BILATERAL INVESTMENT TREATIES: WHEN DOUBLE TAXATION AGREEMENTS ARE NOT ENOUGH

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The U.S. enters into bilateral investment treaties ("B.I.T.'s") to protect and promote foreign investment. Unlike double taxation agreements ("D.T.A.'s"), which relate exclusively to tax matters, they are not usually seen as a defense mechanism when dealing with foreign tax authorities. Interestingly, they are!

Over the last few years B.I.T.'s have become useful tools for investors dealing with what appear to be unresolvable tax issues with foreign governments. This article will explore similarities and differences between B.I.T.'s and D.T.A.'s, and will discuss the recent *Georgian Manganese* case, where the taxpayer chose to rely on the B.I.T. instead of the D.T.A.

BACKGROUND

The U.S. has concluded 47 B.I.T.'s, not including investment provisions and other investment-related instruments, with foreign jurisidictions. Of these countries, nearly half do not have D.T.A.'s in place. They are Albania, Argentina, Bahrain, Bolivia, Cameroon, Democratic Republic of Congo, Croatia, Ecuador, El Salvador, Granada, Haiti, Honduras, Jordan, Mongolia, Mozambique, Nicaragua, Panama, Rwanda, Senegal, Trinidad and Tobago, and Uruguay.

B.I.T.'s and D.T.A.'s are drafted and negotiated by different institutions. A B.I.T. is negotiated by the national investment agency or the Ministry of Trade, while a D.T.A. is negotiated by the Ministry of Finance. Although they represent two different agreements negotiated by two different institutions, there is a great deal of similarity between the two. Both provide certainty when making an investment, provide dispute resolution mechanisms, and assist with growth and investments in the partner countries.

In addition, B.I.T.'s provide many advantages that are not present in D.T.A.'s:

- B.I.T.'s do not require that litigation commence in the local courts. Investors can choose to arbitrate claims in the International Centre for Settlement of Investment Disputes ("I.C.S.I.D.") (Convention Arbitration), the Additional Facility of I.C.S.I.D. (if Convention Arbitration is not available) or any other arbitration institution or rules agreed upon by both parties to the dispute, or they can choose ad hoc arbitration using the Arbitration Rules of the United Nations Commission on International Trade Law ("U.N.C.I.T.R.A.L.").
- B.I.T.'s provide that the host country will not treat a partner jurisdiction investment, or activities associated therewith, less favorably than an investment, or associated activities, of its own nationals or companies, or nationals or companies of any third country. This usually provides a favorable commitment from the host country.

- B.I.T.'s include a commitment to permit all transfers related to an investment to be made freely and without delay into and out of the host country.

Historically, B.I.T.'s have been chosen over the D.T.A.'s due to the availability of international arbitration without going through the local court system.

Notably, B.I.T.'s do not impose tax reductions or exemptions, or impose measures to reduce double taxation. For those benefits, taxpayers should continue to rely on D.T.A.'s.

GEORGIA AMERICAN ALLOYS, INC.

Earlier this year a U.S. private company, Georgia American Alloys, Inc., ("G.A.A.") filed a request with the Department of Treasury for assistance in a dispute with the Government of Georgia pursuant to Article XIII of the U.S.-Georgia B.I.T. G.A.A., through its subsidiaries, is engaged in production of a manganese ferroalloy and has invested a significate amount not only in its Georgian facilities but in the local community's infrastructure and services.

According to the request (the "Submission") filed on May 4, 2017, the Government of Georgia used expropriatory measures[1] when it assessed more than $82.45 million in taxes, penalties, and interest. G.G.A. alleged that the amount would entirely deprive it of its investments in Georgia. According to the Submission, Georgian authorities also intimidated and harassed one of the G.A.A. subsidiaries, Georgian Manganese, LLC ("G.M.") by denying fair court and audit proceedings through the lower court system.

The Submission covers following four issues:

- **Accounting of Waste.** When calculating the value of G.M.'s inventory the Government of Georgia included valueless waste products as inventory, even though the company does not have the technology to obtain an economically viable manganese containing product from these materials. G.M. has tried to commercialize the waste, but the cost exceeds the price for which waste could be sold. Furthermore, two major accounting firms, PwC and EY, both confirmed that G.M.'s accounting method complies with the Tax Code of Georgia and International Accounting Standards.

- **Transfer Pricing.** The Government of Georgia claimed that the exported product was improperly valued. It is not clear how the Government of Georgia priced the products, as it has not produced its calculation method. However, G.M. obtained an opinion from the outside auditors, EY and PwC, that verified the pricing of its products and confirmed it is consistent with the arm's length principal defined in the O.E.C.D. guidelines governing intercompany transactions.

- **Employee Meals.** G.M. provided food (so-called subsidized employee meals) to its employees, for which it recorded its costs and paid taxes thereon based on the market price of the meals. The general standard is market price plus a 10% mark up. However, the Government of Georgia assessed

[1] Expropriation occurs when state measures have the effect of substantially depriving an investor of the value of its investment.

taxes on the meals at the market price plus a 70% mark up. According to the Submission, G.M.'s valuation meets the general standard.

- **Additional Taxes, Penalties and Interest.** In addition to the taxes described above, the Government of Georgia assessed additional taxes, penalties, and interest, which G.A.A. contested.

Interestingly, in this case, G.A.A. did not choose the B.I.T. because of the possibility to arbitrate the case without going to the court. Rather, G.A.A. relied on the B.I.T. with Georgia because the D.T.A. did not provide a feasible defense to the fines imposed to by the Government of Georgia.

Soon after the Submission was filed, Georgia's Kutaisi Court of Appeals overturned the lower court's decision and ordered the Georgian Revenue Service to reopen the case to calculate the correct payment due.

CONCLUSION

In recent years, Georgia has become a popular frontier for foreign businesses. The Kutaisi Court of Appeals decision may be a signal that the court was mindful of the impact its decision could have on future investments in Georgia.

While D.T.A.'s are the traditional way that multinational taxpayers resolve tax disputes, the use of B.I.T.'s provides an interesting alternative. B.I.T.'s are, perhaps, the only method of resolving financial disputes (including confiscatory tax assessments) in those jurisdictions that do not have D.T.A.'s with the U.S. However, *Georgian Manganese* serves as a reminder that their use should not be overlooked in jurisdictions where multiple treaty options are available.

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