Congressional Research Service

## Memorandum July 18, 2006

**SUBJECT:** Legal Issues Related to the Proposed Oman Free Trade Agreement and Port Security

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This memorandum is in response to requests for a legal analysis of three arguments that have been advanced in opposition to the proposed Oman Free Trade Agreement (FTA). Each of the arguments relate to issues surrounding port security and, specifically, the ability of Omani companies or companies incorporated in Oman to perform "landside aspects of port activities" in the United States. This memorandum provides a legal analysis of three questions: First, whether the proposed Oman FTA allows Omani companies or companies incorporated in Oman to perform "landside aspects of port activities"[1] at U.S. ports, especially in light of the dispute over Dubai Ports World's attempt at establishing similar business operations at various ports in the United States. Second, whether the proposed Oman FTA provides some type of advance clearance to Omani companies that wish to begin landside port operations in the United States. Finally, this memorandum provides a legal analysis with respect to the possibility of a third-country company (*e.g.*, Dubai Ports World or similarly-situated foreign entity), establishing a minimal presence within Oman for the sole purpose of taking advantage of the benefits provided by the provisions of the proposed FTA.

One argument that has been raised against the proposed Oman FTA appears to stem specifically from language contained in Annex II of the Agreement. The argument generally asserts that the proposed Oman FTA provides a new right to both Omani-owned companies and companies based in Oman that will allow them to perform "landside aspects of port

[1] For the purposes of this memorandum, we will use the proposed Oman FTA's definition of "landside aspects of port activities," which includes "operation and maintenance of docks; loading and unloading of vessels directly to or from land; marine cargo handling; operation and maintenance of piers; ship cleaning; stevedoring; transfer of cargo between vessels and trucks, trains, pipelines, and wharves; waterfront terminal operations; boat cleaning; canal operation; dismantling of vessels; operation of marine railways for drydocking; marine surveyors, except cargo; marine wrecking of vessels for scrap; and ship classification societies." *See* Oman FTA, Annex II, *available at*, http://www.ustr.gov/assets/Trade_Agreements/Bilateral/Oman_FTA/Final_Text/asset_upload_file765_8833.pdf.

operations" at U.S. ports. Upon close inspection of the language in Annex II, however, it appears that this claim is misleading because it appears that Omani companies are already presently able to perform these services. Currently, there are no U.S. laws that prevent either an Omani-owned company (state controlled) or any other foreign-owned company (regardless of whether the company is state-owned or privately owned) from contracting with port owners to perform "landside aspects of port activities" in the United States. In other words, if an Omani-company (either state or privately owned) wants to engage in contract negotiations with port owners to provide for the types of services envisioned in Annex II, there is no U.S. law that would expressly prevent them from receiving said contracts.

Annex II of the proposed Oman FTA allows the parties to list "the specific sectors, subsectors, or activities for which that Party may maintain existing, or adopt new or more restrictive, measures" that are not in conformity with the various obligations imposed by the Agreement, such as National Treatment (Articles 10.3 or 11.2), Most-Favored Nation (Articles 10.4 or 11.3), and Market Access (Article 11.4).[2] With respect to the Transportation Sector, the U.S. Schedule to Annex II lists 12 types of measures that the United States has specifically reserved the right to either maintain or adopt new more restrictive measures.[3] These 12 types of measures generally reflect the current restrictions placed on foreign investment and/or ownership of maritime assets by U.S. domestic law.[4] Phrased another way, the United States has reserved the right to maintain our existing legal restrictions with respect to those aspects of maritime transportation in which we already have limitations, as well as adopt new measures in these categories that may be more restrictive.

Additionally, the U.S. Schedule indicates that we do not include in our reservations either "vessel construction and repair" or the "landside aspects of port activities."[5] The non-inclusion of these measures in our schedule merely indicates that the U.S. government is not reserving the right to impose a future restrictive measure with respect to "landside aspects of port activities." It does not appear possible to interpret this language as granting any type of new business opportunity to Oman or Omani based companies. Moreover, with respect to "landside aspects of port activities" the language in Annex II specifically states that the promised treatment "is conditional upon obtaining comparable market access in these sectors from Oman."[6] As a result of this language, it appears that the proposed Oman FTA does not grant any new opportunities for business investment to Oman that do not already exist, nor does it allow Oman to establish "landside aspects of port activities" unless it is determined that comparable market access is provided to U.S. companies in Oman. Indeed, in may be possible to argue that the language in Annex II in fact potentially limits the opening of U.S. markets with respect to "landside aspects of port activities" because it imposes a comparable access requirement that does not currently exist under domestic law.

Another argument raised in opposition to the proposed Oman FTA is that it provides a type of "pre-clearance" to businesses in Oman with respect to "landside aspects of port activities." It is unclear at this time precisely what the term "pre-clearance" means in this

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[2] *See* Oman FTA, Annex II, *available at*, http://www.ustr.gov/assets/Trade_Agreements/Bilateral/Oman_FTA/Final_Text/asset_upload_file765_8833.pdf.

[3] *Id.*

[4] *Id.* (listing the applicable provisions of U.S. law).

[5] *Id.*

[6] *Id.*

context. For the purposes of the memorandum, however, we will assume that this language refers to the national security review conducted by Committee on Foreign Investment in the United States (CFIUS). CFIUS, as you may know, was the executive branch entity responsible for reviewing national security and other implications of the Dubai Ports World transaction. U.S. law permits the President, at his discretion, to investigate the national security implications of "mergers, acquisitions, and takeovers ... by or with foreign persons which could result in foreign control of persons engaged in interstate commerce in the United States."[7] In addition, domestic law requires the President to conduct an investigation "in any instance in which an entity *controlled by or acting on behalf of a foreign government* seeks to engage in any merger, acquisition, or takeover which could result in control of a person engaged in interstate commerce in the United States that could affect the national security of the United States."[8] The President, by Executive Order, has delegated the responsibility for these investigations to CFIUS.[9]

Based on our review of the proposed Oman FTA, there appears to be no provision that would amend, alter, or adjust this statutory process or its requirements in any way. As a result of the proposed Oman FTA, should a privately owned company in Oman seek to engage in the "landside aspects of port activities," a CFIUS review could still be performed at the discretion of CFIUS, pursuant to the statute. Similarly, should a company owned or controlled by the Omani government wish to engage in any "landside aspects of port activities" at a U.S. port, they would still, pursuant to U.S. law, be required to proceed through the CFIUS process and receive approval from the committee prior to beginning operations. The proposed Oman FTA appears to contain no language that would exempt Oman or Omani government controlled companies from these domestic legal requirements.

Finally, it has been argued that the proposed Oman FTA would allow so-called "shell corporations"[10] to be established in Oman for the purpose of benefitting from the FTA's provisions. For example, assume that Dubai Ports World (DPW), a company controlled by the government of Dubai, were to establish a store front in Oman for the sole purpose of taking advantage of the FTA's investment, market access, and national treatment provisions. Presumably, part of the incentive for doing this would be so that DPW could avail themselves of the investor-state dispute mechanism should their attempts to do business in the United States be denied. The argument against the proposed Oman FTA assumes that the United States would either have to grant DPW access to the U.S. market or face considerable costs in defending our denial of market access. Should the government deny market access, the ensuing litigation could result in an adverse decision costing taxpayers a substantial amount of money in compensatory payments to Dubai.

A careful review of the text of the proposed Oman FTA, however, indicates that this scenario is unlikely to develop. Specifically, Article 10.11(2) addresses this concern by stating that a"Party may deny the benefits of [the Investment Chapter] to an investor of the other Party that is an enterprise of such other Party and to investments of that investor ***if the***

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[7] 50 U.S.C. App. § 2170(a) (2000).

[8] 50 U.S.C. App. § 2170(b) (2000) (emphasis added).

[9] *See* Executive Order 1266, *reprinted at*, 54 Fed. Reg. 779 (Dec. 27, 1988).

[10] A "shell corporation" is defined as "a corporation that has no active business and usually exists only in name as a vehicle for another company's business operations." BLACK'S LAW DICTIONARY, 344 (7th Ed. 1999).

***enterprise has no substantial business activities in the territory of the other Party*** and persons of a non-Party, or of the denying Party, own or control the enterprise."[11] Thus, the proposed FTA, by its own provisions, clearly permits the United States to deny benefits under the Investment Chapter to any company or individual unless there are "substantial business activities" established in Oman. Therefore, it appears that the establishment of a mere "shell corporation" would likely not be considered the establishment of "substantial business activity" and, as a result, the United States would be entitled to deny benefits.

This legal position is consistent with administration positions regarding substantially similar language contained in other FTAs. For example, in the Statement of Administrative Action that accompanied the North American Free Trade Agreement, the executive branch stated that "shell companies could be denied benefits but not, for example, firms that maintain their central administration or principle place of business in the territory of, or have a real and continuous link with, the country where they are established."[12] This language appears to establish a very high threshold for "substantial business activities" by requiring both central administration and principal place of business in the country before benefit can be claimed. Given this interpretive language, it does not appear that DPW, or any other foreign corporation, would be able to satisfy such requirements through a "shell corporation." In addition, for Oman to obtain any of the benefits listed in Annex II with respect to "landside aspects of port activities" they will, as previously discussed, have to provide "reciprocal market access" or else the United States has an additional legal basis to deny market access to Omani companies.

[11] Oman FTA, Art. 10.11(2), *available at*, http://www.ustr.gov/assets/Trade_Agreements/Bilateral/Oman_FTA/Final_Text/asset_upload_file976_8810.pdf.

[12] North American Free Trade Agreement, Texts of the Agreement, Implementing Bill, Statement of Administrative Action, and Required Supporting Statements, H.Doc. 103-159, 103d Cong. 1st Sess., 145 (Nov. 4, 1993).