 2004 (No. 55/04) and amendments (No. 70/04, 61/05, 85/05 and 101/07).

Serbia has also clarified that insurance companies established in Serbia operate in accordance with the national treatment principle, that is, they can be involved in reinsurance above the limits that could not be reinsured in Serbia, as prescribed in the Law on Insurance from 2004.⁶ Related to

⁶ Article 15 of the 2004 Law on Insurance states “Insurance companies in Serbia are obliged to reinsure contractual obligations exceeding the amount of self insured retention. Insurance companies are obliged to keep a part of the risk in self insured retention. Insurance companies are obliged to reinsure the risk exceeding the self insured retention, with a reinsurance company commercially established in

reinsurance activities, Article 27 of the same law stipulates that reinsurance activities can be performed by joint stock companies which acquire licenses for such activities. Restrictions related to foreign legal persons contained in Article 10, paragraphs 4 and 5, of the Law on Insurance of Property and Persons from 1996 are abolished.

In the maritime transport sector, Serbia has confirmed that regarding the payment of port dues, foreign ships enjoy the same treatment as domestic ones, subject to the reciprocity principle (Article 25 of the Law on Maritime and Inland Navigation). In addition, the issuance of a permit for the registration of a foreign ship in the Serbian Register of Shipping is conditional upon the ship owner or ship operator submitting the decision on the approval of the temporary import of a chartered ship and uniform customs clearance for a temporary or regular import of a ship by the appropriate authority (Article 211 of the Law on Maritime and Inland Navigation).

Serbia has confirmed that a foreign natural person or legal entity cannot invest in gaming according to Articles 6 and 7 of the Law on Games of Chance. However, according to Article 5 of this law, gaming is considered a state monopoly, but can be transferred to some domestic legal entities located in Serbia.

Serbia has indicated that a foreign natural person or legal entity cannot buy a forest or own agricultural land. Foreign and domestic natural and legal entities cannot own urban construction land.

Corporate organisation: Serbia does not use impose restrictions on corporate organisation.

Transparency measures: Serbia has confirmed that a foreign person may not have majority ownership in enterprises dealing with trade of weapons and ammunition, or in enterprises established in restricted areas (such as frontier strip, national parks or military areas) and must have the approval of the competent ministry for investments in such cases. Foreign persons may establish or invest in such companies, however only with a domestic partner upon meeting the aforementioned requirements.

UNMIK-Kosovo

UNMIK-Kosovo was not included in the 2003 OECD Investment Compact review of restrictions to national treatment. A relevant benchmark, therefore, does not exist for assessing changes to measures that restrict national treatment. Research for the OECD's Investment Reform Index 2009 indicate that foreign investors may acquire up to 49% equity holdings in sectors related to military production. The Law on Foreign Investment (No. 02/L-33) does not provide restrictions on corporate organisation of foreign-controlled enterprises. Although restrictions on the ownership of land appear minimal, it is unclear if designated zones exist where foreign enterprises may not purchase land or real property.

Serbia. These reinsurance companies are obliged to reinsure with a foreign reinsurer the portion of the risk they are not able to cover from their own means or the portion of the risk they are not able to cover with a reinsurance company commercially established in Serbia.”

**REVIEW OF BILATERAL INVESTMENT TREATIES SIGNED BY PARTIES TO THE
CEFTA 2006**

This working paper reviews the content of bilateral investment treaties listed in Annex 6 of the CEFTA 2006 with a view to identifying commonalities and potential gaps. The working paper examines provisions on admission and treatment (i.e., national treatment and most-favoured nation); transfers, expropriation, and dispute settlement (i.e., state-to-state and investor-to-state).

INTRODUCTION

Section B “Investment” of the CEFTA 2006, Article 30(1) confirms the parties’ rights and obligations under the existing network of bilateral investment treaties (BITs) signed amongst themselves.⁷ By linking these BITs to the CEFTA, the parties reinforce a layer of protection for foreign investors and their investments. There are currently 14 BITs covering the existing CEFTA parties⁸ (Albania, Bosnia and Herzegovina, Croatia, the former Yugoslav Republic of Macedonia, Republic of Moldova, Montenegro, Serbia and UNMIK-Kosovo).

This paper reviews the content of BITs⁹ in Annex 6 with a view to identifying commonalities and potential gaps. Table 1 of this report summarises the common elements of those BITs.

The structure of BITs in Annex 6 closely follows those used by many OECD countries,¹⁰ covering areas such as: admission and treatment (*i.e.*, national treatment and most-favoured nation), transfers, expropriation and dispute settlement (*i.e.*, state-to-state and investor-to-state).

This paper compares the following provisions in each BIT: definitions, treatment, protection, transparency and application.

⁷ As identified in Annex 6 of the CEFTA 2006. The date of entry into force is noted in parentheses beside each treaty.

⁸ The bilateral treaties signed by Serbia and Montenegro in this review are denoted as “Yugoslavia” given that the Federal Republic of Yugoslavia was the signatory Party at the time of negotiation and ratification. Serbia and Montenegro continue to abide by the terms of the BITs signed and ratified by the Federal Republic of Yugoslavia.

⁹ As Romania and Bulgaria have acceded to the European Union and hence are no longer covered by the provisions of the CEFTA, their BITs with existing CEFTA parties are excluded from this review. Furthermore, only copies of BITs in the English language were reviewed.

¹⁰ The BITs signed by CEFTA parties closely resemble the European model based on the Abs-Shawcross Draft Convention model endorsed by OECD members in 1962. See OECD (2004), *Relationships between International Investment Agreements*. (www.oecd.org/daf). BITs used by North American members of the OECD differ from the European model by including national treatment at the pre- and post-establishment phases of investment.

A. Definitions

Definitions determine the scope of application of rights and obligations under the BITs. All of the BITs in Annex 6 define *inter alia* the following terms:

- investments
- investors
- returns

The definition of “investment” is asset-based and includes a non-exhaustive illustrative typically including:

- (i) Movable and immovable property and any other property rights such as mortgages, liens, usufructs, pledges and similar rights;
- (ii) Shares, stocks and debentures as well as other kinds of securities of a company and any other form of participation in a firm;
- (iii) Claims to money or any other claim under contract having an economic value;
- (iv) Intellectual property rights, such as copyrights and industrial property rights, such as patents, licences, industrial designs or models, trademarks as well as goodwill, technological processes and know-how;
- (v) Rights granted by a public authority to carry out an economic activity, including concessions, for example, to search for, extract or exploit natural resources.

However, the Albania-Republic of Moldova (2004) BIT includes an extra asset:

- (vi) Goods that, under a leasing agreement, are placed at the disposal of a lessee in the territory of a Contracting Party, in conformity with its laws and regulations.

Furthermore, the agreements between Croatia-Republic of Moldova (2001) and Croatia-Yugoslavia (2002) specify intellectual properties:

“as defined under the auspices of the World Intellectual Property Organisation, in as far as the contracting parties are party to them.”

The term “investor” in the majority of BITs is defined as a natural person or a legal person of one of the contracting parties, making investments in the territory of the other party. A “natural” person is typically defined as a physical person carrying the nationality of one of the contracting parties in accordance with its law. A “legal” person is described as an entity, constituted or otherwise duly organised in accordance with the laws and regulations of one contracting party, having its seat and performing real business activity in the territory of that party and making investments in the territory of the other party.

A slight nuance is found in the definition of investor in Bosnia and Herzegovina's BITs. For example, the Bosnia and Herzegovina-Yugoslavia (2004) and Bosnia and Herzegovina-former Yugoslav Republic of Macedonia (2002) BITs parse investors into "natural" and "legal" persons, while the Bosnia and Herzegovina-Republic of Moldova (2003) BIT describes investors as "physical" and "legal" persons.

"Return to investment" is consistently defined as income yielded by an investment and in particular, but not exclusively, including profit, interest, capital gains, dividends, royalties and other fees.

B. Treatment

The treatment which BITs can accord to the other contracting party's investors and their investments may include "relative" and "absolute" standards. Relative standards include most-favoured nation (MFN), whereby the treatment which is accorded to investors and their investments in the host country is no less favourable than that accorded to investors and investments of any third state; or, national treatment (NT), whereby the treatment accorded to investors and their investments is no less favourable than that accorded to investors and investments of the host country.

The obligation of "fair and equitable" treatment offering "full protection and security" to foreign investors and their investments is regarded as an absolute standard, whereby there is some minimum level of treatment that must be accorded to international investors and/or their investments.¹¹ Nearly all of the BITs examined in this review contain provisions for fair and equitable treatment offering of full protection and security. The Croatia-former Yugoslav Republic of Macedonia (1995) BIT includes the fair and equitable treatment standard, however, it does not include the phrase "full protection and security."

The majority of BITs also provide MFN and NT at the post-establishment phase of investment for investors and their investments. Exceptions are the agreements between Albania-Yugoslavia (2004) and Albania-Kosovo (UNMIK) (2005), where MFN and NT are only included for investments and returns to investments. These agreements appear to exclude investors. The Croatia-former Yugoslav Republic of Macedonia (1995) BIT only provides MFN treatment for investments at the post-establishment stage.

¹¹ The obligation of parties to investment agreements to provide "fair and equitable treatment" of each other's investments has been given various interpretations by governmental officials, arbitrators and scholars. Discussion of this standard has focused mainly on whether the standard of treatment required is measured against the customary international law minimum standard, a broader international law standard including other sources (such as investment protection obligations generally found in treaties and general principles) or whether the standard is an autonomous, self-contained concept in treaties which do not explicitly link it to international law. OECD (2004), Fair and equitable standard in international investment law (www.oecd.org/daf)

C. Protection

For the purpose of this review, provisions related to protection refer to those that provide for compensation for expropriation rights to transfers of capital and returns subrogation and dispute settlement mechanisms at the state-to-state and investor-to-state level.

All of the agreements reviewed include broadly consistent provisions regarding compensation of losses, the settlement of disputes between the contracting parties, the settlement of disputes between a contracting party and an investor, and subrogation.

Provisions on expropriation are a standard feature as well. All of the BITs provide that compensation for expropriation should be equal to the market value of the investment immediately before the occurrence of the expropriation or before it becomes public knowledge. Furthermore, the majority of treaties specify that payment must be “prompt, adequate and efficient.” Three BITs use a modification of this phrase: Croatia-former Yugoslav Republic of Macedonia (1995) and former Yugoslav Republic of Macedonia-Yugoslavia (1997) mention a payment that is “adequate, efficient and without undue delay,” while Croatia-Republic of Moldova (2001) cites payment that is “adequate, efficient and without delay.”

The approach regarding calculation of interest on compensation payments differs among the treaties reviewed. The former Yugoslav Republic of Macedonia-Yugoslavia (1997), Croatia-former Yugoslav Republic of Macedonia (1995) and Albania-Kosovo (UNMIK) (2005) refer to an interest rate calculated on an annual LIBOR basis. While Albania-Croatia (1994), Albania-Republic of Moldova (2004), Albania-Yugoslavia (2004), Bosnia Herzegovina-former Yugoslav Republic of Macedonia (2002), Bosnia and Herzegovina-Republic of Moldova (2003) and Bosnia and Herzegovina-Yugoslavia (2004) refer to interest rates calculated according to “normal commercial rates.” In contrast, Croatia-Yugoslavia (2002) and Croatia-Republic of Moldova (2001) do not specify the inclusion of interest on compensation payments.

The commitment to free transfers of capital and other payments is common in the reviewed BITs. These transfers are to be made in a freely convertible currency and without delay. The types of transfers are generally based on an illustrative list which includes the following:

- (i) Returns from investments;
- (ii) The initial capital and additional amounts necessary for the maintenance and development of the investment;
- (iii) Funds in repayment of loans related to an investment;
- (iv) Payments arising from the settlement of disputes;
- (v) Proceeds from the total or partial sale or liquidation of an investment;

(vi) Any compensation or other payment referred to in the Agreement, for example in the case of expropriation;

(vii) Unspent earnings and other remuneration of nationals engaged from abroad in connection with the investment.

Croatia-former Yugoslav Republic of Macedonia (1995), Albania-Republic of Moldova (2004), Albania-Croatia (1994) and former Yugoslav Republic of Macedonia-Yugoslavia (1997) do not specifically mention any transfers resulting from the settlement of disputes. Former Yugoslav Republic of Macedonia-Yugoslavia (1997) does not include the earnings of nationals engaged from abroad in its list of transfers.

D. Transparency

The BITs in Annex 6 typically include transparency-related provisions on consultations. In most BITs, the contracting parties agree to hold consultations at the request of either party, concerning matters related to the application and interpretation of the agreement. Albania-Yugoslavia (2004), Albania-UNMIK-Kosovo (2005), Croatia-Yugoslavia (2002) and Croatia-Republic of Moldova (2001) do not include any provisions that instruct the contracting parties to engage in consultations concerning the operation of their agreements. However, Croatia-Republic of Moldova (2001) does contain a clause that specifies that either “Contracting Party will endeavour to inform the other Party, at the request of either Party, on the investment opportunities in its territory.” Bosnia and Herzegovina-former Yugoslav Republic of Macedonia (2002), Bosnia and Herzegovina-Republic of Moldova (2003), Bosnia and Herzegovina-Yugoslavia (2004) and Croatia-former Yugoslav Republic of Macedonia (1995) have added additional clauses specifying that exchange of extra information on the impact of laws, regulations, decisions, administrative practices or procedures or policies of one contracting party on investments covered by the other contracting party is possible on the request of either contracting party.

E. Application of treaties and other rules

The majority of treaties reviewed provide that only investments made after the entry into force of the agreements shall be covered by the provisions of the BITs. Three exceptions are the agreements between Albania-Croatia (1994), Albania-Republic of Moldova (2004) and Croatia-Republic of Moldova (2001), where investments made prior to the agreements are covered. Croatia-Republic of Moldova (2001) notes that investments made prior to the agreement are covered, but investment disputes arising before the agreement entered into force are not.

Furthermore, all of the treaties, with the exception of Bosnia and Herzegovina-former Yugoslav Republic of Macedonia (2002) include a provision on application of more favourable rules. Such a provision typically provides that:

if the legislation of either party or obligations under international law existing at present or established hereafter between the parties in addition to the agreement contain a regulation, whether general or specific, entitling investments by investors of the other party to a treatment more favourable

than that provided for by this agreement, such regulation shall prevail over the agreement to the extent that it is more favourable.

The Croatia-Republic of Moldova (2001) BIT adds an addition clause stating that:

“Each Contracting Party shall observe any contractual obligation it may have entered into towards an investor of the other Contracting Party with regard to investment approved by it in its territory.”

Furthermore, the Croatia-Republic of Moldova (2001) BIT includes an article specifying that amendments may be introduced in the agreement in due manner, and that these amendments will become part of the agreement and will fall under the same application rules. The other BITs in Annex 6 do not include anything similar.

Summary of Key Provisions of Selected Bilateral Investment Treaties in Annex 6 of the CEFTA 2006

	Definitions			Treatment of investments					
	Investments	Investors	Returns	Fair and equitable treatment	Full protection and security	MFN		NT	
						Investments	Investors	Investments	Investors
Albania – Croatia (1994)	√	√	√		√	√	√	√	√
additional protocol between Albania and Croatia	√	√	√	√	√	√	√	√	√
Albania – Republic of Moldova (2004)	√	√	√	√	√	√	√	√	√
Albania – Yugoslavia (2004)	√	√	√	√	√	√		√	
Albania – UNMIK-Kosovo (2005)	√	√	√	√	√	√		√	
Bosnia and Herzegovina – (FYR) Macedonia (2002)	√	√	√	√	√	√	√	√	√
Bosnia and Herzegovina – Republic of Moldova (2003)	√	√	√	√	√	√	√	√	√
Bosnia and Herzegovina – Yugoslavia (2004)	√	√	√	√	√	√	√	√	√
Croatia – (FYR) Macedonia (1995)	√	√	√	√		√			
Croatia – Republic of Moldova (2001)	√	√	√	√	√	√	√	√	√
Croatia – Yugoslavia (2002)	√	√	√	√	√	√	√	√	√
(FYR) Macedonia – Yugoslavia (1997)	√	√	√	√	√	√	√	√	√

Summary of Key Provisions of Selected Bilateral Investment Treaties in Annex 6 of the CEFTA 2006 (cont'd)

	Protection of investments						
	Expropriation		Compensation for losses	Transfers	Subrogation	Dispute settlement	
	Payment is prompt, adequate and efficient	Market value compensation				State-to-State	Investor-to-State
Albania – Croatia (1994)	√	Normal commercial rates	√	√	√	√	√
additional protocol between Albania and Croatia	√	√	√	√	√	√	√
Albania – Republic of Moldova (2004)	√	Normal commercial rates	√	√	√	√	√
Albania – Yugoslavia (2004)	√	Normal commercial rates	√	√	√	√	√
Albania – Kosovo (UNMIK) (2005)	√	LIBOR	√	√	√	√	√
Bosnia and Herzegovina – (FYR) Macedonia (2002)	√	Normal commercial rates	√	√	√	√	√
Bosnia and Herzegovina – Republic of Moldova (2003)	√	Normal commercial rates	√	√	√	√	√
Bosnia and Herzegovina – Yugoslavia (2004)	√	Normal commercial rates	√	√	√	√	√
Croatia – (FYR) Macedonia (1995)		LIBOR	√	√	√	√	√
Croatia – Republic of Moldova (2001)		Unspecified	√	√	√	√	√
Croatia – Yugoslavia (2002)	√	Unspecified	√	√	√	√	√
(FYR) Macedonia – Yugoslavia (1997)		LIBOR	√	√	√	√	√

Figure 1. Summary of Key Provisions of Selected Bilateral Investment Treaties in Annex 6 of the CEFTA 2006 (cont'd)

	Application of other rules	Application of the agreement		Consultations and transparency	
		Prior coverage	Post coverage	Related to the agreement	Exchange of information on laws, regulations, decisions, etc.
Albania – Croatia (1994)	√	√	√	√	
additional protocol between Albania and Croatia	√	√	√	√	
Albania – Republic of Moldova (2004)	√	√	√	√	
Albania – Yugoslavia (2004)	√		√		
Albania - UNMIK/Kosovo (2005)	√		√		
Bosnia and Herzegovina – (FYR) Macedonia (2002)			√	√	√
Bosnia and Herzegovina – Republic of Moldova (2003)	√		√	√	√
Bosnia and Herzegovina – Yugoslavia (2004)	√		√	√	√
Croatia – (FYR) Macedonia (1995)	√		√	√	√
Croatia – Republic of Moldova (2001)	√	√	√		
Croatia – Yugoslavia (2002)	√		√		
(FYR) Macedonia – Yugoslavia (1997)	√		√	√	

REFERENCES

National Treatment Restrictions in Parties to the CEFTA 2006

OECD (2003), National Treatment of International Investment in South East European Countries: Measures Providing Exceptions, OECD, Paris

Responses to 2009 OECD Investment Compact survey on national treatment restrictions:

- Albania
- Bosnia and Herzegovina
- Croatia
- The former Yugoslav Republic of Macedonia
- Montenegro
- Republic of Moldova
- Serbia

Review of Bilateral Investment Treaties Signed by Parties to the CEFTA 2006

OECD (2004), Relationships between International Investment Agreements, OECD, Paris

The following bilateral investment treaties were reviewed:

- Albania – Croatia (1994) including the additional protocol between Albania and Croatia
- Albania – Republic of Moldova (2004)
- Albania – Yugoslavia (2004)
- Albania – UNMIK-Kosovo (2005)
- Bosnia and Herzegovina – (FYR) Macedonia (2002)
- Bosnia and Herzegovina – Republic of Moldova (2003)
- Bosnia and Herzegovina – Yugoslavia (2004)

- Croatia – (FYR) Macedonia (1995)
- Croatia – Republic of Moldova (2001)
- Croatia – Yugoslavia (2002)
- (FYR) Macedonia – Yugoslavia (1997)

