

The Rule of Law and ASEAN growth

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It is widely accepted that the Rule of Law is critical for continued development in Southeast Asia. What does it really mean, and how does it affect growth and investment? While there are a range of views on how the Rule of Law can be conceptualised and measured, it is clearly one of the most critical conditions for sustainable economic growth, political stability and economic rights for citizens.

That said, high growth rates can and have been achieved in certain countries with poor implementation of the Rule of Law. Such occurrences are the exception, and it is very difficult to overcome the middle income trap without successful implementation of an economic, legal and political system based securely on the Rule of Law which includes the suppression of corruption and strong corporate governance principals.

What does become clear when reviewing the data is that the countries with the highest wealth (as measured by GDP) also score high on ease

of business, Rule of Law and corruption indices. Conversely, those with lower wealth indicators score lower on these indicators.

Singapore, for instance, ranks 5th in the world on wealth, 1st on ease of doing business, and 9th on the World Justice Project's Rule of Law Index, which takes into account factors such as the absence of corruption, open government, order and security, regulatory enforcement, civil justice and criminal justice. Unsurprisingly, Singapore alone accounts for around 50% of all inbound ASEAN Foreign Direct Investment (FDI). A large amount of this FDI ends up flowing through to other ASEAN nations as investors use the city state as an intermediary, taking advantage of the added regulatory protections that an advanced Rule of Law offers. While growth is dependent on a number of factors, an established Rule of Law significantly contributes to investor confidence.

ASEAN countries have been turning their attention to these issues for the past five to ten years with varying degrees of success. A number of

commentators have recently been asking whether ASEAN itself should take greater steps to encourage and promote this process within its member states. This article looks at ASEAN measures related to the Rule of Law and what the future may hold.

Rule of Law

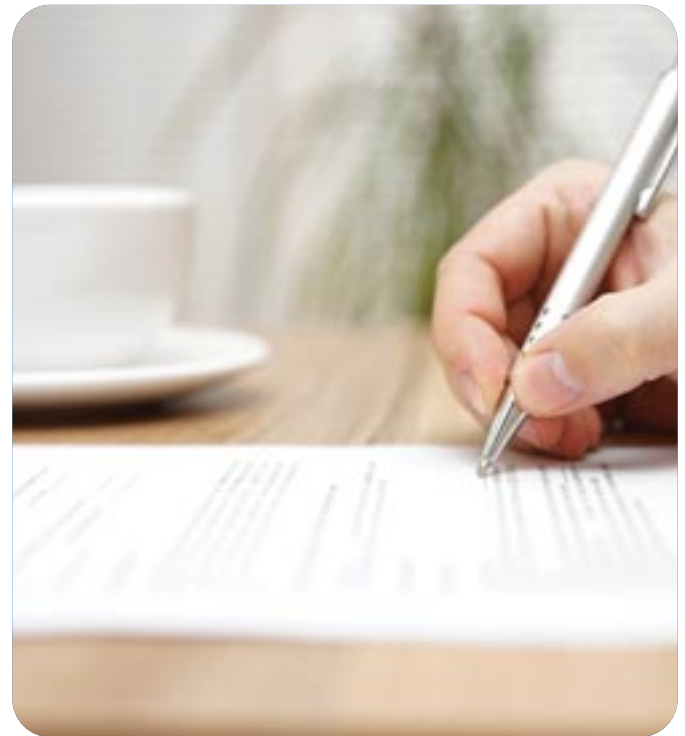
There is a spectrum of approaches to conceptualising the Rule of Law. At one end is a 'formal' list of key prerequisites, at the other a broader, more 'substantive' understanding that adds qualitative elements and assesses the content of the law. A combination of the two approaches yields the four fundamental pillars of the Rule of Law:

1. Government and its officials are accountable under the Law;
2. Laws are equitable, clear, published and fair, protecting fundamental rights;
3. The process by which laws are enacted, implemented and enforced is transparent, fair and efficient; and
4. Justice is accessible to the public and judicial officials are competent, independent and ethical.

Based on this definition, the key ingredients of a Rule of Law based system is reduction in corruption, protection of economic rights and good corporate governance (both private and public).

ASEAN: The early years

The Rule of Law has been a key pillar of ASEAN from the beginning. Officially inaugurating ASEAN in August 1967, the Bangkok Agreement was a two page list of shared aspirations that required no ratification by its signatories. In the context of a growing fear of communism and existing regional distrust due to prior military confrontations, a key purpose expressly stated by the fledgling body was the promotion of



regional peace and stability through abiding respect for justice and the Rule of Law. Other ambitions included the expansion of trade and the raising of living standards.

The Agreement was quintessential of the so-called 'ASEAN Way': a non-binding understanding reached through the consensus of a diverse group of nations that ensured little to no erosion of their individual sovereignty. While justice and the Rule of Law was a worthy aspiration, it was by no means a requirement imposed on members. The evolution of ASEAN was intermittent over the ensuing decades, mostly consisting of a handful of practical trade measures that carried limited legal obligations. Such agreements included the 1977 Agreement on ASEAN Preferential Trading Arrangements, 1981 Basic Agreement on ASEAN



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Industrial Complementation, and 1987 Agreement for the Promotion and Protection of Investments.

The ASEAN Way approach to integration initially saw limited progress as member states relied largely on consensus building and sought not to pressure each other (or themselves) into legally binding standards. It was not until the signing of the ASEAN Free Trade Agreement (AFTA) in 1992 that member states were faced with significant obligations to ratify a clearly defined framework in their respective legislatures. Since then, a proliferation of agreements have been formalised that required substantial ratification and implementation by each member state. This process began to stimulate the development of the Rule of Law following certain norms within member states, albeit almost exclusively related to economic and trade matters.

One can contrast the original ASEAN Way approach with the binding requirements for accession to the World Trade Organisation (WTO), now ratified by all ASEAN member states, requiring parties to promulgate a whole range of laws and regulations to be accepted into the WTO club. This has contributed to substantial improvements to the Rule of Law, especially in the less developed ASEAN member states.

The ASEAN Charter

Adopted in November 2007, the ASEAN Charter represents a significant paradigm shift in the approach to integration, including promotion of the Rule of Law. Although the Charter tends to focus on diplomacy and does not necessarily do away with the ASEAN Way of consensus, it does

outline a number of binding elements and important goals. The goals laid down for the ASEAN member states will have serious ramifications for the region as they are implemented.

One such goal relating to the Rule of Law is found in Article 1.7 of the ASEAN Charter which states that one of the purposes of ASEAN is to “strengthen democracy, enhance good governance and the Rule of Law, and to promote and protect human rights and fundamental freedoms”. While the Rule of Law is not specifically defined, this reference could be used by ASEAN policy makers to pursue a more substantive application of the Rule of Law among its members than under existing agreements. However, Article 1.7 also offers substantial leeway for interpretation, adding the caveat, “with due regard to the rights and responsibilities of the Member States of ASEAN.”

ASEAN Secretary General, Le Luong Minh, acknowledges that while core elements of the Rule of Law should include substantive elements such as equality before the law, “the application of this concept into national political systems and legal structures varies greatly according to the specific contexts and capacities.” Although the ASEAN Charter offers a useful framework for each of its member states to take into consideration, it is effectively up to each state to decide how they should adopt and observe the Rule of Law.

The AEC and the Rule of Law

While the ASEAN Economic Community (AEC) requires certain changes to domestic legal systems in order to improve trade and investment

among ASEAN members, it imposes only a limited number of obligations related to the Rule of Law. Article 9 of the AEC Blueprint states that ASEAN will establish a single market and production base through the free movement of goods, services, skilled labour and capital. The AEC effectively consists of a series of agreements to address these goals, including the ASEAN Trade in Goods Agreement (ATIGA), the ASEAN Framework Agreement on Services (AFAS) and the ASEAN Comprehensive Investment Agreement (ACIA).

Perhaps the most significant of these agreements from a Rule of Law perspective is the ACIA which came into effect in 2012. This agreement requires modification of domestic legal regimes in order to liberalise investment regimes, protect investors, ensure transparency of investment regulations and promote the region as an investment destination. Regulatory transparency and the protection of investor rights are, of course, key components of a Rule of Law based society.

There are a number of specific elements in the ACIA that address Rule of Law issues. Articles 5 and 6, for instance, provide most favoured nation treatment for investors and investments from other member and non-member states. These provisions are intended to target the Rule of Law components of equity and fairness. Articles 13 and 14 ensure that capital can move freely across borders and that investments are not expropriated without due process, addressing fair judicial process and economic rights. In addition, Article 21 provides that member states must make laws and regulations publicly available in order to enhance transparency. This is perhaps the strongest Rule of Law provision in the Agreement, targeting transparency through the publication of laws.

Judiciary and dispute mechanisms

While a number of ASEAN agreements address resolution of disputes through international or regional dispute resolution procedures, none contain measures that impose standards on judicial process, conduct or composition.

One such dispute mechanism is through the 1976 Treaty of Amity and Cooperation (TAC), which applies to disputes that are outside of ASEAN agreements and has been ratified by all member states as well as a number of key ASEAN trading partners. The TAC sets out that disputes should be settled through direct negotiation, with unresolved disputes referred to a High Council made up of representatives from all ASEAN member states as well as the states of the disputing parties. The High Council can then recommend an appropriate dispute mechanism.

Conversely, the ASEAN Protocol for the Enhanced Dispute Settlement Mechanism (EDSM) applies to disputes directly relating to ASEAN agreements. Confirmed in 2004, the EDSM procedure initially requires consultation between the disputing parties, followed by referral to a panel facilitated by the Senior Economic Officials Meeting (SEOM). Either party can appeal the recommendations of the SEOM panel to a body convened by the ASEAN Economic Ministers. The ultimate appellate body is the ASEAN Summit itself, made up of the heads of state, including those of the disputing parties.

The TAC and EDSM are closely modelled on the WTO dispute mechanisms. Unsurprisingly, several ASEAN member states have opted for the tried and tested WTO procedure in recent years, rather than utilise the TAC or EDSM. It is worth noting that all ASEAN member states are also party to the New York Convention which binds signatories to recognise foreign arbitration awards.

Finally, there is also an Investor State Dispute Mechanism (ISDM) under the ACIA. Similar to ISDM provisions found in many free trade agreements, a private investor is able to make a claim against a host state that breaches its obligations under the ACIA where that breach causes loss or damages. The investor must first seek conciliation before it can request formal arbitration proceedings. Arbitration can occur through a variety of forums, including an ASEAN regional arbitration centre, the courts of the host state in question, the International Centre for

Settlement of Investment Disputes (ICSID), or the United Nations Commission on International Trade Law (UNCITRAL). However, the ACIA provisions are only applicable to agriculture, fishery, forestry, manufacturing, mining, and related sectors. Like the TAC and EDSM, the ISDM provisions under the ACIA are yet to be utilised.

Anti-corruption measures

Reducing corruption is a critical measure for achieving sustainable growth and higher value FDI. Transparency International's Corruption Perception Index indicates mixed results for ASEAN member states, with some showing significant improvement while others languish behind. Although perceptions may not be directly related to the level of actual corruption in a member state, the index encourages governments to address corruption in order to improve their comparative advantage and the FDI that follows. In light of this evidence, and the AEC Charter's initial guiding principal to "... enhance good governance and the Rule of Law, and to promote and protect human rights and fundamental freedoms" it is surprising that no major ASEAN corruption initiative has taken root to date.

That does not mean that ASEAN member states are ignoring the issues. To the contrary, almost all have started their own intensified anti-corruption campaigns, including improving the anti-corruption legal infrastructure. Significantly, all ASEAN member states are now signatories to the United Nations Convention on Anti-Corruption (UNCAC), the most comprehensive and binding agreement of its kind. Accession to



UNCAC requires a commitment to implement specific laws and measures aimed at preventing bribery, embezzlement, abuse of power and trading in influence as well as corrupt practices in the private sector. UNCAC closely monitors implementation and offers assessment review, policy guidance and technical assistance to member states in order for them to ratify the agreement.

In addition, the Asian Development Bank (ADB)/OECD Anti-Corruption Initiative has been signed by all ASEAN member states, with the exception of Brunei, Lao PDR and Myanmar. Offering further policy analysis, dialogues and guidance to its 31 signatories, implementation of the UNCAC is a key priority of the initiative. As such, it is an important additional plank to combat corruption through the implementation of measures that reinforce the Rule of Law.

Corporate governance

Through its focus on anti-corruption, legal compliance and stakeholder rights, good corporate governance can also be a significant contributor to the creation of a society based on the Rule of Law and the reduction of corruption. In addition to good governance codes originating from corporates themselves, ASEAN member states have also embarked on some significant initiatives.

One of the most notable is the path taken by Thailand after the 1997 Asian financial crisis in order to significantly improve good governance within its listed and private companies. A raft of reforms were passed in the aftermath of the crisis to improve the rights of minority shareholders, strengthen the role of company audit committees, increase oversight of financial institutions by the Bank of Thailand and limit potential conflicts of interest on company boards, among others.

This has had a dramatic effect, catapulting Thailand to the lead of good corporate governance tables, including the ADB ASEAN Corporate Governance Initiative, which conducts annual surveys of the top listed companies in each member state and produces an annual scorecard based on the results. The scorecard reports assess the following OECD Principles of Corporate Governance:

- A. Rights of Shareholders
- B. Equitable Treatment of Shareholders

- C. Role of Stakeholders
- D. Disclosure and Transparency
- E. Responsibilities of the Board

The 2013-2014 ASEAN Corporate Governance Scorecard covered Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam, indicating specific achievements for each as well as recommendations for areas of improvement. As with the Corruption Perception Index, it is expected that such assessments will provide guidance and encourage governments and corporations alike to adhere to principles of good corporate governance in order to improve the investment environment.

Conclusion

In short, the Rule of Law is a work in progress in ASEAN. While the Charter identifies it as a key component of the association, the various ASEAN agreements adopted since have resulted in little progress in bringing Rule of Law issues into the ASEAN mainstream. Meanwhile, a variety of concurrent international agreements and domestic laws have filled the gap to some degree. ASEAN policy makers are now considering whether they should focus more directly and robustly on Rule of Law issues, including anti-corruption. The steps taken in improving corporate governance are certainly significant and perhaps similar initiatives against corruption will gain momentum in the near future.