



A SUSTAINABLE BALANCE?



INTERNATIONAL INVESTMENT AGREEMENTS: HOW THEY REFLECT THE RIGHTS AND RESPONSIBILITIES OF DIFFERENT STAKEHOLDERS



SOMO, AMSTERDAM
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NOTE

SOMO is a centre for research on multinational corporations. In 1973 SOMO was founded to provide different organisations with knowledge on the structure and organisation of Transnational Corporations (TNCs) by conducting independent research.

In the Seventies the conduct of Transnational Corporations gave cause for intense international discussions. TNCs were accused of using their power in a negative way. There was a lot of debate about the growth of the economic and political power of TNCs as being the main carriers of Foreign Direct Investment. The concerns included the abuse of dominant market positions, a lack of commitment to the host economy, disrespect for labour rights and interference in national politics. At that time it appeared there was little basic knowledge on the structure and organization of TNCs.

SOMO is an independent research and consultancy bureau. Whether a TNCs investment strategy is involved, the environmental policy of an entire sector, or a major reorganisation at a local branch, SOMO can provide a clear analysis and a critical assessment of the relevant factors. SOMO executes research for international trade union secretariats, for environmentalists, human rights organisations, third world organisations, ethical consumer groups and women's groups. SOMO advises works councils of big and small companies but also solidarity groups and consumer organisations. SOMO also provides lectures and courses on different subjects.

The selection of SOMOs clients is deliberate. In democratic countries the political system is based on a certain balance between the three powers of government, parliament and the law. Such a balance however is hard to find in the economic area. This is particularly true where TNCs are concerned. They can move their investments around the globe and can easily back out from their democratic obligations. In this context the phrase 'democratic deficit' is used.

Fortunately there are NGOs which make an effort to make good this deficit, trade unions for instance, which make companies meet minimum requirements for conditions of employment and working conditions, women's groups which demand more opportunities for women in trade and industry, and works councils which try to use their legal rights to best advantage.

Other groups that work in this area are e.g. environmental groups which keep a close watch on companies to see whether they live up to their green image; Third World Groups which keep pointing out companies' responsibilities in the South and consumer organisations which urge consumers to buy products that give workers in Third World countries a better deal.

SOMO supports these groups by research, consultancy and by helping them to find realistic alternatives.

SOMO has built up considerable expertise in the following areas:

International Trade Regulation, WTO, International Investment Agreements, BITs, Regional Treaties and Multilateral Treaties and the position of developing countries, Competition Policy, Governmental and Non Governmental Codes of Conduct, National and European Works Councils, Environmental Issues.

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SOMO
CENTRE FOR RESEARCH ON MULTINATIONAL CORPORATIONS
MARLIES FILBRI & ILZE PRAAGMAN
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PREFACE AND ACKNOWLEDGMENTS

Since 1997 SOMO is working at a research programme on International Investment Agreements (IIAs). It was during the negotiations in the Organisation for Economic Co-operation and Development (OECD) on a Multilateral Agreement on Investment that SOMO got involved in the debate on IIAs.

During the negotiations SOMO became active in the fields of research, consultancy, capacity building and advocacy. The research in 1998 was focused on the effects of the liberalisation of Foreign Direct Investment regulations on labour standards and an analysis of the three anchor approach towards labour in the MAI. For that reason a consultancy project was carried out in India and Mexico on the automotive industry. To discuss the outcomes of the research an expert meeting and public debate were organised in Amsterdam. Meanwhile SOMO participated in the dialogue between the MAI negotiators and civil society to advocate a more balanced approach towards IIAs in which rights and responsibilities of investors were equally addressed.

During the research and advocacy work on the MAI we noticed that NGOs from the North and developing countries have a lack of knowledge on different elements within IIAs. Only few NGOs were able to discuss IIAs with negotiators because of the highly complicated and technical matter of investment regulation.

This research paper therefore analyses the different elements of IIAs (bilateral, regional and multilateral) to give NGOs a tool to discuss national and international investment policies with the respective negotiators. The Expert Meeting organised by UNCTAD on concepts in International Investment Agreements allowing for a certain flexibility in the interest of promoting growth and development, provided the basis of this research paper. It screens the different elements in IIAs on the question how far flexibility elements have been adopted.

Another issue that came up during this expert meeting was the concept of sustainable development. It appeared that especially governments of developing countries are not willing to adopt any references to sustainable development in IIAs. NGOs have an important role to play in pushing governments towards sustainable investment policies. This paper therefore provides an overview of examples how IIAs include sustainability elements at the moment and how far these are effective.

This paper is produced under the responsibility of Marlies Filbri (executive director of SOMO) who provided the structure, edited the text and did the research on the Bilateral Treaties. Ilze Praagman (intern at SOMO) analysed the different IIAs on flexibility and sustainability elements. SOMO discussed the paper during a NGO meeting with WILPF - International, IRENE - International Restructuring and Education Network, CEO - Corporate Europe Observatory, NOVIB and OIKOS.

SOMO will continue working on IIAs to build up capacity with NGOs in the North and the South on International Investment Policy making. SOMO therefore supports UNCTAD in its suggestions to start up NGO capacity building seminars. SOMO has profited largely from the possibility to participate in Expert Meetings of UNCTAD and also from the UNCTAD IIA Issues Paper Series which give an excellent overview and analysis of issues related to IIAs.

Funds for the execution of this research project were provided by: the National Commission on Sustainable Development (NCDO); NOVIB, providing SOMO with the means to participate in the UNCTAD Expert Meeting in Geneva and the Dutch Ministry of Foreign Affairs by funding SOMO's project on capacity building on IIAs with NGOs in developing countries.

Amsterdam, November 1999

Marlies Filbri
Executive Director of SOMO

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List of Terms

Pre-establishment National Treatment

Freedom of entry, the commitment to grant foreign investors the legal right to invest in the economy.

Post-establishment National Treatment

A government must treat a foreign-owned corporation no less favorably than a domestically owned corporation. That is, it cannot discriminate against foreign investors in favor of locally owned firms. National Treatment does not necessarily mean identical treatment for foreign affiliates and domestically owned firms.

Most-Favored Nation Treatment

The obligation of non-discriminatory treatment, meaning that host governments do not accord preferential treatment to investors from certain nations, but is committed to extend the same level of liberalized policy measures to investors from all signatory countries regardless of their nationality.

Standstill Clause

The imposition of the status quo as an irreversible minimum standard for liberalization. No new regulation that is contrary to the treaty provisions may be made.

Rollback Clause

The provision designed to reduce, over time, exceptions to liberalization obligations with a view to their eventual elimination. Investment that existed before the treaty was ratified is also covered by the treaty provisions and all restrictions must be rolled back as the treaty is signed.

Top-down Approach (negative lists)

Members aim to liberalize all sectors, but can determine by means of negative lists the sectors and economic activities in which rights of entry and establishment cannot be enjoyed (the so called country-specific exceptions). In these areas foreign investors will still be faced with restrictions. In future negotiations these exceptions will be subject to further liberalization.

Bottom-up Approach (positive lists)

Members can determine in which sectors they want to liberalize their investment through an 'opt-in', resulting in positive lists in which rights of entry and establishment can be enjoyed. The sectors to which members have no commitment to liberalize, national policy restrictions and regulations are still allowed, but can be subject to further liberalization in future negotiations. This gradual process of liberalization gives members the opportunity to open up their markets selectively to foreign investment, in accordance with their individual needs.

Screening

Discriminating between foreign investors upon admission.

Foreign Direct Investment

When an investor acquires shares in a foreign enterprise for the purpose of having an effective voice in its management.

Portfolio Investment

The investment provides the investor with a stake, but there is no controlling ownership link.

Not-Lowering Standards Clause

This provision is meant to discourage countries from lowering their (domestic or international) labor and environmental standards in order to attract FDI.

Performance Requirements

National conditions which host governments place to secure FDI benefits or to protect domestic industries and investors. A government can for example, require a TNC to transfer technology, to take on a local partner, to hire a certain number of local people or to invest a minimum amount in the local community. From a liberal point of view, Performance Requirements are a form of interference with the market mechanism by governments.

Flexibility

Flexibility is a concept developed by UNCTAD, used to determine the manner in which international investment agreements;

1. take into account the asymmetries in the level of development amongst its members
2. enable developing countries to pursue their own development policies
3. take the above into account factors while serving the interests of business to enable developing countries to attract FDI.

Sustainable Development

Development that meets the needs of the present without compromising the ability of future generations to meet their own needs (definition from the Brundtland Report).

REIO clause

Members of a regional economic integration organization are exempted from the obligation to grant MFN to non-member states.

Host country

The country which receives an inflow of FDI.

Home country

The country from which the flow of FDI originates.

Balance of Payments clause (BoP)

In case of a balance of payments crisis a temporary exception to treaty obligations is permitted.

Peer Pressure

Further liberalization and enforcement of treaty obligations is provided for by means of political persuasion, compromise and monitoring. There is no legally binding enforcement procedure.

The Research

The negotiations on the Multilateral Agreement on Investment (MAI), conducted at the Organisation for Economic Co-operation and Development (OECD), made civil society aware of the lack of balance between the needs of different stakeholders in international investment regulations, and the need to influence policy-makers to make sure that International Investment Agreements (IIAs) serve sustainable development. To determine a strategy to approach future negotiations on multilateral investment regulations, it is important to understand the current situation of international investment law. The aim of this project is therefore to:

- Give an overview of existing International Investment Agreements (Bilateral, Regional and Multilateral) and the way they reflect the needs of different stakeholders.
- Discern the trend in international regulation of Foreign Direct Investment (FDI).
- Determine the extent to which existing International Investment Agreements serve the goal of sustainable development.

Summary and Recommendations

This paper aims to show that the existing practice of investment regulation results in unbalanced International Investment Agreements which do not provide the means to promote world-wide sustainable development practices.

- *Firstly, there is a trend towards treaties which protect foreign investment and only specify the obligations of host governments in that regard.*
- *Secondly, the question of investors responsibilities is only briefly, and non-bindingly, addressed in some regional and multilateral agreements.*
- *Thirdly, and extension of firms' rights and governments' obligations has led to treaties with a minimum of flexibility to pursue development policies.*

The consequence of these trends, is that the ability of developing countries to meet their present and future needs threatens to be compromised. The balance of interests in IIAs reflects the structural inequality of international economic relations. It is questionable whether this balance is sustainable. The following issues should therefore be addressed to make the balance of IIAs more sustainable:

- The weak bargaining position of developing countries.
- The lack of transparency in negotiations and the fact that NGOs usually do not have access to the negotiating process.
- The lack of knowledge on IIAs within NGOs in developing countries.
- The lack of public debate in developing countries on international economic policies.

INTRODUCTION

Introducing the Multilateral Agreement on Investment (MAI)

From 1995 until the end of 1998, the OECD¹ member states negotiated a proposal to be entitled the Multilateral Agreement on Investment (MAI). The MAI was the first serious attempt to come to a uniform global agreement on liberalization and investment protection. In general, Transnational Corporations (TNCs) as well as the majority of OECD member states, attach a high level of importance to a transparent, non-discriminatory and stable investment regime on a multilateral level. They claim that a multilateral investment regime would improve the investment climate and boost Foreign Direct Investment (FDI) on a global scale. The outcome of such an agreement on liberalization would be economic growth, employment and sustainable development for all countries.

However, internal disagreement between OECD members led to the demise of the MAI. External criticism also put a lot of pressure on the negotiators. NGOs and other groups from civil society from all over the world severely criticized the MAI draft. During the early, but critical stages, the negotiating process had been closed to public scrutiny. The MAI draft therefore mainly reflected the interests of TNCs and their home countries. Business was granted far-reaching and legally binding privileges. The draft however, did not provide for binding obligations which would hold TNCs accountable for the negative effects of their activities on sustainable development. For this reason, NGOs advocated international rules that help to preserve the environment, protect workers, promote human rights and hold TNCs accountable. As Mark Vallianatos of "Friends of the Earth" stated:

"We believe the MAI disempowers citizens vis-à-vis corporations and elevates the mobility and protection of capital above sustainability and equity as the core values for the global economy."²

Sustainable development in developing countries became a hot issue during the MAI negotiations. It was also envisaged that the agreement would be open for accession to non-OECD member countries and would promote international standards of treatment of foreign investment world-wide. However, due to the fact that the developing countries were not involved in the negotiating process, their concerns were not addressed by the treaty. They foresaw the likelihood of being locked into a rigid neo-liberal regime which did not fit their specific development needs. The strict National Treatment (NT) obligation to the entry and establishment of investment, was especially controversial as developing countries would no longer have the possibility to screen investment upon admission. If developing countries were to become a party to the MAI, they would be prohibited from requiring TNCs to transfer technology or to attain a certain level of local employment. Under the MAI regime, such rules would be considered to be discriminatory treatment of FDI. Developing countries also regulate the activities of TNCs in their territories by means of so-called Performance Requirements (PR) to ensure that FDI serves the economic, social and environmental priorities of their national development policies.³ These PR's would also be prohibited under the MAI rules.

The positive aspect of the MAI negotiations, from the point of civil society and efforts at achieving sustainable development, is that it has increased the awareness of the importance of balanced FDI regulation. It has also shown that the interests of the different parties involved can be very much opposed to each other. While the MAI reflected the TNCs efforts at realizing deregulation of

¹ Organisation for Economic Co-operation and Development.

² Mark Valliantos, Andrea Durbin, *License to Loot, The MAI and how to stop it*, (Washington 1998) 2.

³ Polaris Institute, *Towards a Citizen's MAI, An alternative Approach to Developing a Global Investment Treaty Based on Citizen's rights and Democratic Control* (1998), 4.

governmental restrictions on foreign investment, opposition from NGOs, citizens and developing countries stressed the need for regulation of FDI to achieve and promote sustainable development.

Seeing that the MAI negotiations broke down, it could be a useful exercise to explore the body of law governing international investments which currently exists. Do other International Investment Agreements serve the purpose of sustainable development, or is sustainable development in these treaties also compromised? Furthermore, what is the trend in international regulation of FDI? By way of broadening the knowledge base on existing investment regulation it will hopefully be possible to determine how to develop a strategy to oppose present investment rulings and to influence future negotiations on a Multilateral Investment Agreement, in an effort to promote sustainable development practices.⁴

A balance of interest in International Investment Agreements ?

At the moment, international investment is loosely regulated in bilateral and regional agreements or by multilateral rules. The United Nations Conference on Trade and Development (UNCTAD) has made a start in bringing a certain level of transparency to the complex network of IIAs by way of providing an overview of investment instruments.⁵

It is apparent that IIAs differ in the way they serve the purpose of sustainable development, defined as;

*“development which meets the needs of the present without compromising the ability of future generations to meet their own needs”.*⁶

Whether an IIA serves the purpose of sustainable development depends mainly on the way it balances the different needs of the parties involved in the negotiating process. Three interest groups can be distinguished that play an important part in the creation of IIAs:

1. business and “home” (most developed) countries “seeking protection of investment and international regulation”
2. developing countries, “host” countries “preferring flexible IIAs”
3. civil society looking for balanced treaties addressing the responsibilities of TNCs towards the needs of labor, human rights and the environment

An International Investment Agreement that serves sustainable development would ideally be an agreement that takes into account the needs of business and their home countries, without compromising the present and future needs of host countries and civil society. In balancing the various interests it could be useful to describe the most important elements of IIAs that serve the various interest groups and the extent to which the elements conflict.

1. Protection and privileges to business and “home” countries.

TNCs looking for markets to invest benefit the most of a predictable, transparent, open and stable investment regime. Host countries of FDI want to regulate the operation of TNCs in their territories to make sure they maximize benefits. These national policies can differ widely as they reflect the shifting

⁴ Presently there are proposals to negotiate further liberalization of investment within the World Trade Organisation (WTO), in the so called “Millennium Round Dialogue Meeting on investment, Brussels 28 April 1999, European Commission, DGI M-2.

⁵ UNCTAD, International Investment Instruments Vol. I, II and III, 1996.

⁶ Brundtland Report

priorities of a society's internal, often shifting priorities.⁷ As TNCs invest abroad they are confronted with these differing national policies, which are at times obstacles to maximizing profits. They therefore strive for uniform international standards of treatment for international investment. The content of IIAs can serve the interest of business in several ways, for instance;

- ♦ a broad definition of investment, with the inclusion of portfolio investment
- ♦ the obligation of non-discriminatory treatment of investment by means of strict National Treatment (NT) and Most-Favored Nation Treatment (MFN)
- ♦ the prohibition of Performance Requirements (PR), as these would frustrate the free flow of investment
- ♦ legally binding standards of treatment by means of a state-to-state and investor-to-state dispute settlement mechanisms

2. Flexibility to enable "host" countries to pursue their own development policies

In view of sustainable development, it would be desirable for IIAs to be more *flexible*.⁸ When both developed and developing countries conclude an investment agreement, there is a formal symmetry. This legal symmetry does however disguise the underlying differences in economic development. IIAs therefore need to be more flexible, and should reflect the *de facto* economic asymmetry and permit developing countries to benefit fully from the agreement.⁹

Flexibility is a concept developed by UNCTAD, used to determine the way in which international investment agreements:

- ♦ take into account the asymmetries in the level of development amongst its members
- ♦ enable developing countries to pursue their own development policies
- ♦ this while continuing to serve the interests of business so that developing countries are able to attract FDI.

Figure 1. The concept of flexibility.

Simply put, flexibility is the recognition that a developing state has both the right and responsibility to regulate investment in order to ensure that FDI serves its development priorities. IIAs can provide flexibility by;

- ♦ having a narrow definition of investment which in effect limits the scope of treaties
- ♦ acknowledging the differences in level and pace of development of member economies
- ♦ recognizing that "host" countries, especially developing countries, have a right to discriminate in the treatment of investment, for instance by allowing exceptions to National Treatment and Most-Favored Nation Treatment obligations, and permitting Performance Requirements
- ♦ and provisions that serve development aims, such as technical assistance and advice.

These provisions, however, are often at odds with business interests. Flexibility in the service of development is seen by investors as a threat to the stability, transparency and predictability of the investment climate. The process of liberalization would be frustrated as flexibility legitimizes preferential treatment, a form of protectionism in the eyes of business.

⁷ Mark Vallianatos, *License to Loot*, 1.

⁸ UNCTAD, *Expert Meeting on International Investment Agreements: Concepts allowing for a certain flexibility in the interest of promoting growth and development* (Geneva 1999), 5.

⁹ *Ibid.*, 23.

Preferably, there should be a balance between flexibility on the one hand, and security for investors on the other. Too much flexibility is not always in the interest of developing countries. If they cannot provide sufficient assurances, investors will look for other locations to invest, and many developing countries would lose out on an important source of income. On the other hand, too much security for investors could undermine the ability of developing countries to pursue their developmental objectives.

3. Labor and environmental standards in the interest of sustainable development

Another controversial issue is how IIAs regulate the responsibilities of TNCs and their home-countries towards labor and the environment. This issue is becoming more and more important, and can be explained by the fact that TNCs move beyond the oversight of governmental control as they cross borders to make investments. As a consequence, an accountability gap is emerging. Many NGOs and citizens from around the world therefore advocate international rules that not only take into account the economic needs of a state and its citizens, but also address social and environmental concerns.¹⁰ To ensure sustainable growth they claim that it is necessary to regulate the operation of foreign corporations and bind TNCs to social and environmental obligations.¹¹ It is pointed out that it is especially important to control the social and environmental implications of FDI in developing countries, as these countries are more vulnerable to irresponsible TNC conduct. As a consequence of their growing dependency on foreign capital for their future development, developing countries are at times prepared to lower their domestic labor and environmental standards in order to increase their competitive advantage in the fierce competition for FDI. Legally binding labor and environmental standards could ensure that TNCs invest in a responsible way and ensure that developing countries refrain from lowering their labor and environmental standards.

TNCs and many of their home countries however, do not desire international labor and environmental standards in IIAs. This is first of all due to the fact that they do not desire international standards that may discriminate between foreign and local investment, even though these standards may be based on legitimate policy concerns. The claim is that international labor and environmental standards in IIAs could lead to a distortion of competition with regards to local investors. TNCs want deregulation, not more regulation of TNC activities. They also wonder why they should be required to comply with international labor and environmental standards when host governments and domestic industries themselves do not implement domestic laws. It is argued that due to the visibility of TNCs, they are always forced to comply with labor and environmental laws. TNCs are generally of the opinion that implementation of labor and environmental law is the responsibility of the governments of host countries.

Developing countries in general do not desire the imposition of binding obligations concerning labor or environment in International Investment and Trade Agreements. This does not mean however, that they are not genuinely concerned about the effect of international investment on sustainable development in their territories. They simply do not want to risk a loss of competitive advantage with respect to their low wages and lax regulatory environments. The danger also exists that labor and environmental standards may be used in a protectionist manner. Imposition of international standards could impose additional financial burdens on developing countries and make their investment climate more expensive and therefore less attractive to foreign investors. Governments of developing countries prefer a flexible approach towards labor and environmental standards and this partially explains the lack of mentioning of, let alone legally binding enforcement of, labor and environmental concerns in IIAs.

¹⁰ Mark Vallianatos, *License to Loot*, 32.

¹¹ Marlies Filbri, *Open markets matter, but to whom?*

The crux of the issue boils down to who will take the responsibility, and who will pay for the social and environmental costs of international investment?" It is quite clear that too much flexibility towards labor and environmental standards is undesirable. The purpose of sustainable development would not be served. People and the environment would suffer the consequences of the irresponsible way in which TNCs would invest abroad, and the lowering of domestic labor and environmental standards by developing countries. Social dissatisfaction in both "host" and "home" countries could result tensions and conflicts which could have the potential to undermine the political and economic stability which is so essential for international investment to thrive. Broad acknowledgment therefore exists that a certain degree of labor and environmental regulation, based on legitimate policy concerns, would benefit not only civil society, but also investors and states and efforts at sustainable development in general.

The research project

In view of future multilateral negotiations on investment regulation, the aim of this project is to:

- Give an overview of existing International Investment Agreements (Bilateral, Regional and Multilateral) and their content.
- Discern the trend in international regulation of FDI, either in the direction of protection or in the direction of promotion and flexibility.
- Determine to what extent International Investment Agreements serve the purpose of sustainable development.

This paper will initially focus on the MAI treaty as it is an example of how current international investment regulation tips the scale in favor of the rights (and not obligations) of TNCs. The MAI was so unbalanced that citizens and NGOs on a global scale mobilized in opposition. By taking a closer look at how the interests of business, developing countries and civil society were reflected in the MAI, the flaws and merits of the draft treaty will become apparent.

Chapter 2 will examine the degree of flexibility (to serve developmental needs) in other relevant regional and multilateral investment agreements, namely;

- APEC (Asia Pacific Co-operation) non-binding investment principles (1994)
- Multilateral Investment Guarantee Agency (MIGA 1985)
- OECD code on capital movements (1961)
- Energy Charter Treaty (1994)
- Trade-related Investment Measures (TRIMS 1994)
- Trade-related Aspects of Intellectual property Rights (TRIPS 1994)
- General Agreement on Trade in Services (GATS 1994)
- North American Free Trade Agreement (NAFTA 1992)

A comparison of these IIAs will be made on the basis of their structure and content. It is important to distinguish the differences in nature of the IIAs. As they indicate the extent of treaty (in)flexibility, the following elements will be compared¹²;

Objectives and principles stated in the pre-amble.

Is the only goal the protection, regulation and liberalization of investment, or does the agreement consider development objectives as well ?

Substantive provisions.

What is the scope of the treaty? And to what extent are countries allowed to discriminate in the treatment of foreign investment and pursue their own development objectives ?

Mode of implementation.

Does the treaty provide for exceptions, temporal derogation's or promotional measures to the treaty obligations, so developing countries have more flexibility to implement treaty provisions?

Structure of the treaty.

Does the architecture of the treaty reflect the formal acknowledgment of the structural inequality in the level of economic development between the member countries?

Once the different IIAs have been examined, they will be placed on a continuum varying from inflexible to flexible investment regulation. Through an improved understanding of these IIAs, it can be determined how future proposals on the MAI towards multilateral regulation relate to them.

At the moment international investment regulation is rapidly being developed in the form of Bilateral Investment Treaties (BITs) between developed and developing countries and even amongst developing countries themselves. In analyzing multilateral treaties it can therefore be useful to compare them to bilateral agreements. Ten BITs (listed below), that have been concluded between the Netherlands and countries in Sub-Saharan African will therefore be examined in the third chapter.

Ivory Coast 1965, Cameroon 1965, Uganda 1970, Tanzania 1970, Sudan 1970, Kenya 1970, Ghana 1989, Nigeria 1992, South Africa 1995, Zimbabwe 1997

The degree of flexibility, as reflected in the structure and content of the treaties will be examined to try to answer the following questions: To what extent do BITs facilitate and promote growth and sustainable development? In which direction are BITs evolving?

The last chapter examines the extent to which IIAs serve the protection of labor and environment in the interest of sustainable development. The main focus will be on a case study that illustrates how a balance of interests can to some extent be achieved; the NAFTA Labor Side Agreement (LSA). The NAFTA is a regional trade agreement between Canada, the United States and Mexico. The Investment Chapter of the NAFTA served as a model for the MAI and is a good illustration of the trend towards further investment liberalization between countries with varying levels of development and substantial differences in labor legislation and implementation; Mexico being a New Industrializing Country, while the United States is the largest national economy in the world.

The LSA¹³ demonstrates how NGOs can exert some influence on the balance of a treaty. Organizations like the US labor union AFL-CIO, criticized the NAFTA program fiercely during the

¹² Ibid., 7

negotiations. They argued that American TNCs would relocate their assembly plants to Mexico's northern border to profit from the favorable investment climate there, caused by the existence of an inexpensive labor supply and the lack of enforcement of labor and environmental laws by the Mexican government. A successful campaign of the NGOs eventually led to the ratification of the LSA by the member states of NAFTA.

On the basis of the insights acquired in the case studies, it will be possible to discern important trends in international investment regulation. In what direction are International Investment Agreements evolving? How do they reflect the balance of interest of the parties involved? Furthermore, how does the MAI, which led to so much upheaval within the OECD itself and to opposition from citizens and NGOs from all over the world, relate to other IIAs? From this exercise important issues can be defined which need to be addressed in the interest of sustainable development. The purpose of this is not only enable strategies to be developed in the context of future multilateral negotiations on investment in the WTO, but also in the continuing trade and investment negotiations on a bilateral and regional level.

¹³ This case study is based on a paper written by Ilze Praagman, with the title : "*Bereid om te luisteren?*" *De Labour Side Agreement, Vakbonden & de Mexicaanse Staat*, (Groningen 1999), ii, 1- 48.

1.1 Globalization and regulation of international investment

The 1990's have been characterized by a further globalization of international economic relations. FDI has grown more rapidly ever since. In 1997¹⁴, FDI accounted for a 19% increase in world inflows and a 27% increase in world outflows of capital, mainly between developed countries.

It seems that as investment becomes more and more globalized, domestic policies affecting investment become global investment policy issues. According to the dominant neo-liberal paradigm, harmonization is needed in those domestic policy areas that contain discriminative measures towards FDI. Only then can transparent, free markets and full competition be guaranteed in which foreign investment can thrive. The growing consensus on the necessity of regulation in combination with the need of countries to attract FDI has led to an increase of IIAs. In the 1990s the number of BITs doubled and now amounts to more than 1500.¹⁵ Most are between developed and developing countries, but developing countries are rapidly concluding BITs among themselves as well.

In regional integration programs (such as NAFTA), investment provisions are also being included. On a multilateral level, the Uruguay Round of the GATT in 1994 led to regulation of investment in areas such as services (GATS), intellectual property rights (TRIPS) and trade-related investment measures (TRIMS). Investors have gained more protection in more areas. Increasingly, however, voices are being heard that the existing multilateral provisions are insufficient. Business in particular is pushing for a uniform multilateral framework in which all areas of investment will be regulated. This new, comprehensive and uniform Multilateral Investment Agreement (MIA) would supersede all other investment regulation. At the instigation of OECD members, Canada, Japan and the members of the European Union, attempts were made to establish a MIA in the WTO framework. The proposals were blocked by developing countries however, who already felt the GATS, TRIPS and TRIMS had gone too far. After the failed MIA proposal in the WTO, the OECD itself, with its twenty-nine industrialized members, established a "Negotiating Group" in 1995 to conduct the negotiations and prepare the draft of a Multilateral Agreement on Investment (MAI). It was envisioned that the MAI would build further on the OECD codes of Liberalization of Capital Movements, that had led to progressive liberalization between the OECD members during the past three decades. Legally binding high investment standards would be designed to protect investment, liberalize and facilitate investment flows. It was thought that the treaty could be concluded in 1997, but internal divisions between OECD members and an effective lobby of NGOs led to a cancellation of further negotiations on the MAI in September 1998. This is predictably not the end of multilateral investment regulation proposals, however. A "working group" has been established in the WTO to examine the links between trade and investment. As the ministerial meeting in Seattle in December 1999 is approaching, some countries (especially from the EU) are pushing for further liberalization and regulation of international investment in the context of the WTO.

As the past has shown, the MAI is highly controversial. Proposals to enhance TNCs rights are not welcomed by critical NGOs and developing countries. This does not mean however, that a more balanced multilateral investment agreement is not feasible. The UNCTAD has tried to look for a more balanced approach by examining the way in which flexibility with respect to development goals is formulated in existing IIAs. The UNCTAD has a consultative status in the WTO working group, and studies on flexibility are taken into account during the discussions.¹⁶ As initiatives to negotiate a

¹⁴ Karl P. Sauvant, (et al), *World Investment Report 1998, Trends and Determinants Overview*, (UNCTAD Geneva 1998) 7.

¹⁵ *Ibid.*, 117.

¹⁶ Dialogue Meeting on investment, Brussels 28 April 1999.

comprehensive investment treaty are continuing and since the MAI was the most serious attempt to conclude such an agreement, it will be of interest to see how the MAI has balanced the differing interests of investors, countries and civil society in its content and structure.

1.2 Flaws and merits of the MAI draft.

1.2.1 The drafters: Regulation of discriminative state¹⁷ practice

The OECD member states drafted a treaty that would establish a fair, transparent and predictable investment regime.¹⁸ The main purpose of the drafters was to provide investors with sufficient protection through high investment standards that were legally binding. The provisions are in fact directed at governments and intend to regulate national policies regarding investment.

To guarantee full protection to investors, the definition of investment covered "every kind of asset". All areas of investment are included in the definition, also portfolio investment. Because the definition of investment is defined so broadly, the scope of the treaty is extensive. Virtually all types of investment are covered by MAI provisions.

Protection against national discriminative policy measures is provided for by means of National Treatment (NT) and Most-Favored-Nation (MFN) obligations which apply to the entry and establishment of investment. This in fact means that a "host" state:

- ♦ must grant foreign investors freedom of entry, namely the legal right to invest in the economy (pre-entry NT),
- ♦ is not allowed to accord preferential treatment to investors from other nations (MFN),
- ♦ must treat investors operating in its territory not less favorably than domestic investors (post-entry NT).

Screening by host-countries of investment applications is therefore no longer permitted. Furthermore, the MAI has pushed for a removal of conditions that governments put in place to secure that FDI benefits the country, or to protect domestic industries and investors. These are called Performance Requirements. Under the MAI, governments are no longer allowed to require TNCs to transfer technology, take on a local partner, hire a certain number of local people, or invest a minimum amount in the local community. These Performance Requirements are seen as market-distorting and are at odds with the liberal principle of non-discrimination. By removing these investment-related obstacles to market access, liberalization of investment flows is thought to be stimulated.

Privatization is also subject to NT. If a public enterprise is to be privatized, a national government must also allow foreign investors to make a bid.¹⁹

There are exceptions to the full application of NT and MFN, but these are narrow and well defined. Certain national measures that are inconsistent with NT and MFN obligations may be taken in the interest of national security or public order. These are the so called general exceptions. A balance of payments clause also allows for a temporary derogation. The country-specific exceptions are the most important. Members aim to liberalize all sectors, but can determine by means of negative lists the sectors and economic activities in which rights of entry and establishment cannot be enjoyed. In these

¹⁷ State here refers to government.

¹⁸ Multilateral Agreement on Investment, Negotiating text (as of 24 April 1998), OECD Directorate for financial, fiscal and enterprise affairs. Preamble, paragraph 4.

¹⁹ Consumer International, *What consumers expect from international rules on investment* (London 1997), 11.

areas foreign investors will still be faced with restrictions.²⁰ In future negotiations these exceptions will be subject to further liberalization.

The treaty also provides for specific investment protection provisions. Nationalization and even measures that have the "equivalent effect" of the taking of foreign property is prohibited. There are exceptions, for instance for a purpose in the public interest, if it is done in a non-discriminatory way, and if compensation is paid promptly, adequately and effectively at a fair market value. A host state must also ensure free transfer of payments without delay and in a freely convertible currency. And to induce the effectiveness of the MAI provisions, an investor whose rights have been infringed can sue the host state by means of a binding international dispute settlement. All treaty provisions are subject to the dispute settlement mechanism. There are two ways by which an investor can claim his right; through the state-to-state dispute mechanism by which the home country of the investor will represent the investor's interests; and through a direct investor-to-state dispute settlement arrangement. It is especially the investor-to-state dispute settlement gives the investor a strong weapon to protect his rights against discriminative state practices.

To secure the uniform application of the treaty provisions and the overall level of liberalization, a stand-still and roll-back clause are also incorporated. These clauses make all existing investment and investment regulation subject to the treaty provisions. This means that no new regulation contrary to the treaty provisions may be made and that investments which existed before the treaty was ratified are also covered by the treaty provisions; all restrictions must be rolled back when the treaty is signed. The MAI also has strict withdrawal rules. A state is permitted to withdraw from the treaty but then only after having been a signatory for 5 years. Furthermore, the treaty must still be observed by the state for a full 15 years after withdrawal.

1.2.2 Critics' views: lack of regulation of business practices

As proponents of the MAI are pushing for regulation of national investment policies, critics argue that business practice should be regulated. The main criticism of the MAI draft, first of all, is that the investment provisions can directly constrain governments, especially in developing countries (with their specific needs), from controlling activities of foreign owned companies. Secondly, there are no provisions that hold TNCs accountable for their activities in "host"-countries.²¹ Thirdly, critics point out that the MAI has failed to address legitimate policy concerns in the area of sustainable development. Finally, it is argued that the extensive rights of TNCs granted by the MAI will reduce the economic sovereignty of national governments.

As one can conclude from the above, the MAI permits state control as long as it is based on National Treatment, which means as long as foreign investors are not treated less favorably than domestic investors.²² Through examination of the treaty draft it is obvious that "host" countries' discretion in directing and implementing foreign investment policy has been limited. The MAI provisions narrow down the investment policy choices of "host" countries to regulate international investment flows.

The definition of investment used in the MAI draft treaty covers all areas of investment. The problem of such a broad definition is that anything a government undertakes that affects any investment assets

²⁰ Frans Engering, "The Multilateral Investment Agreement", *Transnational Corporations*, vol.5, no 3. (December 1996) 151.

²¹ Mark Vallianatos and Andrea Durbin, *License to Loot. The MAI and how to stop it*, (Friends of the Earth, Washington 1998) 2.

²² This is different from non-discrimination as under national treatment, treating foreign investors on more favorable terms than domestic investors is permitted.

is covered by the MAI.²³ This full coverage may not be consistent with a state's development policy at every period in the life of the agreement²⁴. The inclusion of Portfolio Investment is especially controversial. Portfolio Investment can be beneficial to a country's development as it is a source of capital. But it can also create the possibilities for capital volatility. By means of provisional safeguards the negative effects of capital volatility can be addressed, but when the transfer-pricing provisions of the MAI are taken into consideration, no safeguards are built in, and therefore restrictions on international capital speculation are not allowed.

Secondly, the NT and MFN obligations are extensive, and in combination with other provisions, do not provide much flexibility. The way NT and MFN treatment are formulated, leaves room for more favorable treatment of TNCs with regard to local investors, but specifically prohibits positive discrimination of local investors for instance by means of performance requirements²⁵. Because TNCs differ from local investors and already have a competitive advantage related to "scale and scope", post-entry NT in fact favors TNCs in comparison to local investors and therefore TNCs might even "outcompete" local firms.²⁶ This could have serious implications for developing countries which would no longer be able protect local investors or industries through national standards, or benefit fully of FDI by demanding local content or transfer of technology. Because NT applies to the pre-entry stage of investment, the economy of a host country is actually opened up to virtually every form of economic activity. A host state can no longer screen the development implications of investment upon entry.

The broad scope of the definition of investment and NT and MFN treatment actually implies that the range of protection, regulation and liberalization of investment has expanded; and at the expense of sustainable development, say its critics. Developmental concerns could have been taken into account by excluding certain types of investment from the definition of investment, by limiting the applicability of the definition of investment to specific operative provisions or by granting more and broader exceptions or derogations to MFN and NT. In the case of the MAI however, these concerns are insufficiently addressed. The definition of investment applies to all operative provisions and the exceptions or derogations to MFN and NT are limited.

General exceptions are allowed to MFN and NT but do not explicitly concern developmental needs, labor or environmental concerns. The only temporal derogation allowed from MFN and NT is in the case of a balance of payments crisis. Furthermore, the treaty does not provide for temporal phasing provisions, to allow developing countries in transition more time and more possibilities to adapt their policies and laws to MAI standards. Promotional measures for developing countries, such as technical advice and assistance are also lacking. The treaty however does provide for country specific exceptions. Member countries commit themselves to fully liberalize sectors that are not on these negative lists. Along the way, however, full liberalization of sectors for which no exceptions have been made beforehand, may not always be consistent with a state's development policy²⁷. One cannot predict the emergence of new industries or sectors, but any new economic industries would automatically fall under the MAI provisions. Because of the stand-still, roll-back clauses and the strict withdrawal criteria, a country is locked into the commitment. A country can make no exceptions to the sectors that are not on the negative list and may not regulate the same sectors or economic activities in a way that is inconsistent with MAI provisions. Even if it withdraws from the treaty, it must observe the treaty obligations for another 20 years.

²³ Mark Vallianatos and Andrea Durbin, *License to Loot. The MAI and how to stop it*, (Friends of the Earth, Washington 1998) 5.

²⁴ Karl P. Sauvant and Pedro Roffe (et al), *Scope and definition in: UNCTAD Series on issues in international investment agreements* (New York and Geneva, 1999) 62.

²⁵ The long illustrative list of prohibited performance requirements goes further than the TRIMS agreement.

²⁶ Consumers International, *What consumers expect*, 11-12

²⁷ Karl P. Sauvant, *Scope and Definition*, 62.

Thirdly, criticism is aimed at the point that the rights granted to investors, especially due to their binding nature, go too far. For instance, the definition of expropriation is very controversial. Not only is direct expropriation prohibited, but indirect expropriation or measures having the equivalent effect are also included in the prohibition. The experiences with this type of clause in the NAFTA agreement has initiated a discussion concerning "regulatory takings". In some instances national regulations related to the environment or labor can have the same effect as "expropriation". Even though these measures can be based on legitimate policy concerns, a TNC can sue the state by means of investor-to-state dispute settlement. This is what happened in the *Ethyl case*. The Canadian government banned the import of the gasoline additive MMT, because it was considered a public health hazard. The only company that produced MMT was based in the United States, and sued the Canadian government for infringement of its rights under the NAFTA, claiming that it had been "expropriated". A deal was made and the company dropped the lawsuit²⁸. NGOs however are concerned that the *Ethyl case* will set a precedent. This case is an example of how powerful a TNC becomes when it can protect its rights through a legally binding dispute settlement mechanism. By means of the dispute settlement mechanism the MAI treaty provisions can have a direct effect on a government. Because all treaty provisions are subject to the dispute settlement mechanism, the effect is even more substantial. Unfortunately, the mechanism is not open to civil society, and democratic checks and balances are in effect not in place.

1.3 Drawing up the balance.

The main objective of those involved in the MAI negotiations, was protection of investment through high standards of treatment. This objective is clearly reflected in the MAI draft. The absence of provisions that address concerns other than investment protection, regulation or liberalization, can be explained by the fact that neither developing countries nor NGOs were invited to join the MAI negotiations. The whole MAI negotiations process and procedure lacked transparency.²⁹ The result is that the interests of business have clearly been taken into account in the MAI treaty, without addressing the important issue of "corporate responsibility". When the ratification of the MAI was still an option, it was feared that the democratic deficit of the MAI would further restrict the possibilities of national governments and civil society to control the activities of TNCs and to adequately protect environmental and labor standards.

It must be pointed out however that the drafters did balance the rights of the investors to some extent, by means of a three anchor approach towards labor and environmental protection. First of all, there is the mentioning of sustainable development in the preamble as a general objective, and there are references to international treaties and organizations that are concerned with labor and environmental protection. Secondly, in the substantive provisions a "not lowering standards clause" is included. States are prohibited from lowering their domestic labor and environmental standards in order to attract specific investment, as this would be a counterfeiting measure. Thirdly, there is a proposal to annex the OECD-guidelines on MNEs (Multinational Enterprises) to the treaty. There are also some subject-specific exceptions (article 1.c) allowed to the prohibition on, for example, local content. National environmental measures necessary to protect human, animal, plant life or health, that do not constitute a disguised form of investment restriction, are allowed. But it is very debatable as to whether these exceptions and the three anchor approach provide sufficient checks and balances. While TNCs have acquired rights that are legally binding, the three anchor approach does not constitute a binding obligation for TNCs to respect. States are in fact faced with more obligations to protect and promote investment, but the obligations they can impose on TNCs have been narrowed down.

²⁸ Marlies Filbri, *The Multilateral Agreement on Investment*, 7.

²⁹ Dialogue Meeting on investment, Brussels 28 April 1999.

THE MOST SIGNIFICANT CONSEQUENCES OF THE MAI WOULD HAVE BEEN THAT STATES WOULD NO LONGER BE ABLE TO :
1. Screen investment upon entry.
2. Treat local investors more favorably than foreign investors.
3. Put in place conditions on the establishment of the investment, such as performance requirements.
4. Pursue policy objectives concerning sustainable development that could infringe upon the rights of foreign investors (for example if regulations have the equivalent effect of expropriation), without running the risk of being sued by an investor.
5. Limit the risk of capital volatility through restrictions on international financial speculation.
6. Withdraw without the obligation to maintain the application of the MAI provisions for a minimum of 20 years.
7. Favor local investors above foreign investors in privatization schemes as privatization is also subject to NT.

Figure 2. Consequences for signatory states if the MAI had been adopted.

2.1 Flexibility: Having development considerations in mind.

Developing countries are important members to IIAs as they are growing markets for investment. Compared with 1990, the inward flows of capital to developing countries have by 1997 increased by one-fifth and now accounts for a third of global inward FDI. Most capital is exported from the industrialized countries and accounted for 90% of global outflows in 1997.³⁰ The developed countries are the home base of most TNCs. Many IIAs are targeted at the developing countries, in order to *liberalize* these markets for further inflows of FDI upon entry, to *protect* investment after establishment, to *regulate* discriminative national investment policies or to *promote* foreign investment to developing countries by means of technical assistance or insurance of investment. It is generally accepted that agreements to which developing countries are a party, have as an essential goal, next to stimulating and protecting investment, the promotion of social and economic development.³¹ The extent to which an agreement is able to ensure sustainable development can, amongst other things, be determined by the flexibility of the agreement. Flexibility in IIAs can be discerned by posing the following questions:

*Does the agreement take into account the asymmetries in the levels of development of its members and;
enable developing countries to pursue their own development policies;
while serving the interests of business so developing countries are able to attract
needed FDI?*

To answer these questions the objectives and principles, the substantive provisions, the mode of implementation and the structure of the selected IIAs will be examined.

“Objectives and principles”

To be able to interpret the provisions of an IIA, one must understand what the purpose of the agreement is. Is the only goal protection and liberalization of investment, or does the agreement consider development objectives as well? Here it is necessary to examine the preamble, because within it the objectives and purposes of the treaty are stated. Flexibility in the preamble can be reflected in several ways. Development concerns could be introduced for the first time in a general or more specific way, or the objective of sustainability can be stated. A treaty often also includes a chapter usually referred to as the ‘general part’, with articles stating the objectives and principles, where development concerns can also be formulated.

“Substantive provisions”

The substantive provisions are the actual content of a treaty, the tools for giving effect to the stated objectives in the preamble. The development concerns of the parties can determine what issues are included and the way in which the issues are dealt with: Is the definition of investment broad or narrow? Does full MFN and NT apply or is state control permitted? Are Performance Requirements allowed or forbidden? Are standards of protection of investment included? Are provisions included such as rollback and standstill clauses? Is there a binding dispute settlement mechanism, and if so, who permitted to use it, and against whom?”

³⁰ Karl P. Sauvart (et al), *World Investment Report 1998*, table 5.

³¹ UNCTAD, *Concepts allowing for a certain flexibility*, 6.

“Mode of implementation”

This refers to the way in which an agreement operates to further the development objective. Does the treaty provide for exceptions and (temporal) derogation's? Are developing countries permitted more time to adapt their legislation, standards or investment regime to the required standards through temporal phasing provisions? Are any promotional measures in favor of developing countries provided for?

“Structure of the treaty”

The very “architecture” of the treaty reflects the relationship between the parties. Does the treaty mirror the structural economic differences through a formal distinction between developed and developing countries and by a bottom-up approach, so developing countries can progressively liberalize?

Although most international regulation of investment is to be found in bilateral agreements, a body of investment regulation in multilateral and regional agreements has also been developed. In the following paragraphs the most relevant agreements will be examined, namely; the APEC non-binding investment principles, the MIGA, the OECD Code on Capital Movements and the WTO investment rulings (TRIMS, TRIPS, and GATS). Finally the NAFTA treaty will be examined on the basis of the elements of (in)flexibility mentioned above.

2.2 Regional and Multilateral Investment Regulations

2.2.1 APEC non-binding investment principles (1994)

The Asia-Pacific Economic Co-operation³² agreement aims to promote free and open trade and investment liberalization in the Asia-Pacific region. In 1994 the APEC non-binding investment principles were adopted. Even though these investment principles are merely a “best effort commitment” with the objective to *liberalize* the flow of investment, they are worth looking at. There are some elements of flexibility in the statement that are of interest and the expectation is that these principles will become binding obligations in the future to support “open regionalism” in the Asia-Pacific region. The preamble in “acknowledging the diversity in the level and pace of development of member economies as may be reflected in their investment regimes (...)”, therefore address the issue of the asymmetrical levels of development between APEC members. The specific mentioning of *flexibility as regards to the investment regime* is a unique feature of the APEC and is not found in other IIAs.

The main focus of the APEC statement is on the treatment of investment, in particular to further market access. At first sight it seems like national policy discretion is narrowed down, especially as countries are not allowed to discriminate against foreign investors as they seek to invest in the country concerned. This is reflected in the combined MFN and NT treatment, that applies to the entry and establishment of investment. Furthermore, it is stressed in the preamble that it is important to fully implement the TRIMS agreement. This would imply that certain export and product requirements are no longer allowed. On the other hand, policy discretion is still permitted. The NT requirement is flexible as the responsibility of investors is addressed through the “*investor behavior*” clause, another unique feature of the APEC principles. In this clause it is stated that if foreign investors must abide by

³² The following countries are member to the APEC: Canada, Chile, Mexico, Peru, USA, Brunei Darussalam, China, Hong Kong, Indonesia, Japan, Korea Rep., Malaysia, Philippines, Singapore, Taiwan-China, Thailand, Vietnam, Australia, New Zealand, Papua New Guinea and Russia.

the host country's laws, regulations, administrative guidelines and policies, just as any domestic investors should, market access will be facilitated. This in fact means that exceptions to NT can be made on the basis of domestic law. There is a requirement in the APEC to minimize the use of performance requirements that have a distorting effect on the flow of investment.

On the whole, the APEC statement remains quite vague. There is no dispute settlement. If a conflict occurs, the treaty refers to consultation, negotiation or arbitration without specifying any mechanism. Countries must sort things out among themselves. Furthermore, the scope of the treaty is unclear as there is no definition of investment and nothing can be said about the mode or structure of implementation. It would not be surprising if the statement evolved into an agreement that is less flexible. A future agreement will probably include a negative list, as this corresponds with the combined NT and MFN model. It can also be expected that the non-obligatory commitment to minimize the use of TRIMS, will become obligatory and that therefore the NT obligation will be less flexible.

2.2.2 Multilateral Investment Guarantee Agency, MIGA (1985)

The MIGA³³ is part of the World Bank Group, together with the International Development Agency (IDA), the International Finance Corporation (IFC), the International Bank for Reconstruction and Development (IBRD) and the International Centre for the Settlement of Investment Disputes (ICSID). What makes the MIGA such a special IIA is that it is tailored to fit the specific needs of developing countries. The MIGA aims to encourage investment flows to developing countries in particular. Firstly it provides investors insurance against non-commercial risks, namely the losses resulting from currency transfer, expropriation (and similar measures), a breach of contract and war and civil disturbance. Secondly, it provides technical assistance to developing countries so as to improve their ability to attract FDI. In fact both investors and host-countries can benefit from the promotional activities of the Agency.

The balance of interests is reflected in the preamble, where the objective of the promotion of investment to developing countries is formulated; "*under conditions consistent with their development needs, policies and objectives, on the basis of fair and stable standards for the treatment of foreign investment*". Flexibility is provided for, as the MIGA accepts that developing countries have the need to restrict and regulate foreign investment through laws and regulations. There is as such no obligation of NT or MFN treatment, and full state control is allowed.³⁴ Developing countries may screen investment and make performance requirements; in other words, they may discriminate.

There are obligations prescribed to foreign investors and host countries as the Agency will only guarantee "*eligible investment*".

Before insuring an investment, the Agency shall determine (article 12.d):

- The economic soundness of the investment and its contribution to the development of the host country.
- Compliance of the investment with the host-country's laws and regulations.
- Consistency of the investment with the declared development objectives and priorities of the "host"-country.
- The investment conditions in the host-country, including the availability of fair and equitable treatment and legal protection for the investment.

Figure 3. The eligible investment clause of the MIGA

³³ The agency is an autonomous institution, organisationally linked with the world bank. 155 Countries have signed the MIGA, of which 134 are full members.

³⁴ This is an investment control model.

In fact the whole structure of the treaty reflects the focus on developing countries and their need to attract investment from developed countries on a "discriminatory basis". Developing countries are the only eligible host-countries and the Agency will only conclude a contract of guarantee if the host-state approves that contract.

The Agency provides several avenues to settle disputes (articles 56-58, Annex II). If disputes cannot be settled amicably, states and the Agency (as surrogate of an affected investor) can take recourse to international arbitration. The parties of a dispute can choose whether to go to the ICSID of the World Bank or to UNCITRAL, the Commission on International Trade Law of the United Nations.

2.2.3 OECD Code on the Liberalisation of Capital Movements (1961).

The Organisation for Economic Co-operation and Development (OECD) is the successor to the Organisation for European Economic Co-operation and promotes sustainable development throughout the OECD area³⁵ on a non-discriminatory basis and while maintaining financial stability. When the OECD was established in 1961, the OECD Code on the liberalization of capital movements was also adopted. The OECD Code is of importance as it is a good example of how restrictions and distortions to capital movements can be removed progressively. OECD members are required to abolish any national restrictions upon transfers and transactions to which the code applies³⁶. The article on "general undertakings" however makes clear that the Code also takes into account the ability of member states to liberalize their capital flows. In this article there is an implicit recognition of the divergence in the levels of development between members through the principle of "*progressive liberalization*". The bottom-up structure of the treaty reflects this principle as members can determine in which sectors they desire to liberalize their investment through an opt-in procedure, resulting in positive lists in which rights of entry and establishment can be enjoyed³⁷. In the sectors to where members have no commitment to liberalize, national policy restrictions and regulations are still allowed, but can be subject to further liberalization in future negotiations. This gradual liberalization process gives members the opportunity to open up their markets selectively to foreign investment, in accordance with their individual needs.

Other elements of flexibility are provided for by a narrow transaction-based definition, insisting on investment control over the enterprise; and portfolio investments are therefore also included. The sectors listed in Annex A determine which transaction investment is included in the definition. The pre-entry MFN treatment therefore only concerns transactions and is not concerned with the protection of assets. Furthermore, there are several exceptions to the pre-entry MFN treatment, such as a general exception in case of public order, health and safety, a REIO clause³⁸, and an exception to non-discrimination in the case of a balance of payments crisis.³⁹

³⁵ Members to the OECD are: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Hungary, Iceland, Italy, Japan, Korea Republic, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom, USA.

³⁶ Karl P. Sauvant and Pedro Roffe (et al), *Most-Favoured-Nations Treatment* in: UNCTAD Series on issues in international investment agreements (New York and Geneva, 1999) 23,24.

³⁷ Karl P. Sauvant and Pedro Roffe (et al), *Admission and Establishment* in: UNCTAD Series on issues in international investment agreements (New York and Geneva, 1999) 16.

³⁸ Members of a regional economic integration organisation are exempted from the obligation to grant MFN to non-member states.

³⁹ *ibid.*

However, liberalizing efforts are subject to a standstill obligation, provided by article 1.e Part I of the treaty:

"members shall endeavor to avoid introducing any new exchange restrictions on the movements of capital or the use of non-resident owned funds and shall endeavor to avoid making existing regulations more restrictive".

Figure 4. Standstill obligation in the OECD Code on the Liberalisation of Capital Movements

The OECD Code on liberalization of capital movements does not have a dispute settlement mechanism. The drafters believed that peer pressure, political persuasion and compromise were the best solutions to resolve disputes in the field of capital control.⁴⁰ In case of a conflict, a member state can refer it to the OECD, which can offer suggestions. While the matter is under the review of the organization, the member can also enter into bilateral discussions on the matter with the other member concerned. Furthermore, the organization provides for a framework of notification, examination and consultation within a specialized Committee. The recommendations and decisions finally made by the OECD Council can be effectively monitored and asserts pressure on Member countries to liberalize their capital movements.

2.2.4 Energy Charter Treaty, ECT (1994)

The "final act of the European Energy Charter Conference" makes clear that the Energy Charter Treaty (ECT) aims to stimulate economic recovery in Eastern Europe and the former Union of Soviet Socialist Republics and also to promote cooperation between ECT members⁴¹ in the energy sector. As is the case with the OECD Code, there is no direct acknowledgment of the asymmetries in economies of the members of the Energy Charter Treaty. However, there is an implicit one by means of *progressive liberalization*. The centrally planned economies that are now in a period of transition towards a market-oriented one are therefore able to conform to the treaty provisions selectively.

The scope of the Energy Charter Treaty is however, in comparison to the OECD Code, narrowed down. The definition of investment is broad asset-based, and is limited to one sector, energy (and insists on investor control or ownership). The OECD Code covers more sectors, but is limited to transactions. On the other hand, the Energy Charter does go further in its objectives. The Energy Charter is a mixture of liberalization, promotion, regulation and protection aims, and this is reflected in the substantive provisions.

The Energy Charter narrows down the investment policy choices of host countries by conferring more obligations on the treatment of foreign investment. This is apparent first of all from the combination of NT and MFN, although the NT obligation does not apply to the "pre-entry" phase, but only to the post entry period. Furthermore member states are prohibited from using Performance Requirements and the text of the TRIMS agreement is quoted⁴². This prohibition is flexible in the sense that countries in transition are conferred temporal phasing provisions, so they have more time to adapt their policies and regulations to the Energy Treaty. The goal is prohibition however as soon as the transitional phase is concluded. It is therefore no surprise that a draft supplementary treaty provides for pre-entry NT as well.

⁴⁰ http://www.oecd.org/daf/cm/codes/oecd_exp.htm#3

⁴¹ As of 1998 the ECT has 50 member parties, of which 38 have ratified the treaty.

⁴² Energy Charter Treaty, Part II, article 5.

The investment policy choices of host countries are also narrowed down as the provisions on the protection of investment convey extensive, and legally binding, rights to investors. The provision on expropriation includes “measures having equivalent effect.” Enforcement of the treaty provisions is provided for by an investor-to-state dispute settlement mechanism (article 26-28). All parties have the right to choose the form of international arbitration that best suits their needs, namely UNCITRAL, the ICSID or the Stockholm Chamber of Commerce. The progress of members towards the fulfillment of the treaty obligations can also be monitored through “peer group” review.⁴³

While “host”-countries are faced with many obligations, the mode of implementation does convey some flexibility. The temporal phasing provisions concerning the implementation of the TRIMS have already been mentioned. Besides that there is a possibility to make a general exception on the basis of public order or to protect human, animal, plant life or health. There are promotional measures adopted to stimulate access and transfer of energy technology on a commercial and non-discriminatory basis. Also of importance is that the structure of the treaty provides flexibility, through the positive lists and the implicit distinction made between East European countries in transition and the market economy members.

2.2.5 World Trade Organisation: TRIPS, TRIMS & GATS (1994).

Although during the Uruguay Round (1986-1993) investment *per se* was not formally placed on the negotiating agenda, the Final Act contains a number of provisions dealing with issues relating to investment liberalization and even protection, namely the General Agreement on Services (GATS), the agreement on Trade Related Intellectual Property Rights (TRIPS) and the agreement on Trade Related Investment Measures (TRIMS). The agreements share many similarities even though they are very different. The agreements form an integral part of the Marrakech Accords establishing the WTO, are related to foreign trade, and share the same general aim, namely the reduction of distortions and impediments to international trade and investment flows. Enforcement of treaty obligations is provided for by means of the Dispute Settlement Understanding (DSU)⁴⁴, the extensive GATT/WTO dispute settlement mechanism which is only open to states.⁴⁵ The decision of the international arbitrator is final and binding.⁴⁶

Nevertheless, there are many differences between the treaties. Each treaty serves the general cause in a different way and in a different sector, and all three acknowledge the special needs of developing countries, although the degree of flexibility among the treaties varies substantially.

Trade-Related Investment Measures.

The TRIMS is the least flexible provision, as it prescribes host countries how to treat investment, without rendering them any “real” rights in return. Article III on the obligation of NT and article XI on the prohibition to use quantitative restrictions of GATT 1994 are further clarified by the TRIMS. In practice the TRIMS agreement aims to effectively eliminate certain national discriminative investment measures with respect to the trade in manufactured goods. There is a non-limitive illustrative list⁴⁷ of production and export requirements that are no longer permitted. Especially important are the prohibitions on local content and import quotas related to export volume. Member countries must

⁴³ <http://www.encharter.org/English-effective-35882>.

⁴⁴ Articles XXII & XXIII of the GATT 1994.

⁴⁵ The WTO-GATT dispute settlement has been strengthened by tightening the schedules for the settlement of the dispute process, the requirement for a unanimous vote to reverse a panel finding and the creation of a process of appeal.

⁴⁶ Not only is there a dispute settlement mechanism to guarantee enforcement of treaty obligations, each treaty provides it's own monitoring mechanism.

⁴⁷ Annex to the TRIMS Agreement.

notify all TRIMS they are applying which are not in conformity with the provisions of the Agreement, 90 days before the entry into force of the WTO Agreement. They must notify their TRIMS to the Council for Trade in Goods. The Committee on Trade-related Investment measures will monitor the operation and implementation of the Agreement and report the results to the Council.

The sharpening of investment regulation has not been welcomed by developing countries, as they use Performance Requirements to benefit as much as is possible from foreign investment, for example, to upgrade their economic and technological base by requiring local content. The preamble recognizes that the particular trade, development and financial needs of developing countries, especially of the least-developed countries (LDCs) should be taken into account.

In practice the effect is that developing countries can temporarily deviate from the prohibition to use Performance Requirements in the case of *balance of payments* problems. Secondly, these countries are permitted more time to conform to the TRIMS obligations by means of *transitional arrangements*. Developed countries must eliminate the TRIMS within two years, developing countries within five years and the least-developed countries within seven years after the entry into force of the WTO agreement. If a developing state or a LDC member has difficulty in implementing the provisions on time, it can request an extension of the transition period. The Council for Trade in Goods will determine if the extension will be accorded to the member in question, by analyzing the individual country's development, financial and trade needs. This right is apparently a conditional one.⁴⁸ The right to deviate from the prohibition of making use of Performance Requirements is however restricted by a "stand-still" requirement. When countries start implementing the TRIMS provisions during the transition period, there is no turning back, because notified TRIMS cannot be modified and new TRIMS cannot be introduced except if the aim is not to disadvantage established enterprises which are subject to a TRIM.

Trade-related intellectual property rights, TRIPS

The TRIPS Agreement contains no provisions which directly address the treatment of investment. However, it will create an environment conducive to investment by enhancing the protection of intellectual property rights. Intellectual property rights give the creator an exclusive right over the use of his or her creation for a certain period of time.⁴⁹ The aim to protect intellectual property rights is established in three ways; firstly through the provision of standards and principles of intellectual property rights; secondly by promoting their effective and adequate enforcement; and thirdly by means of a dispute settlement mechanism. The areas of intellectual property rights covered by the treaty are mentioned in the treaty⁵⁰. The protection of intellectual property rights is subject to post-entry NT and MFN. There are limited exceptions to these obligations, such as a general exception, namely in case of security interests and a subject-specific exceptions such as the Bern and Rome Conventions⁵¹. Enforcement of intellectual property rights is guaranteed by means of the obligation that member countries must make enforcement procedures (that are specified in Part III of the Treaty) available under their own law and permit effective remedies against infringement of the agreement. Dispute prevention is provided for by a transparency obligation, under which is understood that member

⁴⁸ A country must notify beforehand which TRIMS will prevail, but only TRIMS that existed 180 days before the date of entry into force of the WTO agreement can benefit from the transitional provisions.

⁴⁹ <http://www.wto.org/wto/intellect/intell1.htm>

⁵⁰ Part II TRIPS: Copyrights and related Rights, Trademarks, Geographical Indications, Industrial Designs, Patents, Layout-Designs (Topographies) of Integrated Circuits, Protection of undisclosed Information, Control of Anti-competitive Practices in Contractual Licenses.

⁵¹ These international conventions deal with the protection of intellectual property rights and allow the parties to deviate from the MFN standard with regard to the acquisition and contents of copyrights.

countries to the TRIPS Agreement have to make their laws and regulations⁵² publicly available and have to notify them to the Council for the TRIPS that monitors the operation of the Agreement. As was mentioned above, in case of a dispute, parties can take recourse to the DSU of the WTO.

Developing countries were not content with the TRIPS Agreement. To them the treaty went to far and they feared that access to technology, so important for their development, would become even more problematic. Moreover, the TRIPS agreement is heavily unbalanced since there is no protection of 'informal' innovations (for example traditional farmers). Since the vast majority of formal research takes place in the developed countries it is possible that newly created products will not be suitable for conditions in the South. It could for example prevent the local production of generic drugs which are relatively cheap.

The unbalanced approach of the TRIPS (apparent in the substantive provisions) might be an explanation as to why it is flexible in the principles and objectives, structure and mode of implementation. It not only recognizes in the preamble that the needs of the least developed countries must be taken into account, countries also have flexibility with regard to national laws and regulations needed to create a sound and viable technological base. Furthermore, member countries are free in the way they wish to implement the TRIPS provisions and they are also permitted to take measures to protect public health and nutrition, and to promote the public interest⁵³ as long as these measures are consistent with the provisions of the agreement. Article 7 (Part I) on "objectives" also states that the TRIPS agreement should contribute to the promotion of technological innovation and the transfer of technology.

The needs of developing countries are also taken into account via the mode of implementation of the treaty. This is done firstly by means of *transitional arrangements*, where developing countries and countries in transition can benefit from a period of delay of four years, before the treaty provisions must be applied. The delay can be extended to developing countries for another five years if patent protection of products is difficult. The extent of policy discretion of members making use of the transitional arrangements is limited by a "stand-still" requirement: "Changes in laws, regulations and practice made during the transition period may not result in a lesser degree of consistency with the provisions of the agreement."

Secondly, there is a special provision for the LDCs which allow for a transitional period of ten years, although countries are required to apply the NT and MFN provisions. Upon a duly motivated request the Council of TRIPS may allow an extension. This is therefore a conditional right. *Technology transfer* to these countries is to be encouraged by developed countries. This, however this is merely a "best effort commitment".

Thirdly, Article 67 provides that *technical and financial cooperation* in favor of developing countries and LDCs will be provided by developed country members. This however, is only on "request and mutually agreed terms and conditions". The cooperation can take the form of, for instance, the training of personnel or the development of laws and regulations.

Through the transfer of technology and cooperation provisions, the TRIPS agreement addresses the fear of developing members that they may be shut out of the process of technological development. However, the preferential treatment is not always a actual right, but often conditional, too abstract or dependent on the willingness of developed countries to support these rights.

⁵² Art 63, Part V. paragraph 1. These are laws, regulations that are made effective by a Member pertaining to the subject matter of the TRIPS Agreement (the availability, scope, acquisition, enforcement and prevention of abuse of intellectual property rights).

⁵³ TRIPS Agreement, Part I, article 8.

General Agreement on the Trade in Services.

The GATS is the most flexible of the three agreements in the WTO related to investment. The preamble addresses the special needs of developing countries in three ways. First of all, member countries have *"the right to regulate"* and introduce *"new regulations"*. Secondly, it aims to *promote and progressively liberalize investment* in the trade of services. Thirdly, *the participation of developing countries in the trade of services will be facilitated* by strengthening their domestic services, efficiency and competitiveness. The needs of the LDCs in particular will be taken into account.

"The right to regulate and introduce new regulations"

Although the scope of the treaty is quite extensive as it covers all services (except for government procurement)⁵⁴ and the principle of non-discrimination is provided for by both NT and MFN, elements of flexibility can be found throughout the substantive provisions, implementation mode and structure of the treaty. The scope of the GATS is limited in several ways and there are many exceptions allowed to MFN and NT.⁵⁵ Policy discretion is permitted and this means that countries can make use of Performance Requirements in the service sector. Upon implementing the GATS provisions, states can deviate temporarily from their obligations in the case of a Balance of Payments crisis. And the list of general exceptions is extensive. As long as it is not a disguised restriction, governments can make a general exception in order to protect public order, health, safety, national security, human, animal or plant life, the privacy of individuals and to prevent deceptive and fraudulent practices. There is also a subject-specific exception to MFN by means of a REIO clause.

"Progressive liberalization"

As the GATS provides for progressive liberalization, governments can choose the services in which they make market access and national treatment available. Five years after the entry of force of the agreement, member countries are required to enter into successive rounds of negotiations. Appropriate flexibility will be provided for developing countries during the process of liberalization.

Not only does the GATS have a positive list, there is also a negative list provided for in an annex. The structure of the GATS is hybrid. In these lists exemptions to the obligation of MFN upon entry of the agreement are notified. This means that countries can give more favorable treatment to certain countries. An exemption to MFN can last, in principle, only for 10 years and will be subject to negotiations in future rounds of negotiation.

GATS members may modify or withdraw any commitment to their liberalization schedules, but the modification must be notified to the Council for Trade in Services, which will monitor these modifications. The modifying member must also enter into negotiations to reach an agreement on compensation (on a MFN basis). If no agreement has been reached, an affected party can request international arbitration.

"Facilitation of participation of developing countries"

An important issue is the fact that flexibility is conferred to developing countries and in particular to the LDCs by means of promotional measures. The ways to increase the participation of developing countries is described in more detail in article IV. First of all, specific commitments will be negotiated, to, for example, stimulate access to technology on a commercial basis. Secondly, the developed

⁵⁴ GATS, Part II, article XIII

⁵⁵ Governments can limit the degree of market access and National Treatment they provide.

countries will establish contact points within two years to facilitate the access of service suppliers in developing countries to information. When implementing these provisions priority will be given to the special needs of LDCs. Article (XXV) on technical cooperation determines that developing countries can gain access to technical assistance through the above described contact points. But technical assistance will be decided upon by the Council for Trade.

2.2.6 NAFTA (1992)

The free trade agreement between Canada, Mexico and the United States of America aims to promote regional economic integration in North America. Chapter 11 of the NAFTA deals with investment in detail as to ensure a predictable commercial framework and increase the investment opportunities in the region. NAFTA however does not acknowledge the different levels and pace of development between its members, although especially the economies of the United States and Mexico are characterized by a sharp asymmetry. There is a reference to promote sustainable development, but the objective is not further specified and remains rather vague.

In many ways the investment chapter of the NAFTA agreement shows similarities to the MAI. The main features are very much alike and this is not very surprising as the NAFTA treaty served as an example for the MAI drafters. The controversial issues of the MAI can all be traced back to the NAFTA; the broad asset-based definition of investment with the inclusion of portfolio investment, the obligation of full MFN and NT treatment to the pre- and post-entry phase, the prohibition of performance requirements, that go far beyond the TRIMS obligations⁵⁶, the inclusion of the debatable phrase "measures tantamount to expropriation" inserted in the provision on expropriation and compensation, the investor-to-state dispute mechanism, the standstill and rollback clauses and finally the top-down structure of the treaty.

There nevertheless are some important differences between the NAFTA and MAI treaties. The main difference is that the former covers far more than only investment (also trade) and is regional and not multilateral in scope. Furthermore, it allows for fewer general exceptions as only national security is deemed an appropriate basis for an exception. Some flexibility elements have been included. The difference in the level of development between Mexico and the other two countries is implicitly acknowledged as Mexico has been given, by way of temporal phasing provisions, ten years to open up its market to investment in certain sectors. The structure of the treaty is hybrid as the negative lists are subject to an 'opt-in' clause with respect to sectoral liberalization at a future date (a positive list).⁵⁷

2.3 Conclusion

The flexibility of international investment agreements was the starting point of this report. IIAs need to be flexible so that developing countries can pursue their own development policies. It should be apparent that the treaties reviewed have unique characters and serve the interests of (developing) countries and business in a very different manner. The differences between the agreements in the degree of flexibility can be explained mainly by the divergence in objectives (liberalization, regulation, promotion, protection or a mixture of these objectives). For example, a treaty like the MIGA is specifically concerned with the promotion of investment to developing countries and shows a high degree of flexibility, reflected by the "eligible investment" clause. On the other hand, a treaty like the TRIMS that aims to sharpen investment regulation, shows far less flexibility. It prescribes countries

⁵⁶ NAFTA, article 1106. There is a long list of prohibited Performance Requirements, namely; export percentages, domestic content percentages, domestic purchase requirements or preferences, relationships between imports and exports or foreign earnings, technology transfer requirements, or exclusive supplier arrangements.

⁵⁷ Other important differences related to labor and the environment will be further discussed in Chapter IV, were the Labor Side Agreement will be examined.

how to treat investment by prohibiting Performance Requirements, and only allows developing countries more time to conform to obligations that often do not desire. Though the IIAs examined differ from each other substantially, important elements of (in)flexibility can be discerned.

“less flexible treaties”

IIAs that are less flexible share the following elements:

- They focus on the objectives of liberalization, protection and/or regulation and are addressed at states.
- National investment policy is regulated by high standards of treatment of investment.
- Standards are legally binding through an investor-to-state dispute mechanism.
- The tools to guarantee non-discriminatory treatment and the free flow of international investments are provided for by the core principles of freedom of entry, NT, MFN and investment protection.
- They are usually extensive in their scope, by means of a broad asset-based definition of investments, sometimes even including portfolio investments.
- In general, they only confer a minimum amount of flexibility in their implementation mode, which means only a general exception in the case of national security and a temporal derogation in case of a balance of payments crisis.
- They do not confer any promotional measures.
- The architecture of treaties does not reflect a formal acknowledgment of the asymmetrical economic relations between the member states.
- they are usually characterized by a top-down structure in combination with standstill and rollback obligations that lock a country into a rigid liberalization scheme. Because of the long duration of the contract, it is difficult for signatories to withdraw.

“more flexible treaties”

The more flexible treaties share the following elements:

- They focus on the object of promotion of investments (to developing countries) next to the aim of liberalization, regulation or protection.
- Often refer to flexibility explicitly. National policies are permitted to correct the structural inequality between the member states.
- They acknowledge limited exceptions to MFN and NT, the right to regulate by Performance Requirements and allow selective liberalization and the right to discriminate⁵⁸.
- They are limited in their scope, by a transaction-based definition or a broad-asset based definition that is narrowed down, for instance to a specific sector or by state control.
- Extensive exceptions are provided to the core principles. This can result in a long list of general exceptions to protect human, animal or plant life as long as they are not disguised restrictions.
- Subject-specific exceptions like a REIO clause and clauses of temporal derogation are provided for.
- They confer promotional measures such as like technology transfer and technical and financial assistance, although these promotional provisions do not always confer real rights, but are often mere expectations. The formulation is then non-obligatory, vague or conditional.
- They specify the means to promote technical assistance and advice so countries can make use of promotional measures.
- In general they are characterized by a bottom-up structure which allows countries to liberalize selectively and gives more weight to the formal acknowledgment of asymmetry in development between the members.

"A continuum"

Every treaty has elements of flexibility and the distinction between the flexibility or inflexibility of a treaty is not always as clear-cut as it may appear in the lists above. Comparing treaties is a bit little comparing "apples and oranges", as every treaty is based on the different concerns of the parties involved in the negotiating process. The stated objectives and principles that determine the content, implementation and structure of the treaty, are in fact the legal result of the conflict of interests between business, states and civil society. Bearing this in mind the IIAs can be placed on a continuum varying from flexible to inflexible. The main determinant of (in)flexibility is the degree of "investor freedom"⁵⁹ towards "state freedom"⁶⁰.

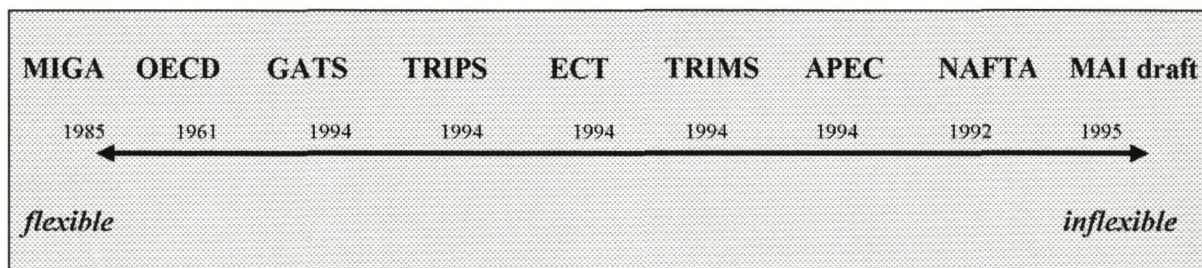


Figure 5. A continuum of regional and multilateral investment agreements

MIGA

The MIGA is the most flexible treaty. It is designed to promote FDI to developing countries (they are the only eligible host countries) and also assist them to attract FDI. Only eligible investment will be insured by the Agency, which means that investment must be made under conditions consistent with the needs, policies and objectives of developing countries. Developing countries therefore maintain full state control over their investment policy.

OECD Code of Liberalisation of Capital Movements

Even though developing countries are not member to the OECD Code of capital movements, it is a good example of flexibility. One should remember that the code was established in 1961 when there were big differences in the level of development and the openness of the economies of the OECD members. The scope of the treaty is limited to transactions (insisting on investor control) and the only objective is to liberalize capital movements. The core principles of non-discrimination are used in a flexible way, as the industrialized countries are permitted to liberalize their capital transactions progressively. The gradual liberalization of the past three decades has made it possible for the industrialized countries to selectively open up their markets to foreign investment in accordance with their individual needs.

GATS

The GATS typically shows many elements of flexibility. Its scope is limited to the service sector and it permits states to regulate (in comparison to the TRIMS, states may use Performance Requirements) and to introduce new regulations. Furthermore, the treaty provides for selective liberalization (so NT and MFN are flexible) and specifies the way in which investment towards developing countries should be promoted. But just as is the case with other WTO treaties, it is a question as to whether the flexibility really balances the acquired investor freedom. Developing countries are required to

⁵⁹ Leading to more restrictions of discriminative state policy.

⁶⁰ Leading to less freedom of investors.

liberalize a vulnerable sector that is not yet in a position to compete on a competitive basis with the service sectors of the industrialized countries.

TRIPS

The TRIPS agreement provides flexibility in many ways, with regard to policy discretion (members are free in the manner in which they implement the provisions) and there are many exceptions to the obligation of non-discrimination, such as promotional measures. The protection of Intellectual Property Rights however, is a very controversial issue and the level of investor protection in this area is quite high. This is due to the fact that conformity with respect to intellectual property rights standards is guaranteed by specified enforcement procedures (that have to be implemented under domestic law) in combination with the binding WTO state-to-state dispute settlement mechanisms.

TRIMS

This agreement restates existing GATT obligations and clarifies the NT obligation and the prohibition to use quantitative restrictions. It offers a short illustrative list of prohibited Performance Requirements⁶¹. Flexible elements of the treaty are provided by the very narrow scope of the treaty as it only covers manufactured goods and there are references to the special needs of developing countries and LDCs. In essence, however, the treaty provides more prohibition of national investment policies than flexibility. It locks developing countries into "unwanted" obligations without conferring developing countries actual substantive rights in return. This kind of acknowledgment of flexibility therefore does not really have a *de facto* relevance.

APEC

It is a bit tricky to place the APEC on the continuum as it has not yet evolved into a binding treaty. The treaty does already consist of elements that give an indication of the direction in which it will evolve. It provides for combined NT and MFN to the post-entry stage. At the moment the NT obligation is still very flexible because of the "investor behavior" clause. But it is questionable if this clause will be maintained. Already there is a "best effort commitment" to comply with the TRIMS and the future scenario will probably be that this commitment will become binding, leading to a pre-entry NT obligation accompanied by a top-down structure.

Energy Charter Treaty

The Energy Charter Treaty has many flexible elements, as it provides for many exceptions to the core principles of non-discrimination. The scope of the treaty is limited to the energy sector, which is to be progressively liberalized and promotional measures are provided for. However, state control over investment flows is being narrowed down by NT and MFN, that will soon also include pre-entry NT (when the supplementary agreement is adopted and the TRIMS obligations are fully implemented). The ECT also provides for a high level of investor protection because of the investor-to-state dispute settlement mechanism.⁶²

NAFTA

The NAFTA treaty is characterized by a strong neo-liberal vision. The inflexibility of the treaty is created by a very broad coverage of investment, the application of pre-and post entry NT and MFN supported by standstill and rollback clauses and a very extensive list of prohibited performance

⁶¹ See the Annex of the TRIMS.

⁶² This dispute settlement is not as extensive as the NAFTA Dispute settlement.

requirements, going far beyond the obligations under the TRIMS. Furthermore, investors are accredited a high level of protection, have access to an investor-to-state dispute settlement mechanism and the structure of the treaty has a top-down structure. The flexibility in the treaty is provided by Article 4 and the transitional arrangements for Mexico.

The MAI draft

Although the MAI negotiations have failed, it is important to place it on this continuum as it is a very good example of the trend towards IIAs focused on protection of investors rather than promotion of investment (or investor obligations). As has been stated previously, the MAI draft has many similarities with the NAFTA treaty. Even though the NAFTA treaty is in many ways more detailed and furthers extensive integration, one can conclude that the MAI is less flexible, because the geographical scope of the MAI treaty is so much broader. The MAI treaty was intended to be an open-standing treaty, so that not only the 29 OECD-members, but also non-OECD members could become party. A MAI treaty would therefore have had a broader impact than the NAFTA treaty.

3.1 Introduction

International legislation on investment is not only attractive at a regional or multilateral level but also, and especially, at the bilateral level. At the bilateral level the number of treaties has increased significantly in the 1990s; about three-quarters of the over 1300 treaties in existence at the end of 1997 date from the 1990s.⁶³ The widespread recognition of the benefits associated with foreign investment in both developed and developing countries has led to a world-wide liberalization of national policies and the noted proliferation of BITs.⁶⁴

Due to the reduced levels of foreign aid being dispensed and the broad recognition of the importance of FDI as a source of economic growth, developing countries feel an urgent need to attract and encourage FDI. The high speed at which developing countries have been negotiating new BITs shows the presumption that the protection of foreign investment encourages investment flows to their countries and that this in turn will contribute to their development. Different studies which have been conducted on the link between BITs and FDI flows shown that BITs appear to play a only a minor and secondary role in influencing FDI flows. Other determinants of FDI flows, especially the size of a host country's market, are more important. Although this might be true, developing countries do not want to endanger their attractiveness to foreign investors by not having BITs.

The need for FDI creates imbalance between the capital-importing country and the capital-exporting country. The need to attract FDI is of such high importance for developing countries that it makes their negotiating position rather weak. It will be difficult to demand flexibility in investment treaties if capital exporting countries are not willing to support it.

Ten BITs negotiated between The Netherlands and ten Sub-Saharan African (SSA) countries⁶⁵ between 1965 and 1997 were selected to study the different elements of flexibility and the effects of the imbalance between negotiating partners. The study on the contents of the BITs will show how far measures have been put in place to facilitate and promote growth and sustainable development. In this document we refer to these ten BITs when discussing the different elements of flexibility.

3.2 Objectives and Principles

A BIT is a treaty which imposes certain obligations on the contracting parties with respect to the treatment of foreign investment, and which creates dispute-resolution mechanisms to enforce those obligations⁶⁶. BITs are aimed at promoting FDI between the two countries. Most BITs are concluded between developed and developing countries.

The early BITs (until the 1970s) were part of agreements on economic and technical cooperation. The objectives were far more focused on promotion of investment than on protection. Taking as an example the BIT between The Netherlands and Ivory Coast of 1965, the contracting parties agreed to cooperate and to assist each other to promote development in their countries with a focus on economic and technical aspects.

⁶³ Karl P. Sauvant, *World Investment Report 1998*, 117.

⁶⁴ Thomas L. Brewer and Stephen Young, 'Investment Policies in Multilateral and Regional Agreements: a comparative analysis, *Transnational Corporations*, Vol.5 no. 1 (April 1996), 11.

⁶⁵ BITS exist between The Netherlands and; Ivory Coast 1965, Cameroon 1965, Uganda 1970, Tanzania 1970, Sudan 1970, Kenya 1970, Ghana 1989, Nigeria 1992, South Africa 1995 and Zimbabwe 1997.

⁶⁶ UNCTAD, *Bilateral Investment Treaties in the Mid-1990s* (New York and Geneva, 1998).

Recent BITs are considered treaties for the protection and promotion of investment, and this is often directly stated in the title. The strong emphasis on protection in the late BITs is reflected by the reference in the preamble to the desirability of fair and equitable treatment of investment. It is very unfortunate that the cooperation clauses have disappeared in later BITs. More recent treaties define the promotion of economic cooperation as a goal to be reached via the protection of investment and not as an instrument leading towards economic development.

A positive aspect in the Dutch BITs is that economic development is identified as one of the objectives of the treaties. Such recognition in the preamble helps to ensure that BITs are interpreted in ways that support growth and development or at least in ways that do not obstruct it.

3.3 Substantive Provisions

It is the actual contents of the BIT that should give effect to the development objective in the preamble. The preamble therefore discusses the definition of investment, the admission clause, Performance Requirements, relative standards as National Treatment and Most-Favored Nation standards, absolute standards, the expropriation clause, financial transfers and the dispute settlement mechanism. For the purpose of this study it is relevant to assess how far have these provisions cover the concerns of developing countries.

In the more recent BITs the definition of investment is broad and open-ended and covers all sectors. In some BITs (Uganda, Tanzania and Kenya) the scope of the definition is limited by state control as they define investment as investment that is made in accordance with the laws in the host country. In this way a country is able to ensure that only investment considered desirable from the point of view of its developmental goals are given protection. The scope of the definition is unlimited in the later BITs (from the late 1980s and onwards). Here we refer to the BITs concluded with Ghana, Nigeria, South Africa and Zimbabwe.

The process of globalization is exerting increasing pressure on host countries to grant market access to foreign investors on the basis of National Treatment. In Dutch BITs, NT and MFN do not apply to entry and establishment (as *is* the case with US BITs). They leave the matter of entry subject to national law. Admission clauses are amongst the most important from a developmental perspective. Entry conditions and restrictions are some of the ways through which developing countries can give expression to their development strategies.

To encourage the beneficial effects of FDI, countries have often sought to impose Performance Requirements (PRs) on foreign investors. Dutch BITs do not explicitly restrict PRs. In case of both contracting parties are a member of the WTO, provisions of PR are now subject to the TRIMS Agreement.

NT and MFN standards are important principles to foreign investors. Host governments however are not always very keen on granting NT as they will not be able to grant advantages to domestic industries. Governments have therefore sought for ways to limit its application. In a few of the BITs concluded in the 1970s (Uganda and Kenya) the application of NT is limited to certain areas; the payment of taxes, fees or charges, the free enjoyment of fiscal deductions and exemptions or with regard to the protection of industrial property. However, in general from the 1980s onward, NT is applicable to all investment without provisions that limits its application. It is only with respect to taxes, fees and charges and to fiscal deductions and exemptions that the Dutch model code and the BITs with South Africa and Zimbabwe contain a reference to investment 'in the same circumstances', mitigating some of the most sweeping effects of the standard.

It is interesting to see how the definition of NT has changed over the years. In the early BITs it is mostly defined as “equal to, and the same treatment as” that given to local investors. This implies that foreign investors cannot be favored over domestic industries. In later BITs, NT is defined as “not less favorable than”, which gives the home country the ability to favor foreign industries above home industries.

As with the NT standard, the application of the MFN standard has also been broadened through the years. The unconditional application of the standard has prevailed. This has important consequences because as virtually all BITs include an MFN provision, any form of favorable treatment given to foreign investors by a host country should be extended, in principle, to investors of every other country with which the host country has concluded a BIT containing a MFN clause.

When comparing the BITs in the field of *absolute standards*, the growing emphasis on protection of investment in the later BITs is obvious. The absolute standards stipulate the treatment that the host country must grant the investment once it has been established. In early BITs this standard was limited to ‘fair and non-discriminatory treatment’ and later on by the ban on ‘unjustified and discriminatory measures.’ Since the 1980s the BITs add explicitly ‘full protection and security’.

The *expropriation clause* has changed slightly over the years. In recent BITs, expropriation includes measures tantamount or equivalent to expropriation, which was not the case in the early BITs with Ivory Coast, Cameroon, Uganda, Tanzania and Sudan. In the 1970s, only the agreement with Kenya covered indirect expropriation.

On *compensation* the Dutch BITs do not use the international standards of “prompt, adequate and effective”. The standards used for compensation have been broadened and specified through the years, however. Initially it was “adequate, justified or fair”, but recent agreements refer to just compensation that represent the genuine value of the investment affected. The transfer should be made without undue delay, transferable and convertible.

The provisions on the *transfer of payments* are among the most important in a BIT. Home countries generally seek specific and broad guarantees. They look for a provision that guarantees to investors the right to transfer payments related to an investment into a freely convertible currency without delay at a specified exchange rate. The Dutch model code covers these provisions, as do the BITs with countries in SSA since the 1989 agreement with Ghana. For host countries the sudden repatriation of large profits or the proceeds from sale or liquidation can have an adverse effects on their Balance of Payments (BoP). Therefore a balance of payments exception in the event of a crisis should have been considered, but was not adopted in most of the BITs which were studied for this document. The exceptions are the BITs with Tanzania and Zimbabwe which will be discussed in the paragraph on implementation.

Another way (used in Dutch BITs) to address the BoP problem is by adopting the provision to guarantee transfer without *undue* delay or to be effected in reasonable installments. The word *undue* leaves room for interpretation which is important in case of a BoP crisis.

One last important item of the substantial provisions of BITs is the Dispute Settlement Mechanism which caused so much discussion in the MAI debate. In the early BITs with Ivory Coast, Cameroon, Tanzania and Sudan only a state-to-state dispute settlement mechanism existed. The investor-to-state mechanism is currently the rule.

3.4 Mode of Implementation

As preambles generally mention no explicit development objectives, it is difficult to find measures (such as temporal exceptions, derogations and promotional measures) which promote such objectives in BITs. Nevertheless, some BITs provide for protocols in which subject-specific exceptions and derogations from the obligations of the agreement are formulated. These are however not necessarily related to development.

An interesting derogation related to development is adopted in the BIT with Tanzania, where a provision is made for "the exception on the principle of free financial transfer when it is permitted by the IMF" (BoP clause). The BIT with Zimbabwe has included a protocol with a subject-specific exception on NT regarding land acquisition and a derogation on the free transfer of payments. This protocol (as is the case with the treaties with South Africa and Uganda) is an interesting example of a way to provide flexibility in the interest of a host country.

Almost all BITs cover MFN exceptions for REIOs (Regional Economic Integration Organizations) and double taxation treaties.

The promotional measures in Dutch BITs, as mentioned above, not extensively covered in treaties. In early BITs, one can find references to promote the holding of economic and commercial fairs and the establishment of mixed commissions to promote economic cooperation. There are however, no provisions to support the efforts to promote private investment in the host countries or to encourage the dissemination of information which is of such importance for developing countries.

The 'application in time' and the 'withdrawal clauses' are an example of how the BITs have moved become unbalanced treaties emphasizing the protection of investors. Although host countries are often reluctant to provide treaty protection to investments which were established prior to the entry into force of a treaty, in recent BITs, the roll back clause has generally been agreed to.

The same is the case with respect to the withdrawal clauses. The treaties concluded in the 1960s with Ivory Coast and Cameroon remained in force for one year; those in the 1970s with Uganda, Tanzania, Sudan and Kenya remained in force for five years; the BITs agreed to in the 1980s with Ghana and Nigeria remained in force for ten years; while those in the 1990s, with South Africa and Zimbabwe, will remain in force for fifteen years. The longer the BIT remains in force the more stable the legal environment is, which should obviously be attractive to foreign investors.

3.5 Overall Structure

The approach of a treaty towards development objectives also needs to be reflected in the overall structure of the treaty which reflects the relationship between the parties. Most importantly the asymmetry in economic development and in the availability of information and resources between the negotiating states needs to be addressed. Only then it is possible to respond properly to the concerns of developing countries. None of the BITs studied however make any distinction between the rights and obligations applicable to developed or developing countries.

Asymmetry in economic development and in the availability of information and resources between different negotiating parties causes asymmetry of power, which leads to a lack of balance between rights and obligations of investors. Obligations of investors in the field of social and environmental standards have not been addressed at all in the treaties studied.

3.6 Conclusion

The overview of the objectives and principles, substantive provisions, mode of implementation and overall structure of the ten selected BITs between the Netherlands and Sub-Saharan African countries has tried to show how, in thirty years time, the Bilateral Investment Agreements have grown more explicitly towards instruments which aim to protect foreign investment and leave the question of investors obligations unanswered. In addition, there are no references to any social or environmental standards or corporate responsibilities.

Over the years the definition of investment has been broadened and now covers all sectors. NT and MFN standards have unlimited application, absolute standards are specified towards full protection, expropriation extended towards indirect expropriation, and last but not least, the dispute settlement mechanism also covers a investor-to-state dispute settlement mechanism.

Under most BITs however, a host country maintains wide discretion to control the establishment of foreign investment in its territory via:

- ◆ The definition of investment used, and by using the qualification “in accordance with the law in the host country” which permits a country to refuse treaty protection to investment that it considers unworthy of such protection.
- ◆ Leaving the matter of entry and establishment subject to national law. Under the typical BIT, the host country has the sole discretion to decide whether investment shall be permitted in its territory. Entry into the host state is not subject to the NT/MFN.
- ◆ Not explicitly restricting performance requirements.

In this sense, BITs provide a degree of flexibility to enable host countries to pursue their development policies to a far greater extent than would have been possible under the MAI regulatory regime. A concerning matter however is the fact that US BITs already extend national treatment to the matter of entry and establishment. It appears that this will be a hot issue during the next WTO round of negotiations (in the event that it is put on the agenda). Judging from the experiences of the last thirty years, it can be expected that BITs will continue to develop in the direction of liberalization of investment and the promotion of the rights (and not obligations) of the investor.

The structure of BITs provides developing countries with certain opportunities to address specific development concerns by way of, for example, subject-specific and country-specific exceptions either within the treaty itself or in protocols. The question remains to be answered however as to whether developing countries are in a position to demand exceptions and elements of flexibility while simultaneously competing for foreign investment.

4.1 The need for international rules on Multinational Corporations.

The current situation with respect to international law in the field of investment policy shows that states are prepared to transfer some of their economic sovereignty in the field of international investment policy to strong intergovernmental bodies with legal enforcement mechanisms. This transfer of economic sovereignty is however, not accompanied by a transfer of social and environmental sovereignty. IIAs are also characterized by a one-sided approach. They mainly address the obligations of host-countries to treat FDI in a non-discriminatory way. Social and environmental responsibilities of TNCs, related to their investment made abroad, are usually left out. As TNCs cross borders to invest, they move beyond the supervision of states authorities and an accountability gap emerges. No global framework of rules and regulations yet exists to supervise TNCs and ensure proper and responsible investment practices.

In this rather anarchic state of affairs, developing countries become vulnerable to irresponsible TNC conduct. Because developing countries are faced with the obligation of non-discriminatory treatment of FDI, they have to give up some of their economic sovereignty, without receiving any veritable rights in return. The MAI for instance prohibits many Performance Requirements. These PRs can be very important tools for developing countries in ensuring that FDI serves the economic, social and environmental priorities of their national development policies. Their dependency on FDI aggravates the situation. Due to the fierce competition for FDI which exists, developing countries try to increase their competitive advantage by not enforcing or even lowering their labor and environmental standards. An "international race to the bottom" where standards are continually lowered to attract investors from developed countries would in the end be a no-win situation for developing countries, their citizens and the environment.

Because of the accountability gap, and the dependency of developing countries on FDI, it is of importance that the social and environmental responsibilities of TNCs, home and host countries are regulated in IIAs. For advocates of more regulation of corporate responsibility, it could be of interest to know the extent to which IIAs provide the means to protect labor and environmental concerns while finding a balance between the rights and obligations of foreign investors.

4.2 Labor and environmental concerns voiced in IIAs

Before the 1990s, not much can be said about the protection of labor and the environment in IIAs as they simply did not address the issue. They were characterized by a complete lack of a commitment to encourage sustainable development. Although BITs in general still do not mention environmental and labor concerns, there are some examples of regional and multilateral investment agreements that to some extent do deal with the issue of sustainable development.

"Objectives & principles"

The treaties such as the Energy Charter Treaty, NAFTA and the MAI do commit themselves to sustainable development. Both the NAFTA and the MAI explicitly mention "sustainable development" in their pre-ambular objectives. They do this in a general way in referring both to labor and environmental concerns.

The NAFTA parties commit themselves "to protect, enhance and enforce basic workers rights" and "to strengthen the development and enforcement of environmental laws and regulations". An important feature of the NAFTA is Article 104. This article states that environmental and conservation agreements prevail over NAFTA trade obligations in the event of an inconsistency.

In the preamble of the MAI, commitments to the Rio Declaration on Environment & Development and Agenda 21 are renewed. There are more references to labor concerns in the MAI than in the NAFTA agreement, such as commitments to agreements such as the Copenhagen Declaration of the World Summit on Social Development and to the observance of internationally recognized core labor standards. The treaty countries confirmed the International Labour Organisation as the appropriate institution to determine and deal with the core labor standards.

The Energy Charter Treaty does not mention sustainable development as an objective, but implicitly supports the objective in its reference to the "UN Framework Convention on Climate Change, the Convention on Long-Range Transboundary Air Pollution and its protocols (...)". Furthermore it is recognized that "there is an increasing need for measures to protect the environment, including the decommissioning of energy installations and waste disposal, and for internationally-agreed objectives and criteria for this purpose. However, as opposed to the MAI and the NAFTA, the Energy Charter Treaty does not address labor concerns.

"Substantive provisions"

The substantive provisions that are available to give effect to the objective of sustainability are very limited. The most important provision is the "not-lowering standards clause". This provision is meant to discourage countries from lowering their labor and environmental standards in order to attract FDI. This clause is found in several agreements, in various forms including diverging manners of enforcement.

First of all the APEC agreement, which does not mention any objective towards sustainability in its preamble, does have an article on investment incentives, stating that "member economies will not relax health, safety and environmental regulations as an incentive to encourage foreign investment". This "not-lowering standards clause" remains unclear on whether it concerns domestic or international regulations. Furthermore the APEC guidelines are unenforceable, so the effect of the clause is completely dependent on the willingness of the parties to abide by the provision.

The NAFTA treaty goes a step further as it recognizes that it is inappropriate to encourage investment by waiving, derogating from, or relaxing domestic health, safety and environmental measures. The treaty specifically mentions that this provision concerns domestic measures and there is no reference to international minimum standards. Furthermore, as is the case with the APEC agreement, labor measures are not included in the clause. Enforcement of the provision is however provided for. If one party considers that another has lowered its standards it may request consultations.

Finally, the MAI draft offers four alternative "not-lowering standards" clauses. The alternatives reflect the diverging views on how the objectives of protection of labor and environmental standards should be achieved. The four clauses represent four major important issues. It was first of all debated as to whether a clause should be included to deal with environmental standards only, or should also include labor standards and measures. There was widespread consensus that environmental measures should not be affected, but there was much opposition to the inclusion of labor standards. Secondly, there was a debate on whether the MAI draft should protect domestic standards and measures or international standards, such as ILO international core labor standards. Thirdly, the negotiators failed to agree on whether the clause should relate to specific investments, or be more general in nature. Finally, there was the issue of whether the clause should be legally binding, in other words subject to dispute settlement mechanism.⁶⁷

⁶⁷ <http://www.parliament.the-stationery-office.co.uk/pal/c199899/cmtrdind/112/112R05.htm>

Other provisions in IIAs that deal with the issue of sustainable development are hard to find. With the exception of Article 8 of the TRIPS agreement, the rest of the treaty is not concerned with labor or environmental issues.

Article 8 stipulates that:

Members, in formulating or amending their laws and regulations, may adopt measures necessary to protect public health and nutrition, and to promote the public interest in sectors of vital importance to their socio-economic and technological development, provided that such measures are consistent with the provisions of the agreement.

Figure 6, article 8 of the TRIPS Agreement.

“Mode of implementation”

The implementation mode of an IIA can convey references to the environment and labor, especially by means of general exceptions. For example, the Energy Charter allows general exceptions to protect human, animal, plant life or health. Treaties that do not take labor and environmental concerns into account as an integral part of the treaty can refer to the protection of human, animal or plant life in their general exceptions, as in the GATS agreement. However, these exceptions are only allowed if the measures taken are not a disguised restriction. Finally the MAI and NAFTA do not refer to labor or environmental concerns in their general exceptions, although they do allow for subject specific exceptions to the prohibition of certain performance requirements, like local content. National environmental measures necessary to protect human, animal, plant life or health, that do not constitute a disguised form of investment restriction, are allowed. –

“Other legal instruments that encourage protection of environmental and labor concerns”

There are examples of IIAs that have legal instruments that aim to promote international cooperation and encourage protection of environmental or labor concerns. The Energy Charter for example has a protocol on energy efficiency and related environmental aspects (1994) attached to it⁶⁸.

Monitoring of environmental or social policies can also be provided for. The World Bank Group for example, has been heavily criticized by environmental advocates for financing environmentally destructive projects. There has been a sequence of reforms to monitor the environmental policies of the World Bank and the implications of these policies for the projects. The MIGA now has its own environmental review procedure. The Environmental Assessment Policy provides policy and general principles that help to ensure that the MIGA will provide guarantees only to those projects that are environmentally sound and sustainable.⁶⁹ Beside the Environmental Assessment Policy, the MIGA board has also approved the proposal for a disclosure policy, which commits the MIGA to disclose information on the activities it carries out. The proposal for environmental and social review procedures has also been approved. The review procedures are meant to guarantee that the MIGA programs are carried out in an environmentally and socially sound manner.

Another example of an instrument that encourages protection of the environment and labor are the OECD Guidelines for Multinational Enterprises. These Guidelines are non-binding, but were proposed by the drafters of the MAI to be annexed to the MAI treaty as part of the three anchor approach. The OECD Guidelines are currently under review. They will most probably remain non-binding, but are

⁶⁸ <http://www.encharter.org/English/Secretariat/index.html#Anchor-Effective-35882>.

⁶⁹ <http://www.miga.org/disclose/envIRON.htm>.

proposed to be enhanced by means of peer pressure and political persuasion so TNCs will be encouraged to invest abroad in a responsible manner.⁷⁰

Finally, there is the NAFTA treaty, with its supplementary agreements on labor and environmental co-operation. It is the only treaty that directly links labor issues with international trade and investment. The NAFTA Labor Side Agreement (LSA) will now be examined as a case study to demonstrate how NGOs have furthered their interests to protect labor concerns and how labor cooperation between countries that are very diverse in their levels of development and labor legislation can be stimulated by means of adopting non-binding labor standards.

4.3 Protecting Labor through the Labor Side Agreement.

The NAFTA Labor Side Agreement (LSA) is a good illustration of how well NGO lobbying can lead to the adoption of sustainable development in international agreements. American NGOs feared that the far reaching liberalization program of the NAFTA would reinforce the competition between countries to attract FDI. It even had the potential to encourage member states to not enforce, or even to lower, labor and environmental standards to strengthen their competitive advantage. Without sufficient checks on corporate responsibility guaranteed in the investment agreements, TNCs would have a "blank check" to profit and exploit the lax regulatory investment climate. Labor and environmental standards therefore had to be incorporated in the agreements. The broad coalition of American NGOs opposed to NAFTA was so strong that the "side issues" began to overshadow the "central issues" and even endangered ratification of the treaty. Eventually two agreements, on labor cooperation and on environmental co-operation, were supplemented to the NAFTA treaty and ratified in 1994 by all three member countries.

The LSA is a good example of how a controversial issue such as labor protection can be dealt with amongst three countries at different levels of development and with diverse labor legislation.

When the negotiations on the LSA agreement started, it soon became clear it was a delicate subject, with the potential to infract on various issues of sovereignty. American labor unions proposed a supranational organization that would have the ability to impose and enforce common minimum standards. The member states however were not willing to give such extensive legislative, controlling and sanctioning powers to an independent organization. Mexico and Canada feared that a supranational organization would be dominated by American interests. Furthermore, due to the sharp economic, social and political asymmetries between the members, Mexico was afraid that it would have to carry the main burden of the expenses. In balancing these interests, the compromise eventually agreed to decided that effective enforcement of domestic labor law would be the most appropriate approach for the LSA. In addition, the member states would open up their "enforcement" regime to tri-national scrutiny.

In all three countries a National Administrative Office (NAO) was set up as part of the labor department. The dispute settlement is open to businesses, states, NGOs and private individuals. The interested party has to issue the complaint with the NAO of another member state. There are no common minimum standards, but eleven labor principles have been developed.⁷¹ These principles are subject to the national labor law of every member state. Every state has committed itself to stimulate the principles in the national judicial regime. The labor principles have a different status in the dispute settlement mechanism. There are three categories: "freedom of association and the protection of the

⁷⁰ Consultative meeting of the (Dutch) National contact point for Multinational Corporations, Ministry of Economic Affairs, The Hague 16 June 1999.

⁷¹ North American Agreement on Labor Cooperation between the government of the United States of America, the government of Canada and the government of the United Mexican States. Final draft September 13, 1993, Annex 1.

right of organization”, “the right to strike” and “the right to negotiate collectively”. These are the most fundamental labor principles, but they receive the least extensive treatment as they are sensitive national issues. The dispute settlement procedure consists of four stages. Firstly, one can issue a complaint and the NAO examines whether the complaint is within its’ jurisdiction. If the NAO determines it as a case of treaty infringement, and no solution has been achieved, the complaint goes on to the second stage where the NAO decides if ministerial consultation is needed. The first category of labor principles cannot continue beyond this stage, whereas the other labor principles can be accorded evaluation by a Committee of Experts and ministerial consultation in the third stage. Only complaints concerning the principles “prohibition of child labor”, “the right to a minimum wage” and of “security and health” can go on to the successive stage. Here a panel of arbiters takes a final decision and sanctions and fines can be imposed.

The NAFTA treaty has been severely criticized by American NGOs and Mexican unofficial labor unions⁷². As no common minimum standards have been formulated and the NAO lacks means of enforcement (especially for the first category of labor principles), the regime is “weak” and “toothless”. Changes in the labor situation of Mexican Maquilladora workers are not yet observable. Workers who have been dismissed for joining an unofficial union or for striking usually do not get their jobs back, even after a successful LSA appeal. The registration of unofficial labor unions is still frustrated by the state-dominating PRI party⁷³, the official labor union the CTM⁷⁴ and by TNCs, so these unions remain “illegal”. Taking into account that the effect of the LSA is marginal and that the NAFTA agreement gives a lot of freedom to investors, can one speak of a balance of interests, or is the LSA merely a “consolation prize”?

If one is looking for quick results, the LSA is bound to disappoint as one would quickly overlook the positive aspects of the LSA. In Mexico, the PRI and the CTM have structurally denied workers’ rights in the Maquilladora’s. Unofficial labor unions were unable to gain access to the political decision-making-process at the national or local levels. To actually effectuate an improvement in workers’ rights, the underlying regime, characterized by an authoritative, corporatist decision-making process⁷⁵, would have to be democratized. Workers need to get a voice in the Mexican policy-making process through labor unions which are currently “illegal” and therefore have no access to the formal political processes. By way of the LSA, these unions have for the first time achieved access to an international platform where they can voice their interests. The LSA has given these unions access to a dispute settlement procedure on a tri-national level where they can expose the poor labor conditions in the Maquilladora’s and put up for debate the legitimacy of the Mexican labor policy. The NAO-dispute settlement procedure is easily accessible as the NAO uses its mandate in a flexible way. Even though the LSA uses “soft” law to encourage compliance with the labor principles, the NAO does make a judgment and has to decide whom the “guilty” party is. This in effect means that the member states are under pressure to conform with the treaty obligations. Ministerial consultations can have the same effect. The political pressure has increased as the NAO procedure has brought more transparency to the workers’ situation, disputes get a lot of publicity, and international cooperation between labor unions is expanding⁷⁶.

⁷² Unofficial Unions are Unions that are not connected to a large labor confederation like the CTM, CROC, CROM which are connected to the state party, the PRI.

⁷³ PRI stands for Partido Revolucionario Institucional.

⁷⁴ CTM stands for Confederacion de Trabajadores de Mexico.

⁷⁵ Philippe Schmitter: a system of interest representation in which constituent units are organized into a limited number of singular, compulsory, non-competitive, hierarchically ordered and functionally differentiated categories, recognised or licensed (if not created) by the state and granted deliberate representational monopoly within their respective categories in exchange for observing certain controls on their selection of leaders and articulation of demands and supports. Maria Lorena Cook, Organising Dissent, Unions, the State and the democratic Teachers Movement in Mexico (1996 Pennsylvania), vii, 32.

⁷⁶ often American labour Unions file the complaints together with their Mexican counterparts

The LSA also features other positive aspects. For the first time a specific link has been made between investment liberalization and enforcement of domestic labor law. There has until now been no precedent in free trade agreement (other than the NAFTA) which makes the link with domestic labor law and has a dispute settlement accessible to NGOs. Furthermore, the inclusion of the eleven labor principles and especially the sensitive "category one" principles is far-reaching. In fact the LSA has developed common minimum standards, but then only in "principle". The whole procedure that has led to the adoption of the LSA illustrates how powerful non-governmental lobbies can be, and that they indeed can make a difference.

4.4 Conclusion

Due to the accountability gap which exists as TNCs move beyond governmental oversight, developing countries become vulnerable to irresponsible TNC conduct. That is why a need arises for international rules that ensure that TNCs invest abroad in a responsible way. To this day there is still a legal vacuum with respect to this aspect of international law. The vacuum reflects an unwillingness on the part of TNCs, host and home countries to regulate TNCs internationally. Important issues such as the responsibility for the social and environmental costs of FDI, and how the costs should be shared, remain unresolved.

Upon examination of the IIAs it becomes apparent that there is still a structural denial of social and environmental responsibilities of TNCs. The BITs especially exemplify a total lack of concerns for sustainable development. They provide for more regulation of the treatment of FDI by host countries and accord more protection to foreign investors. Crucially, the trend towards more regulation and protection of FDI in BITs is not accompanied by more regulation of TNC responsibilities.

Although most multilateral and regional investment agreements do not touch the subject of labor and environmental protection, there are examples of treaties that to some degree serve the purpose of sustainable development. Surprisingly, the least flexible agreements, namely the NAFTA and the MAI, give the most attention to sustainable development. This can be explained by the fact that as these treaties accord more legally binding rights to foreign investors, NGOs and unions put more political pressure on the negotiators to balance these rights with obligations. It becomes a political compromise on the order of "If you scratch my back, I'll scratch yours." In other words, if TNCs get more rights, labor and environmental rights should also be acknowledged.

Although both the MAI and NAFTA were not completely deaf to NGOs demands, we have seen that they are characterized by several weaknesses. First of all, the responsibility for sustainable growth is mainly placed with host countries. One of the most important, and in fact only, legally binding instrument found in the treaties to protect labor and the environment, is the not-lowering standards clause. This clause however is addressed at states and in particular concerns developing countries. The consequence will be that the countries with the least financial capacity will eventually end up being obliged to bear the costs of sustainable growth. This however, is not to say that host countries should take responsibility for the sustainable development of developing countries. The legally binding non-lowering standards clause is not accompanied, or balanced if you will, with similar legally binding responsibilities for TNCs.

The lack of legally binding instruments of enforcement, in particular of TNC responsibilities, becomes apparent in several cases. The MAI drafters for instance did propose to annex the OECD guidelines for Multinational Enterprises (MNEs). These guidelines are non-binding and depend entirely for their enforcement on peer pressure and the willingness of TNCs to comply.

The LSA is in many ways an important turning point. For the first time environmental and labor concerns were directly linked with investment liberalization in the NAFTA region and a dispute

settlement mechanism open to NGOs and workers was established. In reality, the LSA remains in the realm of soft law. The structural denial by the Mexican government of the right of Maquilladora workers to strike, to bargain collectively and the right to associate freely leaves the workers vulnerable and unprotected during the liberalization process. And still these rights are denied legal enforcement by the LSA. Enforcement remains dependent on the willingness of the NAFTA states to comply. Considering that NAFTA does accredit legal enforcement of investors' rights through the investor-to-state dispute settlement mechanism, it is doubtful whether the LSA provides sufficient means to protect workers rights against the negative effects of the liberalization process in the NAFTA region.

It can be concluded that to this day IIAs do not provide legally binding international standards to serve sustainable development. The only exception is the NAFTA not-lowering standards clause, that can force member states to refrain from lowering their domestic environmental or labor standards. But this clause only addresses domestic standards, not international ones. Furthermore the effect of the clause is limited in its scope to three countries. IIAs do provide some alternatives, for instance:

- ♦ the protocol on energy efficiency and related environmental aspects of the Energy Charter Treaty and the NAFTA Labor Side Agreements that stimulate cooperation in the field of labor and environmental protection
- ♦ the non-binding OECD Guidelines for MNEs, that set out a certain code of conduct for Transnational Corporations.
- ♦ the environmental assessment policy, disclosure policy and environmental and social review procedures of the MIGA. These programs commit the MIGA to assess the environmental implications of FDI and that the MIGA ensures beforehand to disclose information on the activities it carries out and to review its activities.

These alternatives however do not fill the accountability gap. The policy reviews and procedures of the MIGA are furthermore mainly aimed to ensure that the MIGA as an organization operates in a sound manner. The effectiveness of for example the protocols, the side agreements and the OECD Guidelines, remain dependent on peer pressure, political persuasion and the willingness to cooperate.

CONCLUSION

The purpose of this research was to examine various International Investment Agreements (IIAs) to determine the extent to which issues of sustainable development were taken into account. In doing so it is hoped that the formulation of a strategy for future IIA negotiations will be facilitated.

The research aimed to:

- Determine the extent to which IIAs serve the purpose of sustainable development.
- Discern the trend in international regulation of FDI; either in the direction of protection or in the direction of promotion and flexibility.
- Give an overview of existing International Investment Agreements (Bilateral, Regional and Multilateral) and their contents.

To what extent do IIAs serve the purpose of sustainable development?

This paper is based on the premise which defines sustainable development as; “development which meets the *needs* of the present without compromising the ability of future generations to meet their own *needs*”. In the IIAs examined, three different interest groups were distinguished; namely business, host countries and civil society. The conflict of interests between these groups revolves around two opposing views. One view supports the drive for deregulation of governmental restrictions on foreign investment, while the opposing view is that there is a need to regulate FDI so as to promote sustainable development. In answering the question as to whether IIAs serve the purpose of sustainability, as defined above, one must conclude that the needs of developing countries and civil society have been insufficiently represented. The IIAs have mainly focused on how host countries should treat FDI, emphasizing deregulation of state policy concerning FDI. Existing IIAs do not sufficiently serve sustainable development as there is no balance of interests between rights and obligations of investors and states. However, this general conclusion should not overshadow the fact that every treaty has a unique character and contains elements of sustainability. The degree of sustainability varies, is determined by the objective of the treaty, but is in the end the result of the unequal balance of power between business, states and civil society.

Trends in the international regulation of FDI

Important insights and trends in the political process of international regulation of FDI have been acquired in this report. For instance:

- There is first of all a *trend towards TNC rights and “host” governments’ obligations*.⁷⁷ The most recent international investment agreements are focused on more protection and regulation for investors, whereby restriction of states’ rights has increased.

⁷⁷ This trend has been underlined by Thomas L. Brewer and Stephen Young who state that “a clear shift in emphasis has occurred from one focusing upon *firms obligations and governments rights* to one emphasising *firms rights and governments obligations*. This is a reflection of changing attitudes and priorities at the host country level and the recognition of the beneficial contribution of international investment (...) But it can also be a reflection of the growing bargaining power of TNC’s. Thomas L. Brewer, *Investment policies, Transnational Corporations*, 16

- Secondly, *the increase of TNC rights and "host" governments obligations has led to less flexibility*, so that one may expect it to become more difficult for developing countries to pursue their own development policies.
- Thirdly, *TNC responsibilities and obligations are only briefly addressed in some regional and multilateral agreements*, and do not balance the increase of investor freedom..

"Increased rights for TNCs, more investor freedom"

During the 1990s, regional and multilateral investment agreements have been increasingly focused on regulation and protection of international investment. The effect of this has been that the freedom of national governments to determine the nature of international investment flows to their territories has been limited by international standards that aim to protect "investor freedom". The direction towards more regulation and protection in regional and multilateral agreements is specifically reflected by :

1. a broadening of the definition of investment, also covering portfolio investment
2. full MFN and NT, also covering the pre-entry phase of international investment
3. more restrictions on Performance Requirements
4. expropriation extended to "measures tantamount to expropriation"
5. legally binding standards of treatment by means of an investor-to-state dispute mechanism
6. fewer exceptions allowed to the agreed core principles of non-discriminatory treatment

The trend towards more "host" country obligations is well illustrated by the increase of regulation of Performance Requirements, starting with the short illustrative listing of the TRIMS⁷⁸, evolving into long illustrative listings of prohibited performance requirements in the NAFTA and the MAI.

The growing rights of investors can be discerned in the Dutch BITs examined as well. They have evolved more explicitly towards instruments which protect foreign investment. In comparison to the regional and multilateral agreements however, the Dutch BITs maintain wide discretion for host countries to control the establishment of foreign investment. Pre-entry NT is not provided for and the entry of investment remains subject to national law. They therefore do not explicitly restrict Performance Requirements. On the other hand, American BITs already require pre-entry NT.

"less flexibility"

The consequence of more "investor freedom" is that it will become harder for developing countries to pursue their own development policies. As the objectives of IIAs are more determined by the interest of TNCs to regulate "host" country investment measures and to protect their investment abroad, IIAs become less flexible.⁷⁹ Especially the NAFTA and MAI agreements which are addressed at "host" countries, impose obligations on how to treat investment, but provide very limited flexibility in return.

⁷⁸ The APEC has a "best effort commitment" to fulfill with the TRIMS agreement, and the Energy Charter Treaty has the obligation to comply with the TRIMS but does provide transitional arrangements.

⁷⁹ This can be explained by the fact that flexibility accumulates as more national discriminatory investment policy is permitted to correct the structural inequality between member states. The trend towards more "investor freedom" is totally opposed to discriminatory treatment of investment and therefore effectively limits the ability of states to determine their own investment policy as they acquire more freedom, or in other words "rights".

The decrease of state control in the area of international investment does not mean that these IIAs do not "claim or aim" to confer flexibility. There are several examples of recent treaties that refer to flexibility in an explicit manner. One should however be careful in this respect as the many references to flexibility, especially in the WTO agreements, can be misleading and hide political-economic realities. The WTO treaties cover very sensitive areas of investment. During the negotiations, developing countries did not want multilateral regulation of Performance Requirements, protection of intellectual property rights or liberalization of the service sector. However, the TRIMS, TRIPS and GATS were pushed through, conferring *de jure* preferential rights to developing countries. Upon close inspection of the treaty texts, the preferential rights conferred are not always *de facto* rights. They are often mere expectations, dependent on conditions or the willingness of states to comply, are temporary or far too vague. It is therefore very questionable if the flexibility of the treaties actually balances the increase in regulation and protection of international investment.

"corporate responsibility only briefly addressed"

At the moment, IIAs show a flexible view on labor and the environment. To this day, Dutch BITs do not address concerns of sustainable development at all. Labor and environmental concerns were not voiced in multilateral and regional investment agreements either, although there are some recent examples of references to sustainable development. These references remain brief and the instruments available to protect labor and environmental concerns are very limited and lack effective means of enforcement. The not-lowering standards clause is a provision that directly deals with the issue of relaxation of labor and environmental standards by countries in the effort to attract FDI. But as the APEC, the NAFTA and finally the MAI have shown, there are still many controversies, such as; "Should the provision include labor standards or not, should the standards be universal or only domestic and finally should the provision be legally binding?" Furthermore, this provision is mainly addressed to host countries and in particular developing countries. TNCs are not confronted with international legal obligations to invest abroad in a responsible way. There are however, some examples of treaties that have semi-legal instruments to enhance cooperation and protection in the field of labor and environment, such as the MIGA Environmental Assessment Policy, The Protocol on energy efficiency and related environmental aspects of the Energy Charter Treaty, The OECD Guidelines on MNEs and finally the NAFTA supplemental agreements on labor and environmental cooperation. These alternatives however do not fill the legal vacuum in IIAs concerning TNCs responsibilities towards sustainable development.

It is striking to see that the less flexible treaties, such as the NAFTA and the MAI address the concerns of civil societies most substantially. This can be explained by the fact that the trend towards more investor freedom can generate more opposition from civil society (especially "home" countries) as the stakes become higher. The NAFTA case study shows how NGOs have successfully confronted the increasing freedoms granted to foreign investors. The desire of civil society to protect labor against free trade in North America led to the supplemental agreements on labor and environmental cooperation. Although the Labor Side Agreement (LSA) has not yet led to improved working conditions and higher wages of Mexican Maquilladora workers, and it is questionable as to whether the LSA balances the increase of investor freedom with obligations, the LSA is a major breakthrough for several reasons. For the first time, a direct link was made between investment liberalization and domestic labor law. This allowed illegal Mexican labor unions to be acknowledged in the NAO dispute settlement and they have consequently gained a voice in the political process. Furthermore, the issue of "corporate responsibility" has become a higher priority on the political agenda and corporate conduct has become more transparent. Last but not least, international cooperation between the governments, NGOs and experts has increased. In comparison to the NAFTA, the MAI three anchor approach to protect labor and the environment is far weaker.

IAs: A sustainable balance of interests?

There remains no doubt as to the importance of FDI for sustainable development. The increasing flows of FDI exemplify the growing mobility of TNCs in moving across borders to find attractive locations to invest. As TNCs invest abroad, they move beyond national control and an accountability gap emerges. Investment issues therefore become global issues even though there is no international framework to supervise TNC activities. Meanwhile, states are under more pressure and are more willing to transfer a certain degree of their economic sovereignty to intergovernmental organizations. They are under pressure because of the strong bargaining power of TNCs and the fierce competition for FDI. Their willingness stems from the recognition of the possible beneficial contribution of international investment. In practice, the transfer of sovereign economic power entails that the ability of host countries to regulate TNC operations in their territory is limited by legally binding international standards of treatment for FDI. Meanwhile, the transfer of economic sovereign power is not accompanied by a similar transfer of social and environmental policy discretion, as national governments obviously desire to keep social and environmental policy in their own hands. Therefore the rights of international investors are acknowledged internationally, while social and environmental rights are still denied acknowledgment and have a lower status.

The consequence of this situation is that the needs of developing countries and civil society are insufficiently represented in IAs and that efforts at attaining sustainable development threaten to be compromised.

While developing countries are becoming more dependent on FDI for their development, it is becoming more difficult for them to benefit from FDI on their own terms. This is due to their dependency on FDI and the fierce competition which occurs between states to attract FDI which weakens their bargaining position towards TNCs and their home countries. The weak bargaining position is reflected in IAs as these treaties become less flexible. Developing countries are less able to regulate FDI to serve their own development needs. Current IAs in effect prohibit regulation of FDI by host countries, for instance by means of Performance Requirements. One gets the impression that developing countries are trapped in a downward spiral. As developing countries need FDI, they are under pressure to sign treaties that do not fit their specific development needs. They are often prepared not to enforce (and at times even lower) their labor and environmental standards to attract investment. This situation can obviously have consequences for achieving sustainable development practices. As developing countries focus on short term gains, there is a significant threat that "human and environmental capital" is lost in the long term.

It is therefore very important to strengthen the capacity of NGOs in developing countries to enable them to effectively lobby their governments on the importance of attracting FDI for sustainable long term economic development. There has been little public debate on international investment policies in developing countries. NGOs and donor organizations from the north, in supporting southern partners, should address this problem in their advocacy on sustainable IAs.

The lobby efforts of NGO against the NAFTA and the MAI treaties have shown that if public awareness of the salience of sustainable IAs increases, limited gains can be achieved. However, current international investment organizations remain intergovernmental and lack democratic checks and balances. NGOs usually do not have access to these organizations and negotiations on international investment regulation often lack transparency⁸⁰. It is therefore increasingly difficult for

⁸⁰ Consultative meeting of the (Dutch) National contact point for Multinational Corporations, Ministry of Economic Affairs, The Hague 16 June 1999.

Dialogue Meeting on investment, Brussels 28 April 1999, European Commission, DGI M-2.

NGO-meeting on Multilateral Investment Regulation, SOMO, The Hague 23 June 1999.

NGOs to promote their concerns, which are not only domestic in nature. This is especially the case as environmental issues become a global concern.

The MAI is a very good example of the trend that policy choices, whereby host countries in controlling, differentiating between, and benefiting from investment flows, are being determined increasingly by the interests of TNCs and their "home" countries. The main parties in the MAI negotiations were the governments of the developed countries which were extensively lobbied by TNCs. It is therefore not surprising that the interests of host governments and TNCs determined the objectives, content, implementation and architecture of the treaties.

The MAI however, can also be seen as a turning point in the practice of international investment negotiations, as its demise demonstrates that when the stakes are high, civil society can gain leverage as the legitimacy of government policy becomes vulnerable. Democratic countries are responsible for the well-being of their citizens and if their constituents are not content, governments stand to lose support and elections. It is therefore not surprising that the neo-liberal interests promoted by TNCs lost their momentum during the MAI negotiations. TNCs do have strong bargaining and lobbying power, but it is not limitless. Both internal disagreement between OECD countries, as well as the lobby efforts of civil society, led to the end of the MAI⁸¹. The MAI went too far, and as such it revealed the extent to which investor freedom is acceptable, but also when it has reached its limit.⁸² This aspect of the MAI should not be forgotten in future negotiations.

⁸¹ Ibid.

⁸² Not even in the NAFTA case, where the NAFTA was nearly pushed aside because of the strong NGO lobby, did the TNCs lose their bargaining position. The supplemental agreements were a gain for NGOs, but can also be seen as a mere consolation prize. They do not really balance "investor freedom" in the NAFTA, but were enough to stop NGO pressure from ending the NAFTA negotiations.

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ANNEX 1 CRITICS VIEW ON THE MAI DRAFT

	MAI (draft treaty 1998)	Critics views
A. Objectives		
Investments	Protection, regulation and liberalisation oriented.	Too much emphasis on how host states should treat foreign investments. The treaty should be more oriented towards regulation of TNC activities.
B. Substantive Provisions		
Definition investments	Broad definition : "every kind of asset", including portfolio.	The definition is too broad. Especially the inclusion of portfolio investment is controversial as the treaty provides no safeguards towards volatility risks.
Admission & establishment under national law	Combined NT & MFN model.	The MFN & NT treatment is extensive and inflexible. It grants more favorable treatment to TNCs but prohibits positive discrimination of local investors who already have a competitive disadvantage related to scale and scope as regards to TNCs.
Admission & establishment upon entry	Pre & Post entry.	Especially application of NT to the pre-entry stage is controversial as it reduces state's discretion to screen investments beforehand.
Performance Requirements	Long illustrative list of prohibited Performance Requirements, for instance on local content and transfer of technology.	The prohibition of Performance Requirements is more extensive than the TRIMS.
Protection of investment		
expropriation & compensation	Broad definition of expropriation including "measures tantamount to"	"Regulatory Takings" may be seen as the taking of foreign property.
transfers	To ensure free transfer of payments without delay in a freely convertible currency	No safeguards are provided for to protect a host state against capital volatility. Restrictions on transfers are prohibited.
existing and future investments	Rollback & Standstill	Commitments made may not be consistent with the needs of a country at every period of time.
Dispute settlement	State-to-state & investor-to-state	The high level of investment protection is not sufficiently balanced by corresponding obligations of investors towards sustainable development. The dispute settlement is not open to civil society.
C. Implementation		
General exceptions	National security & public order	No general exceptions are provided for that specifically address sustainable development. (except for environmental measures concerning Performance Requirements).
Clauses of derogation	Balance of Payments clause	There are no temporal phasing provisions or promotional measures.
Withdrawal	The treaty will continue to apply for 20 years	Countries will be locked in for too long.
D. Overall Structure		
Structure	Top down	Bottom up structure is more flexible
Distinction made in development level	No	No acknowledgment of structural differences between members.
E. Labor & Environment		
The three anchor approach	Preamble, not-lowering standards clause & annexing OECD Guidelines	This three anchor approach does not sufficiently balance the new rights of investors.

ANNEX 2 INTERNATIONAL INVESTMENT AGREEMENTS

OBJECTIVES AND PRINCIPLES

	Investments	Development	Environment	Labor
GATS 1994	Promotion, progressive liberalisation of investments in the trade of services.	Recognition of flexibility, (especially for LDCs) as regards to the content of national laws and regulations. Article IV specifies how to facilitate their participation in the trade of services.	No reference	No reference
TRIPS 1994	Protection of trade related intellectual property rights	Recognition of flexibility, same as GATS. Article 7 reference to the aim of technology transfer. Article 8 national measures permitted to protect the public health and promote the public interest (...)	No reference	No reference
TRIMS 1994	Regulation (Progressive Liberalisation) of trade-related investment measures	Recognition of the special development, trade and financial needs of developing members (especially LCD's), without reference to national law or regulations.	No reference	No reference
Energy Charter 1994	Progressive Liberalisation Protection Promotion	no direct acknowledgment	Reference to UN framework Convention on Climate Change, on Long-Range Transboundary Air Pollution and it's protocols (et al).	no reference
MIGA 1985	Promotion of investments in particular to developing countries	Promotion under conditions consistent with developing needs, policies and objectives on the basis of fair and stable standards for the treatment of foreign investment (further detailed in article 12 on eligible investments)	no reference	no reference
NAFTA 1992	Liberalisation Protection Regulation of investments in the North American economic integration.	Reference to sustainable development in general	Strengthen the development and enforcement of environmental laws and regulations. Trade obligations in environmental and conservation agreements prevail to the extent of the inconsistency, article 104.	Protect, enhance and enforce basic workers 'rights
OECD Code 1961	Progressive Liberalisation	no reference	no reference	no reference
APEC 1994 non-binding	Liberalisation	Acknowledgment of diversity in the level and pace of development of members. Flexibility as regards to their investment regimes	no reference	no reference

SUBSTANTIVE PROVISIONS

	Definition	Admission & Establishment	Performance Requirements	Not-lowering standards
GATS 1994	Broad asset based, limited to service sector & by an opt into sectoral commitments	Selective liberalisation Market access and NT has to be negotiated progressively per country	No prohibition, accepting the right of developing countries to regulate.	No reference
TRIPS 1994	Broad asset based, limited to intellectual property rights	Combined NT & MFN	no reference	No reference
TRIMS 1994	Broad asset based	Combined NT & MFN	Prohibition on local content and import quota's related to export volume (and other production & export requirements) as regard to goods (services are not included)	No reference
Energy Charter 1994	Broad asset based, limited to energy sector.	Combined NT & MFN restricted to post-entry (draft supplementary treaty also pre-entry)	Conform TRIMS, subject to temporal phasing derogations.	No reference
MIGA 1985	Broad asset based, limited by host country laws, development objectives and priorities.	Investment control, recognition of restrictions and regulations on the admission of FDI	No prohibition	No reference
NAFTA 1992	Broad asset based. Inclusion of portfolio, limited by negative list	Hybrid model: Combined NT & MFN and selective liberalisation, pre and post entry	Prohibition local content, export requirements & transfer of technology as regards to all investments. There are exceptions.	Recognition that it is inappropriate to encourage investments by waiving /derogating from or relaxing <u>domestic</u> health, safety and environmental measures. If one party considers that another has done so, it may request consultations.
OECD Code 1961	Transaction based, narrow insisting on investment control over the enterprise	Hybrid model: Selective liberalisation & mutual NT non-discrimination. Pre-entry MFN, NT implicitly	Annex A	
APEC 1994 "best efforts commitment"	No definition	Combined NT & MFN treatment: but NT is subject to domestic law exceptions (investor behavior), pre and post entry	No prohibition, but in the preamble their is an acknowledgment of the importance of fully implementing the TRIMS agreement	Member countries will not relax health, safety and environmental regulations as an incentive to encourage foreign investments.

SUBSTANTIVE PROVISIONS (CONTINUED)

	General Treatment	Expropriation & Compensation	Protection from Strife	Transfers	Dispute settlement
GATS 1994	Transparency	No reference	No reference	No restrictions allowed except for BoP in conformance with IMF provisions	Recourse to the DSU, the binding dispute settlement procedure of the WTO. State to state
TRIPS 1994	Fair & equitable procedures	no reference	no reference	no reference	Recourse to DSU
TRIMS 1994	Transparency	no reference	no reference	no reference	Recourse to DSU
Energy Charter 1994	Fair, equitable, favorable & transparent conditions. Most constant protection & security.	No expropriation or measures having equivalent effect, except in the public interest, on a non-discriminatory basis, under due process of law and against prompt, adequate and effective compensation at fair market value.	Compensation for loss owing to war or other armed conflict, state of national emergency, civil disturbance or other similar event.	Ensure free transfer of payments without delay in a freely convertible currency	Recourse to ICSID, investor to state
MIGA 1985	Fair & equitable treatment	The MIGA guarantees <u>eligible investments</u> against a loss resulting from the following risks: 1. currency transfer 2. expropriation and similar measures 3. breach of contract 4. war & civil disturbance			
NAFTA 1992	Fair, equitable, full protection and security.	Includes measures tantamount to expropriation. Expropriation not allowed except for public purpose, on a non-discriminatory basis, under due process of law. Compensation before expropriation took place at a fair market value and without delay.	In the case of losses suffered as a result of armed conflict or civil strife, each Party shall provide compensation on a non-discriminatory basis.	Freely and without delay prohibition of forced repatriation. Exceptions: e.g. BoP	State-state and investor to state
OECD Code 1961					None, system of peer pressure
APEC 1994 non-binding	Transparency obligation	No expropriation or measures with a similar effect allowed, except for a public purpose & on a non-discriminatory basis, prompt, adequate & effective compensation	No reference	Further Liberalisation towards free and prompt transfer of funds, in freely convertible currency.	None, refers to consultation, negotiation or arbitration without specifying any mechanism.

MODE OF IMPLEMENTATION

	General Exceptions	Clauses of Derogation	Subject Specific exceptions	Promotional measures	Withdrawal
GATS 1994	Public order, health, morals, safety, national security, protection of human, animal or plant life (i & ii) as long as it is not a disguised restriction	Balance of Payments (BoP)	Article V economic integration	Technical assistance to developing countries. Article IV specifies how to facilitate their participation in the trade of services.	
TRIPS 1994	Security, art. 8	Temporal phasing provisions for LDCs, developing countries and countries with central planned economy in the process of transition.	MFN limited by Bern & Rome convention	Technical & financial co-operation to LDCs and developing countries. Encouragement of technology transfer to LDCs.	
TRIMS 1994	No reference	Developing countries may deviate temporarily in case of BoP. Transitional arrangements, with an extension for developing countries which demonstrate particular difficulties.	No reference	No reference	
Energy Charter 1994	Protection of human, animal or plant life or health. Public order, security interests.	Temporal phasing provisions as regards to TRIMS. Transitional arrangements	REIO clause Exception to MFN as regards to intellectual property rights	To promote access to and transfer of energy technology on a commercial and non-discriminatory	
MIGA 1985	No reference	No reference	No reference	Technical assistance and advice	After the expiration of 3 years after entry of force of the agreement, withdrawal is possible at any time and is effective 90 days after notification
NAFTA 1992	National security, not related to development	BoP clause Temporal phasing provisions for Mexico (10 years to open up market to investments) All non-conforming federal measures of Canada and the USA are grandfathered.		No reference	Six months after notification.
OECD Code 1961	Public order, health, morals, safety and security interests	Temporal derogation if the economic & financial situation justifies such a course. BoP clause	REIO clause	No reference	Effective within 12 months from the date of notice received
APEC 1994 non-binding	No reference	No reference	No reference	No reference	

OVERALL STRUCTURE

	Top Down	Bottom Up	Distinction made in development level	Stand still & roll back
GATS 1994	Opt into positive lists	negative list for limitations on market access and NT, public procurement	Distinction between developed, developing and LCDs reflected in treaty	stand still
TRIP's 1994	No reference	No reference	ibid. & countries with a centrally planned economy in the process of transition	stand still
TRIM's 1994	No reference	No reference	ibid.	stand still
Energy Charter 1994	Opt into positive lists	no reference	Implicitly between East European countries with an economy in transition and other members with market economy.	no reference
MIGA 1985	No reference	No reference	Based on distinction between developed and developing	No reference
NAFTA 1992	negative listing	negative list subject to op into sectoral liberalisation at a future date	Implicit distinction between development of Mexico, Canada & USA.	Stand still & roll back
OECD Code 1961	Opt into positive list	No reference	Implicitly, through progressive liberalisation	stand still & roll back
APEC 1994 non-binding	No reference	No reference	No reference	No reference

PROTOCOLS ON LABOUR AND ENVIRONMENT

	Principles	Dispute Settlement	Substantive provisions
NAFTA 1993 supplementary agreement on labor co-operation	11 principles	national administrative office	
NAFTA 1993 supplementary agreement on environmental co-operation			Environmental measures allowed on NT basis.
Energy Charter 1994 Protocol on energy efficiency & related environmental aspects (1998)	article 19. "The polluter pays"		Sovereignty over exploration & development of it's energy resources and to regulate the environmental and safety aspects of such exploration and exploitation.
MIGA 1985 Draft Environmental Assessment Policy			

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