IWOGDA

POLICY BRIEF*

Multilateral Framework on Investment

Introduction

In the past decades, the significance of foreign direct investment (FDI) as a tool for economic growth and development has received increasing attention. FDI has been recognised as a source of finance, a principal channel for transfer of technology and managerial know-how, a tool for increasing productivity and expanding productive capacity, to create export potential and improve competitiveness in the international market.

However, developing country experiences have also shown that FDI sometimes fails to generate the expected positive impact on the host economy. The net effect on gross domestic investment, employment creation, environment and sustainable growth and development of the host economy depends largely on FDI-related policies of the host government, regulatory oversight and attractiveness of the investment climate offered.

Proponents of a multilateral framework on investment (MFI) have argued for a multilateral accord to ensure and strengthen the protection of the rights of the foreign investors in the host countries and to curtail the role of the host government in putting conditions on their entry and operation. This according to them will facilitate greater flows of FDI to developing countries (DCs). However, DCs have argued that FDI will, in practise, contribute to development objectives only if multilateral rules allow for *national policy space* to effectively regulate and channel FDI into areas of interest to their economy.

Further, it is argued that proponents of an MFI have not attached adequate importance to the need for international investment rules to curb those actions by governments that very often lead to wasteful competition among the governments to attract FDI (e.g., government tax breaks and subsidies).

The Doha Declaration, signed at the WTO Ministerial Meeting at Doha in Nov 2001, mandates the Members to "focus on the clarification" of certain identified elements in respect of a potential MFI before "negotiations…take place after the Fifth Session of the Ministerial Conference on the basis of a decision to be taken, by explicit consensus, at that session on modalities of negotiations."

The prime aim of this policy brief is to analyse the elements identified in the Doha Declaration for a potential MFI. These issues/elements have been discussed in synoptic tables later in this paper, which cover all elements of a potential MFI discussing the proposals for each element, their implications for development, the issues that need further discussion and the way forward.

The main negotiating issues with regard to a potential MFI are:

- The need for MFI and its appropriateness in the WTO framework.
- Modalities/nature of negotiations; WTO's General Agreement on Trade in Services (GATS)-style or opt-outs.
- The application of WTO principles such as non-discrimination to investment.

*This policy brief has been prepared by CUTS under its new programme: International Working Group on the Doha Agenda (IWOGDA). IWOGDA is another initiative of CUTS Centre for International Trade, Economics & Environment, Jaipur (www.cuts.org) which seeks to examine the various agenda items under the Doha Declaration of the WTO. It engages researchers and experts from developing countries and prepares synthesised inputs for negotiators. In the 1st phase the programme has undertaken the two issues of competition policy and investment framework as likely negotiating agenda to be launched at the Cancun Minsiterial Conference. The programme has been supported by the Governments of the Netherlands, Sweden and the United Kingdom.

Pros of an MFI

Firstly, it is widely believed that the existing scenario in terms of international investment agreements is not quite satisfactory from the viewpoint of DCs. Many DCs have conceded (and are still conceding) major concessions to industrialised countries (ICs) in bilateral and regional settings. Collective bargaining can give more strength to DCs with similar agenda, as compared to individual bargaining for BITs. If there are multilateral negotiations on investment regulations, some DCs will gain from taking a common stand with other DCs. In addition, the transaction costs will be lower in an MFI, as compared to any non-multilateral setting.

Secondly, incentive bidding where DCs outdo each other by offering the most beneficial investment incentive packages, can only be addressed in a multilateral framework.

Thirdly, multilateral negotiations are believed by some to come under more scrutiny from, for example, civil society actors, as compared to bilateral negotiations, which are unlikely to attract much attention. Transparency of home regulation can thus be enhanced.

Fourthly, a multilateral agreement is more likely to come under regular review, especially if applying a uniform dispute settlement mechanism. A comprehensive set of consistent rules among all WTO Members is believed to provide for a stable, transparent and consistent environment for firms operating in the global market, whatever their ownership structure or place of incorporation.

Cons of an MFI

Primarily, calls for an MFI raises the fear that the resulting liberalisation of foreign investment will reduce national sovereignty by limiting the regulatory and promotional capacity of governments to address development challenges.

Secondly, an MFI would have such a wide reach and involve so many countries that there is a fear that it would result in codification of international customary law, and thus bring in place a certain kind of international investment regulation, long resisted by the developing world.

Thirdly, multilateral fora like the WTO are biased toward free trade and not likely to consider development goals as a priority. A "one size fits all" multilateral framework might give less scope to accommodate differences between countries at different levels of development. This disadvantage can possibly be reduced by providing for country-specific exceptions and special and differential treatment for DCs.

Fourthly, sanctions in a multilateral setting, such as trade restrictions, can be much more deleterious in a multilateral setting than in a bilateral or regional setting.

It is worth noting that once a multilateral agreement is signed it will be hard for any one country to get out of it as opting out of it would mean opting out of the entire WTO regime.

Some other concerns

The main objection against having an MFI in the WTO, as argued by its opponents, is the very inappropriateness of an investment agreement at the WTO. The adoption of GATS-style of negotiation in terms of progressive liberalisation and application of core principles of non-discrimination has convinced the opponents that irrespective of what proponents state, the MFI is more of a liberalisation instrument.

Moreover, in recent years, there has been a phenomenal increase in the cross-border flow of capital, without any multilateral framework. The year 2001 saw a downward trend in this regard but interestingly it affected FDI flows mostly to ICs. Countries are liberalising unilaterally to create a more investor-friendly environment. The principles developed by some international bodies in this regard can indeed help such unilateral liberalisation and an MFI is redundant[1].

1 Principles for a fair agreement on investment have been developed by the UN Expert Working Group (UNCTAD Commission on Investment and Related Financial Issue, 1 Oct 1997, "*Criteria for the development friendliness of investment frameworks*", Geneva: UNCTAD 28-30 May 1997.) These it is claimed could form the basis for a set of core principles and an eventual agreement on international investment. Other rules include UNCTAD's Rules for Control of Restrictive Business Practices and OECD's Guidelines on MNEs. In the same vein, the UN Sub-Commission on the Promotion and Protection of Human Rights has been mandated to develop a code of conduct for companies based on human rights standards including draft principles (standards, liability and redress).

Secondly, the non-transparent operating culture of the WTO is such that its rules are developed, interpreted and applied in a way that often excludes those countries and interests seeking to develop appropriate developmental and environmental policies. Moreover, DCs in the WTO are quite weak and easily manipulated by pressure and green room deals to develop and hold a common front.

Thirdly, the non-discrimination principles proposed for the MFI is expected to parallel GATS'. As it is, DCs have no capacity to understand precisely which sectors to open up and which types of limitation and exceptions to put under each sector so that a country is not economically, socially, or politically harmed. The bilateral services negotiations require an extensive understanding of the various economic sectors, something that DCs are still lacking in. An MFI would simply add on to the already burdensome process and detract the Members from more pressing issues. Moreover, the process will require an understanding of how certain commitments will impact constitutional and legislative mandates as well as domestic regulation in each country.

The impression emerging from the WTO Working Group discussions pertaining to the MFI proposal can be summarised as follows:

1. Most countries are adopting an attitude of wait and see – first gauging how the countries react to the proposals that have been discussed so far, before adopting a position.
2. Countries are still struggling to understand what are the contours of an MFI and its implications of the MFI on their national development and industrial policies.

The following synoptic tables provide brief discussions on the various elements/issues pertaining to the proposed MFI as identified in the Doha Declaration. It also considers some proposals not identified in the Declaration but brought up by some Members at the WTO Working Group on Trade and Investment.

Scope and Definition	
What is proposed	Focus is on the definition of the terms "investment" and "investor" and the relationship between the two. Two main proposals: 1. Limit investment to FDI which in essence means the adoption of an enterprise-based definition i.e. controlling interest in the business enterprise. 2. Broad asset-based definitions with options to narrow it down.
What they mean	1. The narrow definition will affect establishment, operation and exit of FDI only. 2. The broad asset based approach would include every kind of asset including property and property rights, direct and portfolio investments, contractual rights (service agreements), IPRs, reinvested earnings, and business concessions; similar to NAFTA's.
Development implications	1. Narrowing the scope to FDI in the MFI might make regulation in public interest easier due to its long-term nature. This may take into account both host and home country interest in a balanced manner. 2. Due to the missing element of certainty in a broad-based approach: (i) Its open ended nature may commit countries to forms of investment protection they never contemplated (because of the evolving nature of capital markets). Though flexible in coverage, it may restrict their development policies and limit policy options. (ii) Too broad a definition may make it impossible to understand the implications of the substantive provisions proposed (as in the failed MAI). (iii) Inclusion of short-term investment has the potential to create capital volatility in the event of economic turbulence. (iv) Including footloose capital, which is not sector specific, may be difficult in light of the positive list approach of negotiations.
Issues for further discussion	1. When relying on tests of ownership and control, need to clarify the criteria of determining: • long term relationship between investor and the investments • the size of investments • the sector • use of definitional clause to delimit subject matter • duration that can be considered long-term • management control • flow of funds • methodology of industrial classification 2. Consider limitations based on the country's industrial development position. There should be a study of factors underlying the absorptive capacity of countries at different levels of development for FDI to be extremely relevant. 3. Potential benefits of green-field investments v. the acquisition of existing enterprises (UNCTAD study has shown that adverse effect is likely in M&As) 4. Are standards of protection of investment included? NAFTA is the best example of what could go wrong with the adoption of a broad based approach. It was one of the reasons for MAI's failure.
Recommendations	1. It may be well to consider having the definition in the operative provisions as the narrow based approach may also lockout room for compromises. 2. Instead of blindly including IPR provisions in the agreement, advantages that can be gained through transfer of technology (TOT) should be taken into consideration. 3. Australia's suggestions of a review of the development implications of the MFI and a dual approach to investment protection: broad asset-based approach for investment protection and narrower transaction or enterprise-based approach for cross border investment liberalisation agreements.

Core Principles	
What is proposed	1. Extend the application of all the core principles (MFN, NT, and transparency) to both investors and investment. 2. Does full NT/MFN apply or a certain degree of flexibility is essential to permit state regulation?
What they mean	These are to reinforce the core WTO objective of protecting the competitive process and setting standards for the treatment of foreign investment/investors across nations.
Development implications	Full application of the principles to both investors and investment will guarantee free flow of international investments. This might affect government sovereignty in policy making in economic, social and political spheres.
Issues for further discussion	Should minimum treatment standards ("fair and equitable treatment" etc) like those found in some IIA's be included in a multilateral agreement? In most BITs, investment is granted national treatment, while investors are accorded only MFN treatment. It may be interesting to see how this arrangement has worked.
Recommendations	Should allow for limited exceptions, retain right to regulate by performance requirements and allow selective liberalisation and right to discriminate. Could also consider basic minimum standards and broad definitions for effective compliance rather than a broad framework.

Most Favoured Nation (MFN)	
What is proposed	Apply as a general principle.
What they mean	Means that foreign investment/investors are required to be treated equally irrespective of their nationality.
Development implications	No major disagreement among countries in this regard. However, it has been pointed out that it may not be possible to adhere to the MFN principle in all circumstances.
Issues for further discussion	Will granting MFN really help in attracting investment? Whether GATS-type MFN exemption can be considered ?
Recommendations	Should have some flexibility to give preference to investments from particular countries based on past experiences, cultural and historical ties etc.

National Treatment (NT)	
What is proposed	Apply as a general principle. Alternative proposal is that it will depend on: • beneficiary; • scope; and • stage of admission. Or, apply as general obligation unconditionally in the post-establishment phase.
What they mean	Members are obliged to grant foreign investors/investments treatment equal to the one granted to their domestic equivalent.
Development implications	Full NT places a foreign investor on equal footing with national investors, removing the means by which a host country supports and protects its domestic investors. In IIAs NT in the post establishment stage is accepted as a general obligation. However NT in the pre-establishment phase, in effect, is a market access commitment, and an uncommon feature in IIAs.
Issues for further discussion	Equal treatment to foreign investors might actually mean more than equal treatment as the domestic companies may have to adhere to some additional regulatory requirements which may not be relevant to foreign companies. Should it include performance requirements?
Recommendations	Should have enough flexibility to impose performance requirements. Otherwise will have a situation like in Mexico where their export processing zones though successful export wise, are characterised by very low levels of value addition (less than 2%), weak national linkages, dependence on foreign capital and imported technologies, and over-reliance on cheap labour.

Transparency	
What is proposed	Core obligation is to make all relevant information publicly available. Scope will depend on: (i) substantive provisions-what do the provisions apply to and who is responsible, and (ii) purpose – whether the information has relevance to investment.
What they mean	Members are obliged to provide sufficient information to determine whether or not obligations are in fact being met. Also may require that the administration of rules be reasonable and non-discriminatory. In the WTO, it is more important and detailed in areas with wider government discretion
Development implications	There is a conceptual difference in treatment of transparency by the WTO and IIAs. The laws/regulations relating to investment are more extensive than for trade and cover wide areas of public policies. This inevitably means technical and capacity constraints in complying with the proposed transparency obligations. Particularly the need to ensure they are administered in a uniform, impartial and reasonable manner, which introduces the notion of external assessment.
Issues for further discussion	Investment is related to almost all areas of government policy regime, it will be difficult to identify which of these will be required to be notified. Hence, attempt may be made to identify some important areas to avoid confusion and dispute at later stages. Since, BITs are largely silent about it, experiences with existing transparency requirements at the WTO can be good learning points.
Recommendations	Should be limited to easy availability of the relevant rules, procedures and decisions. It should not transgress into substantive areas of decision-making process. Strive to enhance transparency but without creating unnecessary burden, especially on DCs.

Fair and Equitable Treatment	
What is proposed	Not included in the Doha Agenda but has been a subject of discussion. May be proposed as a compliment to NT/MFN.
What they mean	The possible options may be a commitment: • where countries should offer investment FET (the hortatory approach); • that legally requires countries to accord investment 'FET', 'just and equitable' treatment, or 'equitable' treatment; and • in which FET is legally accorded to investment together with other standards of treatment, such as MFN and NT.
Development implications	The FET, which is a vaguely defined standard, is inherently subjective, and therefore lacking in precision. Moreover, difficulties of interpretation may arise because even in its plain meaning, the concept does not refer to an established body of law or to existing legal precedents.The uncertainty and the potential obligations would prove too burdensome for countries. A high standard of treatment may be expensive to provide for in many DCs at different stages of development and with different policy regimes.
Issues for further discussion	Whether a minimum treatment standard would facilitate development in poor countries. It may be good for both domestic as well as foreign investors.
Recommendations	Most problematic proposal. It would probably be better for countries to omit reference to FET in an MFI.

Nature of Commitments	
What is proposed	1. Should it apply to pre- and post entry phase or only post entry? 2. GATS-type positive list approach in both pre- and post establishment phases.
What they mean	The GATS-type approach is meant to grant DCs flexibility to implement treaty provisions through selecting the areas in which they wish to make commitments. Provides means to determine: • stage at which MFN/NT are granted; • categories of investment for commitments, economy wide or sectoral approach; and • selection process: ad hoc, systematic or open door?
Development implications	Though in theory a country is free to select the sectors to commit, in practice its commitments including choice of sectors will be the result of a series of bilateral and plurilateral negotiations with other countries, in particular major industrialised countries. Thus DCs will be under intense pressure to commit sectors, which they would rather not. The flexibility will allow countries to address their development objectives in terms of favouring domestic investors in specific sectors or in sectors of crucial importance for development, sectors with strategic significance as national security.
Issues for further discussion	How to structure the treaty to mirror the economic differences among members? If a GATS-style approach does not give DCs maximum flexibility, what is the other option? What is the case for binding commitments on NT in a pre-establishment phase (market access) at a multilateral level as compared to unilateral market liberalisation? General exceptions are uncommon in most IIAs but common in trade agreements. Should such exceptions be included?
Recommendations	Bottom-up agenda that allows countries to liberalise selectively and gives more weight to differences in asymmetry in development levels between countries. Must be remembered that most IIAs do not include automatic right of admission, except in US-type BITs.

Development Provisions	
What is proposed	Should have adequate flexibility so that DCs can channelise FDI to sectors and areas that will facilitate development in the country.
What they mean	This may result in higher investment in areas of priority and may also ensure technology intensive FDI. However, it could simultaneously lead to strengthening the case for stronger IPRs.
Development implications	Will allow countries to continue with their affirmative action programmes like black empowerment in South Africa or such actions to address regional imbalances in economic development. Development provisions in the agreement might allow countries to adopt appropriate policy instruments to bring technology along with FDI.
Issues for further discussion	Rising FDI flows are not necessarily accompanied by ToT. Moreover, DCs only get low-level type of technology. Of what use would the development provisions be in remedying the technology constraints faced by DCs?
Recommendations	Ensure that MFI is not an instrument of liberalisation and protection of investment as opposed to one for promotion of investments (to DCs). Confer promotional measures such as technology and technical and financial assistance, and must specify the means to promote TA and advice.

Special & Differential Treatment (S&DT)	
What is proposed	Types of S&DT: • phased-in periods of compliance with focused technical assistance; • Permanent "carve-outs" (exemptions) from any obligation regarding admission of FDI; • Right to use performance requirements, investment incentives, etc. Provide for exceptions and temporal derogation to the treaty obligations under special circumstances.
What they mean	• BoP safety valves The exceptions can be: • systemic exceptions for certain measures (e.g. procurement, taxation); • general exceptions (public interest and for regional economic integration agreements) ; • country-specific exceptions (which are exceptions to a general rule or commitments to a conditional rule).
Development implications	The present WTO system, has relied mainly on transition periods, broadly 5 to 10 years, for DCs after which all Members are considered "equal under the law". However, even after such periods of time, it is quite obvious that a level playing field will not be achieved and equal rules will come to apply to unequal players. Too much emphasis on the so-called S&DT provisions may detract DCs from wider interests and as a result they may not explore the opportunities in a proactive manner. There is also a fear that differential treatment in favour of the DCs do not provide real or stable safeguard.
Issues for further discussion	Many of the S&DT provisions in the present WTO arrangement are rather symbolic and do not serve much of real purpose, in terms of granting greater market access. In order to have a targeted approach, some S&DT provisions should be identified which can bring real benefits to the DCs. Another aspect that can be considered is that they should be easy to implement and at minimum cost.
Recommendations	Should consider S&DT of a more structural nature that will automatically promote more of development-enhancing FDI (like greater market access in trade) to DCs. It should be recognised that S&DT provisions for DCs should exist and operate as a matter of right rather than privilege. S&DT should not be bound in time frames but be flexible subject to a review process to determine the conclusion of time period which can be benchmarked on development indicators.

Technical Assistance	
What is proposed	• Policy analysis and development; • Human resources capacity-building; and • Institutional capacity-building.
What they mean	Technical assistance might help countries to understand the issues before and during any negotiations on investment. It may also help them to create a policy environment compatible with their commitment in the MFI.
Development implications	If the technical assistance can be suitably utilised to create a development oriented investor-friendly environment then it will help the countries otherwise as well, even if they do not receive much of FDI. However, if the promised technical assistance does not come through, DCs will find it difficult to cope with the commitments made in the agreement.
Issues for further discussion	Whether provisions can be made to ensure that the actual fulfilment of the commitments made is contingent upon the actual receipt of technical and other types of assistance.
Recommendations	Technical and financial assistance in the areas of trade and investment cannot be delinked from other areas of socio-economic development. An overall development of an economy will make a country better able to fulfil its commitments made at the WTO. Hence capacity building aid in the area of trade and investment should not be at the cost of development aid. Secondly, TA needs to be tailored to need-based requirements.

Balance of Payments (BOP)	
What is proposed	• Need exceptions from disciplines when host countries face BOP problems. • Be patterned after TRIMs BOP exceptions and take into consideration similar GATT provisions.
What they mean	If a developing country has full discretion and flexibility about putting conditions on entry and operation of FDI, it will not need exceptions and BOP safeguards. But if such flexibility is lost within the MFI, a need will arise to include BOP safeguard measures.
Development implications	In the short run FDI inflows improve the BOP position, but in the long run, as the repatriation of profits starts increasing, the situation may worsen.
Issues for further discussion	Current GATT BOP exceptions are inadequate for DCs. What could be the alternative?
Recommendations	Are BOP restrictions a "self-defeating strategy" in the long term given that right to free transfer of capital is crucial especially at the time of high current account deficit? Countries may be allowed to impose higher taxes on repatriated profits.

National Policy Space	
What is proposed	An MFI will have substantial implications for national policy space. The standard of protection to investors may also have implications for national policy space.
What they mean	With greater market access and higher commitment to foreign investors, it is widely felt that national governments will be left with much smaller space in terms of national policy making. NAFTA allows firms to sue governments over the latter's policies that are said to have reduced or eliminated "profits, current and future," including through the concept of "takings" (unlawful deprivation of private property).
Development implications	Shrinking national policy space means that national governments will have little manoeuvrability to manage their economy in line with their development priorities. Expropriations and compensation rules, such as right to regulate for environment protection, would be difficult to enforce (e.g.,Metalclad). Since DCs are yet to put in a basic regulatory framework in place, they are likely to bring in relatively more such measures in the future and they will face more such problems if NAFTA type protection standards are adopted.
Issues for further discussion	DCs need to go beyond the GATS in respect of issues such as performance requirements, as these are important policy instruments to pursue development objectives and to promote domestic industry. The concept of regulatory 'takings' or the related concepts of 'indirect expropriation' and a 'measure tantamount to nationalisation or expropriation' are not clear enough even in advanced jurisdictions.
Recommendations	Need to find the right balance between rules and disciplines on market access and protection of investment in the WTO and safeguarding the national sovereignty and control over one's own economy. The policy choice of governments to privatise public entities should be reinforced. As the relevant concepts are not clear enough, inclusion of such provisions may create problems especially for DCs. Moreover regulatory measures are often enforced at the sub-national and local levels where the capacity to comprehend such issues would be even lower. Regulatory measures should not be linked to the protection of investment unless they are discriminatory in nature.

Dispute Settlement Mechanism	
What is proposed	Should it be a binding provision, and if so who is permitted to use it? Introduce a compensation/fine-based system. Consider provisions for investor-state disputes.
What they mean	The WTO's DSM includes only compliance; compensation is voluntary. Moreover, retaliation is only generated unilaterally by the winning party. A compulsory fine or compensation based system may be more effective and egalitarian.
Development implications	DCs' power to retaliate is doubtful. Hence such a retaliation based dispute settlement mechanism would be against the interests of DCs. Foreign investors may get more than equal treatment as domestic investor will not have the right of action in an international forum against its own country.
Issues for further discussion	Retrospective remedies are available in international investment arbitration. It may be considered that to what extent similar provisions can be made in the MFI at the WTO. The possible implications of introducing investor to state issues at the WTO dispute settlement. Peer review as an alternative to the DSM.
Recommendations	May restrict dispute settlement to state to state. Investors should not have any role as it might complicate the situation and the implications are not yet clear either. They may approach the international forum through their governments, as is done usually in the WTO of framwork.

Relationship with other WTO Agreements, BITs, and RIAs	
What is proposed	The MFI should take note of the existing WTO Agreements: • TRIMs- prohibit negative incentives; • GATS- includes FDI through mode 3: "commercial presence"; and • TRIPs- has implications for FDI in general and transfer of technology through FDI in particular. BITs: • US model- disciplinary provisions are of higher level, core principles apply at pre-and post-entry, and provide for investor-state dispute settlement. • European model-more traditional, standards apply only at the post entry stage.
What they mean	Would TRIMs be incorporated in the proposed agreement on investment by reference? Or should its scope of prohibited practices be modified or further clarified? GATS involves quite a broad definition of investment and hence a narrower definition that most DCs would prefer in a potential agreement might be in conflict with GATS. The proposed MFI may also be in conflict with the existing BITs or RIAs depending on the kind of provisions it includes.
Development implications	The existing investment instruments at the WTO or BITs or RIAs, are often biased against DCs' interests. DCs may take stock of all these to ensure that an MFI if agreed ensures a better situation for them.
Issues for further discussion	What kind of impediments would the agreement address with respect to GATS, given that an overwhelming majority of investment restrictions arise in service industries rather than in manufacturing? If "due regard for other WTO provisions and existing bilateral and regional agreements" as mentioned in the Doha Declaration is interpreted as all such provisions or agreements taking precedence over the proposed MFI, then there will be limited scope for its application.
Recommendations	An MFI at the WTO will have much greater implications for the global community, especially the DCs. Hence, it needs to be balanced compared to the existing instruments at the WTO or BITs or RIAs, which are often biased against DCs' interests.

Investor Responsibility and Obligations of Home States	
What is proposed	This is not included in the Doha Agenda but has been proposed by some.
What they mean	This will require TNCs to behave and operate with full corporate responsibility and accountability in their operations in countries where they operate. In case of violation of law of the land in host countries the concerned home country government will extend necessary cooperation in taking appropriate action.
Development implications	Since many of the DCs find it difficult to take appropriate action against the mighty TNCs for irresponsible behaviour and violation of rules, such a provision in MFI will be beneficial for the DCs. This might also ensure that the TNCs do not take undue advantage of a weak regulatory framework in DCs. A case in point is the Union Carbide's irresponsible behaviour that led to the Bhopal gas disaster in India. The company could not be appropriately punished for its irresponsible behaviour. An MFI with such provisions could probably make the situation different.
Issues for further discussion	Could OECD Guidelines for MNEs serve as the starting point for developing a framework for this provision?
Recommendations	The MFI should oblige TNCs: • not to undertake restrictive business practices; • respect consumer and environmental protection standards abroad; • ensure total transparency in financial transactions and accounting; • not act in a manner prejudicial to the social norms and economic interest of host countries; • provide for international blacklisting of investors found in default.

Incentives Race	
What is proposed	This is also not included in the Doha Agenda but has been proposed by some.
What they mean	In their enthusiasm to attract more and more FDI, governments are offering higher incentives and lowering their regulatory standards, a phenomenon termed as 'race to bottom'. This has serious social, economic and environmental implications for the countries as well as the global community. An agreement to check such an incentive race would enhance global welfare as well as that of the individual countries.
Development implications	TNCs extract undue advantage while countries engage in a zero sum game of getting a bigger slice of the fixed FDI pie and collectively lose in the game. For instance, Chile and Costa Rica were in the race to win Intel's investment. However, the winner, Costa Rica, was able to offer an attractive incentive package including an 18-year "tax holiday", exemption of taxes on exports, imports and repatriated profits and subsidised employment, the incentives not available to domestic investors. But Costa Rica is now left with an investment, of admittedly enormous importance, from which it cannot raise revenue through taxes, and where local supply is not favoured as input imports are duty-free and employees cannot bargain collectively. Hence the potential gain from the investment is minimized by the cost of government incentives. A check on such a race will be good for collective welfare, especially for DCs.
Issues for further discussion	Balancing the TRIMs (which prohibits negative incentives) by regulating the use of "positive TRIMs" investment incentives.
Recommendations	At this stage it is indeed difficult to arrive at a set of global standards for regulatory framework for different areas or taxation regimes. Moreover regulatory requirements are also likely to be different in different countries. However, it may be noted in this context that many countries offer treatment to foreign investors in this regard, which is far better than that given to domestic investors. This can be stopped.

Different Country Positions on an MFI

Many DCs are not so enthusiastic about the idea of launching WTO negotiations on an MFI. They are rather adamant about certain issues, which are crucial to them, thus posing a challenge for the future of the discussions. For instance, to the main demandeurs of the agreement, EC and Japan, inclusion of the non-discrimination principle is very critical. But the DCs consider this as one of the main stumbling blocks of the MFI. Moreover, they would like to see issues of interest to them discussed in the working group and eventually form a part of the negotiations. However, the demandeurs are against the introduction of such issues, e.g. discussions on the obligation of the investors as well as the home countries obligations to enforce these obligations introduced by a group of DCs including China and India.

Unlike other countries, which seem ambivalent, India and Malaysia have been steadfast in their opposition to an MFI in the WTO. According to India, investment is not a trade issue, therefore it does not belong to the WTO. Moreover, India has consistently insisted that Members must discuss the movement of natural persons (labour) in any discussion on capital flows. Pakistan has also repeatedly stated that it remains unconvinced of the need for an agreement adding that it would weaken the bargaining position of host countries vis-à-vis investors. As far as it is concerned, this would merely add to the existing imbalance in the WTO against the DCs.

The EU and Japan have tried to placate India and Malaysia as well as other DCs by advocating an approach similar to that under the GATS. In their view, adopting this approach to investment would allow governments to open up areas where they want to attract foreign investors and exclude those considered too sensitive for political, economic, or developmental reasons. In general, DCs have not been supportive of this stance.

Most DCs are in favour of including a narrowly defined and long-term foreign investment i.e., FDI, in the possible MFI if there is to be one at all. This is considered more realistic and achievable as it is also more easily classified from a methodological and statistical point of view, which may be necessary while adopting a positive-list approach.

But the US is of the opinion that a broad-based and open-ended definition (which includes portfolio investment) and pre-establishment rights are necessary to maximize the benefits of investment liberalisation and protection. This can also contribute to the development agenda. Canada in turn would like to see a broad-based but long term approach for the MFI scope with an exhaustive list. It considers this as the best means of facilitating "common understanding". Australia is exploring the idea of having a narrower definition for entry (pre-establishment treatment), and a broader definition for post-establishment treatment, in part for consistency with BITs.

With regard to transparency, both DCs and ICs consider this to be an indispensable and integral part of the agreement but they differ in scope and reach.

Taiwan has been controversial by suggesting that Members should consider provisions for investor-state disputes through the dispute settlement system patterned after the Independent Entity Scheme for WTO Pre-shipment Inspection disputes. Most countries including Malaysia, Hungary, New Zealand, Hong Kong and China have objected to this proposal on the ground that it is beyond the Doha remit.

The Way forward

DCs need to take the following into consideration before negotiating an MFI at the WTO:

- They must be convinced of the importance of foreign investment to their economy first before considering the necessity of an MFI within or outside the WTO framework. Subsequently, if it is found important enough to warrant the need to regulate investment multilaterally, the existing frameworks and agreements should be explored.

- Most trans-border investment takes place among ICs while most of the international investment agreements are between developed and DCs. The only attempt at a multilateral framework among the industrialised countries, the Multilateral Agreement on Investment (MAI) at the OECD did not succeed. It is thus essential for DCs to carefully study the effects of the existing IIAs as well as the failed MAI process. The OECD MAI was actually targeted at DCs and a study of it might give some indication of the kind of problems/ issues countries might face in this context. In addition, DCs should consider negotiating regionally which will give them adequate experience to deal with the issue at a multilateral forum. For example, NAFTA has given substantial

experience to the north American countries and hence they are in a much better position to handle any multilateral negotiations.

- Within the WTO context, DCs should bear in mind that there is already a lot of unfinished agenda (most likely due to imbalances in negotiating strengths) which include services; addressing assessment of trade in services, autonomous liberalisation, implementation issues; agriculture; S&DT, market access for industrial goods, etc. Hence considering an MFI within the WTO, will overload the system.

- If the WTO proves to be a suitable forum for the MFI, then the DCs must analyse the economic, social and environmental impacts of such an instrument. The GATS, which in a sense, is the first such investment instrument, can provide a model for that. An in-depth analysis of the impact of GATS should be able to provide trade policy-makers with tools to develop a negotiating agenda and a set of policy options that can maximise the contribution of an MFI to sustainable development and minimise its potentially negative implications. E.g. Council for Trade in Services has service trade assessment as a standing agenda item.
  Such a sustainability assessment should include:
  - Quantitative economic effects
  - Social, environmental and human rights implications

- Theoretically, labour and capital movements play the same role in promoting efficiency. Thus investment liberalization can be balanced with equal commitments in labour mobility. The question remains however whether all Members will agree to such a proposition. If yes, then what will be the framework of such an accord?

- The GATS Agreement provides a model of what could go wrong if Members take on further commitments without weighing their future implications. The GATS Agreement has no commitment to undertake sustainability assessments at the national level to identify and address the economic, developmental and environmental implications of trade agreements and policies. Rather, the agreement merely "encourage[s] the voluntary use of environmental impact assessments". It would be sensible for countries to look at the bilateral avenues for negotiations in order to assess whether the GATS really provides a coherent approach to addressing the particular needs and circumstances of DCs.

- Any negotiation must include discussions for establishing obligations of investors and rights of host countries. A legally binding international framework on corporate accountability and liability should therefore be considered as a concomitant requirement for negotiations on an MFI.

- If the decision to go ahead with negotiation is taken, then the proposed MFI must include as per the paragraph 22 of the Doha Declaration:
  - A degree of flexibility with a development dimension that considers DCs -national policy objectives keeping in view their level of development Care has to be taken to ensure that the MFI does not result in the loss of a high degree of sovereignty for host governments in their policymaking. Article XX of GATT provides policy flexibility.
  - A balanced reflection of the interests of home and host countries
  - The right of the host country to regulate in public interest
  - The special development, trade and financial needs of DCs

- As regards the issue of checking the incentive race among the nations, i.e., balancing the TRIMs Agreement with provisions on positive TRIMs as well, a code of good practices can be annexed to it, as in the TBT Agreement. This approach can also be followed with regard to the obligation of the investors and the home countries. This can be a good beginning.

- Giving DCs a fixed transition period for implementation of MFI provisions might not be effective, given that DCs might take more than 10 to 15 years to reach the desired levels of development. Provisions of exemptions until the time DCs reach a certain level of development might be more meaningful.

- Many feel that a multilateral setting may be better than a bilateral setting as the earlier provides a more predictable environment. However, are all existing IIAs going to be abandoned once an MFI is there? If not then what benefits will an MFI

bring? Can we avoid an MFI and do with some modifications in TRIMs, GATS and TRIPs? These are some important questions that need to be addressed.

- An investment agreement giving protection to foreign investors is one of the many factors that determine FDI flows into a country. However this may not be true in all cases. For example, the US is a major investor in both India and Malaysia, but it does not have a BIT with either of them.

- As it is very often argued that foreign investors will benefit the most out of an MFI. But it is not clear the degree of importance that these investors attach to an MFI.

- It may be premature to arrive at a comprehensive MFI with binding obligations at this stage. Hence countries may explore the idea of agreeing to code of good practices. It may be recalled that during the Tokyo Round, the countries agreed on codes for both anti-dumping and technical barriers to trade and full-fledged agreements on these were arrived at during the Uruguay Round. Such a soft law approach may be the best way forward in the present context and depending on the experience of this approach an MFI may finally be evolved.